FACULTY OF JURIDICAL SCIENCES

Lecture-20

3. Limited Liability Partnership (LLP)

According to the Limited Liability Partnership Act, 2008, an LLP is a body corporate formed and incorporated under this Act. It is a legal entity separate from that of its members.

According to Limited liability partnership Act 2008, limited liability partnership means, “a partnership formed and registered under this act”.

LLP agreement means any written agreement between the partners of the LLP or between LLP and its partners which determines the mutual rights and duties of the partners and their rights and duties in relation to that LLP.
Any two or more persons can form an LLP. Even a limited Company, a foreign Company, a LLP, a foreign LLP or a non-resident can be a partner in LLP

Features:

(i) An LLP must be registered under the LLP Act 2008.
(ii) It is a body corporate having a separate entity of its own.
(iii) It has perpetual succession. Any change in its members does not affect its existence, rights and liabilities,
(iv)Any individual or a body corporate can be a partner in an LLP.
(v) Every LLP must have at least two partners.
(vi)There must be at least two designated partners and one of them must be a resident in India.
(vii) An LLP must maintain proper books of accounts as per the double entry system.
(viii) An LLP must file with the Registrar a Statement of Account and solvency along with its annual return in the prescribed form.

Merits:

a. An LLP enjoys stability as changes in partners do not affect its existence.
b. The liability of an LLP and its partners in Limited.
c. A body corporate and a foreigner can be partners in an LLP.
d. An LLP can raise, large amount of funds as there is no restriction on the number of members and risk involved is limited.

Demerits:

a. Time and money are involved in the formation and registration of an LLP.
b. There is less flexibility of operations because an LLP has to comply with certain legal formalities.
c. There is lack of business secrecy as an LLP has to file the prescribed documents with the Registrar. Its accounts are open to the public for inspection.
The LLP gives an entrepreneur the twin benefits of limited liability and a flexible internal structure. It is also free from dividend distribution tax and minimum alternate tax.

4. Company:

With the growing needs of modern business, collection of vast financial and managerial resources became necessary. Proprietorship and partnership forms of ownership failed to meet these needs due to their limitations, e.g., unlimited liability, lack of continuity and limited resources.

The company form of business organization was evolved to overcome these limitations. Joint Stock Company has become the dominant form of ownership for large scale enterprises because it enables collection of vast financial and managerial resources with provision for limited liability and continuity of operations.

A joint stock company is an incorporated and voluntary association of individuals with a distinctive name, perpetual succession, limited liability and common seal, and usually having a joint capital divided into transferable shares of a fixed value.

Chief Justice John Marshall of U.S.A defined a company in the famous Dartmouth College case as “an artificial being, invisible, intangible and existing only in contemplation of law; being the mere creature of law it possesses only those properties which the charter of its creation confers upon it, either expressly or as incidental to its very existence; and the most important of which are immortality and individuality.
“Thus, a company is an artificial legal person having an independent legal entity.

Merits of Company Organization:

The company form of business ownership has become very popular in modern business on account of its several advantages:

1. Limited Liability:
Shareholders of a company are liable only to the extent of the face value of shares held by them. Their private property cannot be attached to pay the debts of the company. Thus, the risk is limited and known. This encourages people to invest their money in corporate securities and, therefore, contributes to the growth of the company form of ownership.

2. Large Financial Resources:

Company form of ownership enables the collection of huge financial resources. The capital of a company is divided into shares of small denominations so that people with small means can also buy them. Benefits of limited liability and transferability of shares attract investors. Different types of securities may be issued to attract various types of investors. There is no limit on the number of members in a public company.

3. Continuity:

A company enjoys uninterrupted business life. As a body corporate, it continues to exist even if all its members die or desert it. On account of its stable nature, a company is best suited for such types of business which require long periods of time to mature and develop.

4. Transferability of Shares:

A member of a public limited company can freely transfer his shares without the consent of other members. Shares of public companies are generally listed on a stock exchange so that people can easily buy and sell them. Facility of transfer of shares makes investment in company liquid and encourages investment of public savings into the corporate sector.

5. Professional Management:

Due to its large financial resources and continuity, a company can avail of the services of expert professional managers. Employment of professional managers having managerial skills and little financial stake results in higher efficiency and more adventurous management. Benefits of specialization and bold management can be secured.

6. Scope for Growth and Expansion:

There is considerable scope for the expansion of business in a company. On account of its vast financial and managerial resources and limited liability, company form has immense potential for growth. With continuous expansion and growth, a company can reap various economies of large scale operations, which help to improve efficiency and reduce costs.

