

# **THE INSTITUTE OF CHARTERED ACCOUNTANT OF INDIA, NASHIK**

## **Seminar on LIMITED LIABILITY PARTNERSHIP**

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# CONVERSION OF PARTNERSHIP FIRM OR COMPANY TO LLP

# Coverage of Topics

- Types of Conversion
- Conversion of a Firm/Company to LLP
  - Why convert (advantages)
  - Legal Provisions relating to Conversion
  - Procedure of Conversion
- Provisions of Income Tax Act relating to conversion of
  - Partnership into LLP
  - Company into LLP
- Check List before Converting
  - Partnership Firm intending to convert into LLP
  - Co intending to convert into LLP.

# TYPES OF CONVERSION

Sr. No	Type of Conversion	Section of LLP Act	Schedule of LLP Act
1	PARTNERSHIP to LLP	Sec.55	Schedule II
2	PRIVATE LIMITED COMPANY to LLP	Sec.56	Schedule III
3	UNLISTED PUBLIC LIMITED Co. to LLP	Sec. 57	Schedule IV

- Whether a PROPRIETARY FIRM can be converted to LPP ?
- Whether a PUBLIC LIMITED CO. can be converted to LPP ?

# Conversion of Firm to LLP

## Why to Convert ?

- ❑ Liability is limited to contributions of Partners in LLP.
- ❑ No upper limit on member of partners.
- ❑ Separate Legal Entity
- ❑ Perpetual Succession(Existence of LLP not dependent on partners).
- ❑ No change in Income Tax Rate
- ❑ No capital gains on Transfer of Assets in the course of conversion.

# CONVERSION OF COMPANY TO LLP:

## Why Convert a Company to LLP ?

### ❑ Minimum Procedural Compliance for LLP

#### Compliances under Companies

Act,2013 with regard to:-

- Share Capital
- Minutes of Board/AGM
- Declarations
- Appointment & Removal of Directors
- Appointment & Removal of Auditors
- Related Party Transactions
- Borrowings

Not Applicable  
to LLP

# Why Convert a Company to LLP?

## □ Status of Separate Legal Entity continues:

- Can sue and can be sued in its own name (LLP)
- Can acquire & hold property in its own name.

## □ Tax Advantage:

- No change in Income Tax Rate (30%)
- No Surcharge
- No Capital Gain Tax on conversion {Sec 47 (xiiib)}.



## Tax Advantage

- No DDT- Share of Profit from LLP is exempt u/s 10(2A)
- No Wealth Tax.
- 2(22)(e) not applicable. ( No Deemed Dividend)
- Partners can claim Interest on Capital.
- Unabsorbed Loss/Depreciation of Company is allowed to Successor LLP (Sec 72A(6A) Finance Act 2010.
- Depreciation in the year of Conversion on prorate basis.
- Restrictions u/s 79 are not applicable to a Partnership Firm.
- Audit applicable if, Turnover 40 Lacs/Contribution 25 Lacs

**LAW RELATING TO  
CONVERSION OF FIRM OR  
COMPANY INTO LLP  
(Section 55 TO 58 & Schedule II, III, IV)**

# LAW RELATING TO CONVERSION OF FIRM OR COMPANY INTO LLP

## ■ Section 55/56/57 (Chapter X ):

A Firm/Company may convert into LLP in accordance with the provision of LLP Act and Second/Third/Fourth Schedule.

## ■ Eligibility for conversion:

- The LLP into which the Firm/Company is converted, comprises, all Partners/Shareholders and no one else.
- In the case of a **Company**, there is no security interest subsisting at the time of application

### ■ Statement to be filed:

- Firm/Company shall file statement by all Partners in *Form 17/18* along with fees (Rs 50 to 200/-depending upon the contribution).
  - Name & Registration No. of Firm, if any/Company
  - Date on which the Firm/Company was registered with ROF/ROC
- Issue of Certificate of Registration(*Form 19*).

## ■ Effect of Conversion Sec.58(4):

- A LLP comes into existence from the date of issue of Certificate of Registration.
- All Assets & Liabilities shall be transferred and vest in LLP.
- The Firm/Company shall be deemed to be dissolved & removed from records of ROF/ROC.

