



Aseem Goswami

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A Comparative Study

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Chapter: 1.Introduction

“Sometimes the difference between the clear, standard case or paradigm for the use of an expression and the questionable case is only a matter of degree. A man with a shining smooth pate is clearly bald ; another with a luxuriant mop clearly is not ; but the question whether a third man , with a fringe of hair here and there , is bald might be indefinitely disputed , it if were thought worthwhile or any practical issue turned on it...Sometimes the deviation from the standard case is not a mere matter of degree but arise when the standard case is in fact a complex of normally concomitant but distinct elements , some or one of which may be lacking in the cases open to challenge. Is the flying boat a ‘vessel’? Is it still ‘chess’ if the game is played without a queen? Such questions may be instructive as they force us to reflect on, and make explicit, our conception of the composition of the standard case...”¹

-Professor H.L.A. Hart

The legal quandary expressed above in the precise words applies to the concept of Limited Liability Partnerships (hereinafter called LLP), new commercial vehicle floated to address the vacuum that existed between partnership law and company law. LLP is a marriage of principles of company law and partnership law in order to address the deficiencies in both the areas for small scale business and professional firms. The present project attempts a deeper understanding of the basic concepts underlying LLP and the way in which company and partnership has been fused to produce this new entity.

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. It is felt opportune that entrepreneurship, knowledge and risk capital combine to provide a further

¹ H.L.A. HART , THE CONCEPT OF LAW 4 (2nd ed. , 2005)

impetus to India's economic growth. In this background, a need has been 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. The Limited Liability Partnership (LLP) is viewed as an alternative corporate business vehicle that provides the benefits of limited liability but allows its partners 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 formation of companies with limited liability led to introduction of "limited liability" concept in partnership law. A limited partnership (LP) consists of one or more general partners liable for all the debts and obligations of the firm and who alone are entitled to manage the firm's affairs, and one or more limited partners whose liability for the debts and obligations of the firm is limited in amount but who are excluded from all management functions.² In contrast, an LLP combines multiple features of a company with a partnership and enables partners who are actively involved in the business of their partnership to limit their liability for the partnership's debts and obligations. A limited partnership is still a partnership with a slight modification and the concept is not very new.

² J.J. Henning, *Partnership Law Review: The Joint Consultation Papers and the Limited Liability Partnership Act in Brief Historical and Comparative Perspective*, Comp. Law. 2004, 25(6), 163-170, p. 168 [the concept of limited partnerships and limited liability partnership has its historical roots in the French *partnerships en commandite* or the Italian *commenda* of the Middle Ages which was in substance an arrangement by which an investor entrusted capital to a trader for employment in mercantile enterprises on the understanding that the investor, while not in name a party to the enterprise and though entitled to a share of the profits, would not be liable for losses beyond the amount of his investment]

Formation of Limited Liability Partnerships in India is a sequel to the recommendations of the Naresh Chandra Committee (2003) and Irani Committee (2005) as a new form of business entity. The LLP concept was initiated in the US in 1991 as an alternative to the partnership mode. This form of organization permits individual partners to be insulated from joint liability of any partner's business decision. Thus an LLP enters into a contract in its name but the liability of its members is limited to their shareholdings. An LLP is a hybrid between a company and a partnership firm. The LLP is a separate legal entity with unlimited capacity where no partner is liable for the unauthorized action of the other partners, and whose liability is restricted to his own stake in the LLP.

The Naresh Chandra Committee had observed that the Indian professionals are now increasingly transacting with or representing multi-nationals in international deals and are therefore exposed to severe liability. Thus to alleviate their apprehension of excessive potential liability, LLP is an imperative necessity. Failure to do so will deprive India of its rightful place in the international community.

Every partner would be an agent of the LLP but the LLP would not be bound by anything done by a partner in dealing with a person if

- (a) The member in fact had no authority to act for the LLP
- (b) The person knows that he has no authority or does not know or believe him to be a partner of the LLP.

Although the UK LLP Law originally intended to confine the LLPs to professionals only analogous to the recommendations of the Naresh Chandra Committee, the UK LLP Act of 2000 extended it to every trade of business as in India. USA however continues to restrict it to professionals only.

In US the LLP concept took birth in the nineties when only two States allowed LLPs. Over forty States adopted LLP legislation by the time LLPs were added to the Unified Partnership

Act in 1996; every State in the USA has its own LLP. Since then other countries such as Singapore, Australia, China and Japan have adopted the LLP model. It is praiseworthy that India has at last joined this league.