7. Public Confidence:

A public company enjoys the confidence of public because its activities are regulated by the government under the Companies Act. Its affairs are known to public through publication of accounts and reports. It can always keep itself in tune with the needs and aspirations of people through continuous research and development.

8. Diffused Risk:
The risk of loss in a company is spread over a large number of members. Therefore, the risk of an individual investor is reduced.

9. Social Benefits:
The company organization helps to mobilize savings of the community and invest them in industry. It facilitates the growth of financial institutions and provides employment to a large number of persons. It provides huge revenues to the Government through direct and indirect taxes.

Demerits of Company:

A company suffers from the following limitations:

1. Difficulty of Formation:
It is very difficult and expensive to form a company. A number of documents have to be prepared and filed with the Registrar of Companies. Services of experts are required to prepare these documents. It is very time-consuming and inconvenient to obtain approvals and sanctions from different authorities for the establishment of a company. The time and cost involved in fulfilling legal formalities discourage many people from adopting the company form of ownership. It is also difficult to wind up a company.

2. Excessive Government Control:
A company is subject to elaborate statutory regulations in its day-to-day operations. It has to submit periodical reports. Audit and publication of accounts is obligatory. The objects and capital of the company can be changed only after fulfilling the prescribed legal formalities. These rules and regulations reduce the efficiency and flexibility of operations. A lot of precious time, effort and money have to be spent in complying with the innumerable legal formalities and irksome statutory regulations.

3. Lack of Motivation and Personal Touch:
There is divorce between ownership and management in a large public company. The affairs of the company are managed by the professional and salaried managers who do not have personal involvement and stake in the company. Absentee ownership and impersonal management result

in lack of initiative and responsibility. Incentive for hard work and efficiency is low. Personal contact with employees and customers is not possible.

4. Oligarchic Management:

In theory the management of a company is supposed to be democratic but in actual practice company becomes an oligarchy (rule by a few). A company is managed by a small number of people who are able to perpetuate their reign year after year due to lack of interest, information and unity on the part of shareholders. The interests of small and minority shareholders are not well protected. They never get representation on the Board of Directors and feel oppressed.

5. Delay in Decisions:

Too many levels of management in a company result in red-tape and bureaucracy. A lot of time is wasted in calling and holding meetings and in passing resolutions. It becomes difficult to take quick decisions and prompt action with the consequence that business opportunities may be lost.

6. Conflict of Interests:

Company is the only form of business where in a permanent conflict of interests may exist. In proprietorship there is no scope for conflict and in a partnership continuous conflict results in dissolution of the firm. But in a company conflict may continue between shareholders and board of directors or between shareholders and creditors or between management and workers.

7. Frauds in Promotion and Management:

There is a possibility that unscrupulous promoters may float a company to dupe innocent and ignorant investors. They may collect huge sums of money and, later on, misappropriate the money for their personal benefit. The case of South Sea Bubble Company is the leading example of such malpractices by promoters.

Moreover, the directors of a company may manipulate the prices of the company’s shares and debentures on the stock exchange on the basis of inside information and accounting manipulations. This may result in reckless speculation in shares and even a sound company may be put into financial difficulties.

8. Lack of Secrecy:

Under the Companies Act, a company is required to disclose and publish a variety of information on its working. Widespread publicity of affairs makes it almost impossible for the company to retain its business secrets. The accounts of a public company are open for inspection to public.

9. Social Evils:
Giant companies may give rise to monopolies, concentration of economic power in a few hands, interference in the political system, lack of industrial peace, etc.

Suitability:
Despite its drawbacks, the company form of organization has become very popular, particularly for large business concerns. This is because its merits far outweigh the demerits. Many of the drawbacks of a company are mainly due to the weaknesses of the people who promote and manage companies and not because of the company system as such. The company organization has made it possible to accumulate large amounts of capital required for large scale operations.

Due to its unique characteristics, the company form of ownership is ideally suited to the following types of business:

(i)Heavy or basic industries like ship-building, coach-making factory, engineering firms, etc., requiring huge investment of capital.

(ii) Large scale operations are very crucial because of economies of scale, departmental stores, chain stores and enterprises engaged in the construction of bridges, dams, multistoried buildings, etc.

(iii) The line of business involves great uncertainty or heavy risk, e.g., shipping and airline concerns.

(iv) The law makes the company organization obligatory, e.g., banking business can be run only in the form of company.

(v) The owners of the business want to enjoy limited liability.