## ■ Intimation to ROF/ROC

The LLP shall intimate the conversion to ROF/ROC within 15 days from the date of Conversion.( Form No.14 )

- Registration relating to Property
- Pending Proceedings
- Existing Agreements / Contracts / Employment.
- Continuation of conviction ruling order or judgement.
- Appointment, Authority or Power

### ■ Notice of Conversion in Correspondences:

- For a period of 12 months
- Statement that the firm was converted w.e.f (date)
- Name & Registration No of erstwhile Firm.
- Penalty for contravention (Rs 10,000 to 1,00,000) and Rs 50 to 500 per day for continuous default.

# **PROCEDURE RELATING TO CONVERSION OF FIRM OR COMPANY INTO LLP**



# PROCEEDURE TO FOLLOW FOR CONVERSION

- STEP 1: Obtain Digital Signature of DP
- STEP 2: File Form 1 for Name Reservation
- STEP 3: File Form 17/18 Conversion application cum Declaration.
- STEP 4 : File Form 2 Incorporation Document
- STEP 5 : Obtain Registration Certificate from Registrar for Conversion in Form 19
- STEP 6: Intimate conversion in form 14 to ROF/ ROC.
- STEP 7: Filing LLP Agreement(Form 3) within 30days.

PROCEDURE RELATING TO CONVERSION OF FIRM OR COMPANY INTO LLP

# DECLARATIONS TO BE MADE IN FORM 17/18 FOR CONVERSION

# Form 17

## Conversion of Partnership to LLP

- Part A: Application
- Part B: Declaration
  - Consent for conversion from all Partner
  - Accepting J & S liability for the Period prior to conversion.
  - Consent of All Creditors obtained.
  - LLP comprises of all Partners & No. one else.

# Form 18

## Conversion of Pvt. Co. to LLP

Part A: Application

Part B: Declaration

- Consent of all Shareholders for conversion obtained.
- Consent of all **Secured Creditors** is obtained.
- All documents due for filing including latest Balance Sheet & Annual Return have been filled under Companies Act.
- LLP comprises of all shareholders and no one else.

# Common Declarations in Form 17/18

1. All the requirements of LLP Act & Rules are complied.
2. All Approvals, permission Clearance are obtained.
3. All information provided in the form is correct & complete.

# CHECKLIST FOR FIRM INTENDING TO CONVERT TO LLP

Considerations	Effect of Conversion	Possible Solution
Does the firm intend to avail presumptive taxation scheme u/s 44AD	LLPs cannot avail presumptive taxation u/s 44AD	-
Does Firm have unabsorbed losses to be carried forward or sett off?	Controversial but arguably be available.	Defer conversion until losses sett-off.
Does the firm have unabsorbed depreciation?	Controversial but arguably be available.	Defer conversion until unabsorbed depreciation is recouped.

# **CHECKLIST FOR COMPANY INTENDING TO CONVERT TO LLP**



Considerations	Effect of Conversion	Possible Solution
Accumulated MAT Credit Available.	Accumulated MAT Credit will be lost.	Defer conversion till MAT credit is recouped.
Does Co. intend to implement VRS scheme	Tax exemption upto Rs 5 Lakhs u/s 10(10C) is available to employee, if employer is a company.	Implement VRS and then convert.
Unavailed installments of deduction u/s 35D.	Availment by LLP after conversion not free from doubt. No enabling provision in Sec.35D	Defer conversion

# TAX PROVISIONS RELATING TO CONVERSION OF FIRM TO LLP

# Provisions under Income Tax Act

- ❖ No provision for taxation in case of conversion of General partnership to LLP.
- ❖ Explanatory memorandum to Finance act 2009  
Conversion has no tax implication if
  - i. Rights and obligations of partners remains same after conversion.
  - ii. No transfer of any Asset or Liability takes place after conversion.
- ❖ Finance Act (no.2) or Finance Act 2010 has not even made any amendment in Sec.2(47) or Sec.47

❖ Arguments to support Conversion is not a “Transfer”

- Conversion does not have attributes of ‘Transfer’.
- Absence of any amendment in the definition of ‘Transfer’ (u/s 2(47) or deemed transfer u/s 45 supports intention of Law.
- Support from judicial pronouncements  
**CIT vs Taxpin Engg & Mfg works (2003) 263 ITR 345**

# TAX PROVISIONS RELATING TO CONVERSION OF COMPANY TO LLP

# Conversion of Company to LLP:

## Conversion not Taxable:

- ❖ New provision u/s 47 (xiiib) from AY 2011-12.
- ❖ Transfer of Capital Assets or Intangible Assets on conversion to LLP is not regarded as transfer for Capital Gains purpose subject to six conditions.
- ❖ Transfer of share or Shares on conversion to LLP is not regarded as transfer for Capital Gains purpose subject to six conditions.