1.1 Research Methodology

1.1.1 Object of Study

It is now well accepted that the concept of Limited Liability represents a dynamic concept, which will find expanded expression and instantly cover new areas as human society continuous to evolve a higher levels of development and organisation. The principle objective of this research work is to make critical study of the concept of Limited Liability Partnership Act in India with a view to identify the areas of potential conflicts in the working of this new piece of legislation. The other objectives formulated for the purpose of the research work are:

- > To explore the historical background of Limited Liability,
- > To examine the justification for the LLP Act,2008,
- > To evaluate the functioning of the LLP's,
- > To review the experience of earlier forms of Business Organisations, and
- > To draw the inferences from the study towards possible improvements in the new Act of Limited Liability in India.

1.1.2.'Scope of the Study

The scope of the study is limited not only to the provisions in the Indian Limited Liability Law but also the position in other countries. The research work is limited

not only to the Indian as well as important international laws and their study. This study has highlighted not only the provisions of the LLP Act, 2002 but also has dealt with their International counterparts. As there is very little chance of any field work for this study the entire study is 'doctrinal'. However the research work will be directly or indirectly helpful to the policy makers towards improving the new Concept of Limited Liability partnerships in India.

1.1.3 Source of Information

Researcher in this work relied mainly on 'Doctrinal Method' of research. The methodology adopted for the present dissertation is doctrinal, analytical and descriptive. The researcher mainly depended on the Primary sources like Statutes and Committee report and Secondary sources like books, articles and websites. Opinions of research scholars, experts in the respective field, and opinions of professionals like Company Secretaries, Chartered Accountants and Advocates who deal with this subject are used as real contribution to this work. Internet has provided with a major contribution of most relevant and latest information on the web, which helped to explore the subject through various dimensions. RMLNLU, Library and e-resources have played a crucial role to bring out specialist material of the dissertation. Westlaw has provided researcher with ample resources to analyze concepts in the light of international perspectives. Opinions of various experts published in web also contributed a great deal for conducting research in the subject. Through out this paper researcher has followed a uniform mode of citation.

1.2. Research Scheme

The present study is an attempt to discuss the concept of Limited Liability Partnerships under The LLP Act, 2008 in the light of detailed study undertaken by the J.J. Irani as well as Naresh Chandra Committees', the US, UK and Singapore law and the decisions of the Indian and foreign courts. The research topic is "EMERGENCE OF LIMITED LIABILITY PARTNERSHIP LAWS IN INDIA –A CRITICAL ANALYSIS (WITH REFERENCE TO U.S., U.K., SINGAPORE AND INDIAN LLP LAWS)".

There are many manifestations of Limited Liability concept with varying end purposes. In evaluating the likely effects of Liability, an important first step is to define the the various forms of Business Organisations because this very concept is the tool to identify and define the boundaries of liability between partners/members of a firm. Once the question of liability has been ascertained, other important aspects of such an organization need to be explored. Next researcher scrutinized entire gamut of Limited Liability Partnership Laws against the background of existing Limited Liability Partnership laws in the US, UK, Singapore and India. All the research questions have been addressed. Considering all the above aspects and to facilitate the discussion and for a thematic development of the subject the research work is divided into seven chapters. Brief overview of the chapters is as follows-

Chapter I deals with 'Introduction'. In this chapter the researcher has given a brief overview of Limited Liability. The researcher has tried to address the question of why the question of Liability is important and has also provided a Research Methodology for the discussion.

Chapter II deals with the 'Historical background of Limited Liability'. For every research work it is very important that the research work firstly makes an attempt to clarify the main concepts. Hence keeping this in mind the researcher in this chapter makes an attempt to clear

the concept of Limited Liability, its Historical Background, Evolution of a new business vehicle LLP and its Definition and Nature.

Chapter III highlights the 'LLP Laws in U.S., U.K. and Singapore. This chapter covers their existing statutes through the realms of History.

Chapter IV deals with the 'LLP's in India'. For a better appreciation of the law dealing with LLP's, it would be beneficial to demarcate between LLP's on one hand and the other forms of Businesses on the other.

Chapter V covers the discussion on 'Comparison with other Countries'. The researcher has dealt with the Laws governing LLP's in U.S., U.K., Singapore and India. The selection of these countries becomes important because the Indian manifestation of LLP is a reflection of its counterparts from these countries only.

Chapter VI deals with 'Legal and Procedural Aspects of LLP's in India'. It is important to examine the entire statute, i.e. the LLP Act, 2008. Hence keeping this in mind the researcher herein makes an attempt to minutely analyse the procedural and all other finer aspects of the Act.

Lastly on the basis of the research work the researcher had drawn conclusion by proving the hypothesis and has also made some suggestions which the researcher thinks is the need of the hour in order to see that Indian Limited Liability Partnership Law is effective when it comes to the existing business scenario in India.