# SIX CONDITIONS PRESCRIBED u/s 47(xiiib)

1	Eligibility Criteria	Average sales/turnover/gross receipts of the company does not exceed Rs.60 Lakhs in any 3 preceding previous years
2	Conditions at conversion stage	<p>I. All shareholders of the company before conversion become partners of the LLP and capital /profit sharing ratio in the LLP should be in same proportion as their shareholding in the company</p> <p>II. Shareholders of the company receive no consideration other than shares in contribution and PSR in the LLP</p> <p>III. All assets and liabilities of the company are transferred to LLP</p>
3	Conditions after Conversion	<p>I. Erstwhile Shareholders of the company to retain atleast 50% PSR for 5 years from date of conversion</p> <p>II. No distribution of accumulated profits of the company as on the date of conversion for 3 years from date of conversion</p>

# Condition:1

- ❖ The Total Sales, Turnover or Gross Receipts in business of the company do not exceed Rs.60 Lakhs in any of the three previous years preceding the previous year in which conversion takes place .

## Issues:

- Total Sales/Turnover/Gross receipts not defined
- Turnover qua year ; not average turnover.
- If Company is in existence for less than three years ?
- Turnover to exclude material supplied by party in contract business .(Circ.684/10.6.94)
- More than one Business



## Condition :2

- ❖ All the shareholders of the company immediately before the conversion become partners of the LLP. Their capital contribution and profit sharing ratio should be in the same proportion as their shareholding in their shareholding in the company as on the date of conversion.
- ❖ Issues:
  - I. Includes Preference Shareholders ?
  - II. Registered Shareholders or beneficial shareholder?
  - III. Minor Shareholders of Company
  - IV. Suitable clause in LLP agreement to bind partners continue for five years to avoid Tax liability.

## Condition:3

- ❖ All assets & liabilities of the Company immediately before the conversion become the assets and liabilities of the LLP

## Objective:

1. Conversion be a total conversion so that all assets & liabilities are vested in LLP
2. No part of asset be transferred to any partner on conversion

## Condition :4

- ❖ The shareholder of the company do not receive any consideration or benefit other than share in profit and capital contribution in the LLP
- ❑ The words consideration or benefit be read as in connection with 'Conversion'

## Condition:5

- ❖ PSR shall not be less than 50% for a period of five years from the date of conversion

## Example:

Date of Conversion 01.04.2015

5 Partner	PSR 31.03.2015	01.04.2015 to 31.03.2020			
		Partner	PSR	Partner	PSR
A	50	A	25	A	20
B	50	B	25	B	25
		C	30	C	30
		D	20	D	25
		<u>Permitted</u>		<u>Not Permitted</u>	

# Condition :6

- ❖ *No payment to any partner out of accumulated Profits of Company for 3 years*

## Objective:

1. Conversion should not be used as a medium to avoid paying DDT by Company.
2. Funds be utilized for Business.

## Planning:

1. Issue Bonus Shares & avoid possible dispute from New LLP partners claim on accumulated profit.
2. Capital account balance in LLP will enhanced & higher interest on Capital can be claimed.

# Unabsorbed Loss/Depreciation:

- **Sec.72A (6A) Finance Act, 2010: Unabsorbed Loss/Depreciation of Predecessor company will be allowed to successor LLP if Condition in 47 (xiiib) satisfied**
- When allowed: It will be allowed in the previous year which conversion took place
- When denied: If conditions are violated benefit of loss allowed to LLP is withdrawn & tax charged in the year of violation.
- Accumulated Loss: includes 'Business Loss' only; not Speculation loss.

# Depreciation Apportionment between Predecessor Company & Successor LLP:

- Annual depreciation apportioned in the ratio of No. of days assets used by Predecessor Company & Successor LLP.
- Apportionment Rule applies only if conditions in 47 (xiiib) complied.

# Breach of condition of Section 47(xiiib):

## ❖ Capital Gains:

Profits arising from the transfer of assets not earlier charged to tax would be deemed to be the profits in the hands of succeeding LLP/Shareholders of the predecessor company in the year of breach.

## ❖ Accumulated Losses/Unabsorbed Depreciation:

The benefit of sett-off availed by the LLP would be deemed to be the profits in the hands of the LLP in the year of breach



Knowledge Speaks  
But  
Wisdom listens

THANK YOU