1.3. Research Hypothesis

Various forms of Business Organisations are of prime importance in today's world of capital market. Nations of the world have come to realize that an effective Business Vehicle/Model is essential for the growth of any economy. India though a bit late in the world in enacting a new LLP Law has been trying to taking initiatives to make the provisions of LLP Act, 2008 enforceable. Keeping this in mind the researcher has formed the following hypothesis and tried to answer the issues-

The aim of research work is to analyze and examine the following issues

- What is limited liability?
- What is the necessity to introduce the limited liability partnership principles amongst the existing forms of business?
- Historical background of LLP?
- Experience of other countries?
- Need of LLP in India?
- Similarities and distinctions in the Acts of various countries and India?
- Whether LLP Act, 2008 in India justifies the reason for its enactment?

The researcher has made an attempt to throw a light on the above hypothesis in the dissertation - "EMERGENCE OF LIMITED LIABILITY PARTNERSHIP LAWS IN INDIA –A CRITICAL ANALYSIS (WITH REFERENCE TO U.S., U.K., SINGAPORE AND INDIAN LLP LAWS) ".

CHAPTER 2: HISTORICAL EVOLUTION OF LIMITED LIABILITY RULE

2.1. Introduction:

This chapter reviews the literature on limited liability. This literature began in the eighteenth and nineteenth centuries with a concern for agency costs rather than for the liability system. After a long hiatus, when it re emerged in the 1960s and 1970s it was concerned primarily with contract liability and with the role of limited liability in facilitating capital markets. It was only after the theoretical literature on limited liability on these topics was relatively well developed that attention turned to tort liability. This literature developed in tandem with the growth of tort actions in the United States for catastrophic liability - generally involving class actions on behalf of large classes of plaintiffs. It became clear with the development of such actions that actors had developed liability-limiting strategies that had the ultimate effect of frustrating the liability system. Because liability systems within societies tend to be unitary, empirical work has generally been difficult to undertake. There are a few examples of parallel systems of limited and unlimited liability, but the evidence on the effects of limited liability remains extremely limited.

The concept of a limited liability partnership surfaced in response to the great real estate and energy prices crumple in 1980s and the consequent impact it had on the banks and other financial institutions. Since not much could be recovered from these failed financial institutions, attention soon shifted to the lawyers and accountants who had represented the failed financial institutions before their collapse.³ The plausibility of recovery came across owing to the backing of these professionals by rich and moneyful partnerships and insurers. The United States, which was the epicenter of that financial crunch—as it has been for most

³ Hamilton, —Registered Limited Liability Partnership: Present at the Birth (Nearly)□ 66 *University of Colorado Law Review* 1065, 1069.

other, including the present sub-prime credit crunch—spearheaded the process of legislating the concept of LLPs. The initial hesitation—both in the academic and legislative circles—in disturbing the long-settled principles of —unlimited liability of the partners of a partnership firm on the grounds of its moralistically weak foundations and its discriminatory nature, was soon overcome by the commercial expediency of its legislation. Thus, came on the statute book, the first law on LLP with Texas enacting the Texas House Bill 278 on 26 August 1991. The other countries have soon followed the idea and thus the evolution of LLP took place.

2.2. The History of the Law of Limited Liability:

2.2.1 Ancient Rome:

In ancient Rome many corporate entities were *de facto* rather than *de jure*, and liability remained unlimited⁴. This is attributed at least in part to the fact that most firms were not highly specialized, because pressure toward limited liability occurs with a separation of ownership and control⁵. While vicarious liability existed in Rome, it was strictly interpreted by limiting the agents' authority, thus creating some *de facto* limited liability⁶. Further, the *pater familias*, the head of the principal economic unit in Rome, was liable for the debts of a slave or son only to the extent of the extent of the *peculium*, or sum entrusted to him⁷. While

⁴ Gillman, Max and Eade, Tim (1995), 'The Development of the Corporation in England, with Emphasis on Limited Liability', *International Journal of Social Economics*, 20-32.

⁵ .ibid.

⁶ . Johnston, David (1995), 'The Development of Law in Classical and Early Medieval Europe: Limiting Liability: Roman law and the Civil Law Tradition', *Chicago-Kent Law Review*, 1515-1538.

⁷ . . Johnston, David (1995), 'The Development of Law in Classical and Early Medieval Europe: Limiting Liability: Roman Law and the Civil Law Tradition', *Chicago-Kent Law Review*, 1515-1538 , Perrott, David L (1982), 'Changes in Attitude to Limited Liability - the European Experience', in Orhnlal, Tony (ed), *Limited Liability and the Corporation*, London and Canberra, Croom Helm, 81-121