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Draft Legislative Guide on an UNCITRAL Limited Liability Organization

Note by the Secretariat

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Background information

1. The draft legislative guide on an UNCITRAL Limited Liability Organization

1. The text of the draft legislative guide is reproduced as an annex to this Note of the Secretariat and it is transmitted to the Commission for its consideration and possible adoption in accordance with the Summary of the Chair and Rapporteur on the work of Working Group I at its thirty-fifth session ([A/CN.9/1048](#)).

2. The text reflects the decisions of the Working Group at its thirty-fifth session and incorporates editorial adjustments made by the Secretariat, or suggested by delegations to the Working Group, to enhance its clarity and cohesion. Guidance to the changes arising from the deliberations of the Working Group at its thirty-fifth session is not reflected in footnotes to the text and the Commission might wish to refer to the Summary of the Chair and the Rapporteur (see para. 1 above).

3. In its deliberations, the Commission may wish to note that the Working Group decided to use the term UNCITRAL Limited Liability Organization (UNLLO) on an interim basis until it could decide on a preferred term to denote the simplified business entity discussed in the guide. At its thirty-fifth session, the Working Group considered possible names for the UNLLO without reaching any conclusion. The Commission may thus wish to agree on such a name and on a phrase or abbreviation that could be used for identification of the UNLLO as recommended in the draft guide (see draft rec. 6).

2. The final version of the Legislative Guide on [an UNCITRAL Limited Liability Organization]

4. Once adopted, the guide will be published in electronic and paper format. A short “Preface” reading along the following lines will introduce it:

“The Legislative Guide on [an UNCITRAL Limited Liability Organization] was prepared by the United Nations Commission on International Trade Law (UNCITRAL) and adopted at its [____] session in [____]. The project arose from a decision of the Commission at its forty-sixth session, in 2013, that work on reducing the legal obstacles faced by micro, small and medium-sized enterprises (MSMEs) throughout their life cycle, in particular, in developing economies, should be added to its work programme and that such work should begin with a focus on the legal questions surrounding the simplification of incorporation ([A/68/17](#), para. 321).

Working Group I (Micro, small and medium-sized enterprises or MSMEs) was given the mandate to address this topic. The Working Group commenced its work on simplification of incorporation in February 2014 in parallel with the work on simplification of business registration. The Commission adopted the UNCITRAL Guide on Key Principles of a Business Registry in 2018.

The Guide on [an UNCITRAL Limited Liability Organization] aims at assisting States at crafting a simplified legal form for MSMEs that can best facilitate their formation and operation, thus enhancing their sustainability and chances of success and growth. The Guide is based on the principle “think small first” that commercial law reform should start with a focus on the actual needs of the smallest businesses and avoid placing unnecessary legal burdens on them. The Guide takes the view that the optimal solution for the creation of an appropriate simplified legal regime for MSMEs should not be to reform and simplify existing company law regimes, but rather to develop a separate legal regime that focuses on such needs.

In addition to representatives of the member States of the Commission, representatives of observer States and a number of international organizations, both intergovernmental and non-governmental, participated actively in the preparatory work of the draft guide.

The final negotiations on the draft guide on [an UNCITRAL Limited Liability Organization] were held during the [____] session of UNCITRAL in [____] and the text was adopted by consensus on [____]. Subsequently, the General Assembly expressed its appreciation to UNCITRAL for completing and adopting the Legislative Guide in resolution [insert the number of the resolution].”

5. The guide will also contain annexes, such as those setting out a list of all recommendations and reproducing the Commission’s decision adopting the guide, and an index.

Annex

Draft legislative guide on an UNCITRAL Limited Liability Organization (UNLLO)

I. Introduction

A. Purpose of the Legislative Guide

1. Most businesses in the world are micro, small and medium-sized enterprises (MSMEs). They are the backbone of many economies and account worldwide for a large share of the employment rate and of States' Gross Domestic Product (GDP). Despite this major role, however, several factors still affect their performance and capacity to develop. Unlike larger businesses, they lack the economies of scale to tap into new markets and expand business, thus missing the growth opportunities offered by globalization and economic integration. International forums and organizations as well as individual States recognize the importance of strengthening the economic role and position of MSMEs and enhancing MSMEs' competitiveness to enable them to benefit from an evolving international economic environment. UNCITRAL has underscored that importance through its decision to take up work on reducing the legal obstacles faced by MSMEs in their life cycle. This work has resulted in, *inter alia*, the preparation of [a draft text] on a simplified insolvency regime and this Legislative Guide on an [UNCITRAL Limited Liability Organization (UNLLO)].¹

2. In order to support MSME formation and operation, various States representing different legal traditions around the world have adopted legislation on simplified business forms. Those business forms can be of a corporate, partnership or hybrid type. They may provide for single-member businesses or for multi-member business forms that entail asset partitioning with or without requiring a separate legal personality. Regardless of their more specific features, those laws all aim for simplified formation, flexibility of organization and operation, and asset partitioning.

3. The adoption of such simplified business forms has often lowered entry barriers, provided effective organizational solutions and reduced transaction costs, thus increasing employment opportunities and economic growth rates. Moreover, it has been found that a large informal sector has a negative impact on economic development. These simplified business forms have thus encouraged migration of business to the formal sector, thus increasing business and tax registration of previously unregistered businesses, promoting greater compliance with legal requirements, and better visibility with the public. The various domestic reforms to creating or improving such business forms – both MSME-specific and otherwise – demonstrate that good practices around the world share various key principles which could thus be said to be international in their application.

4. The Legislative Guide (the “Guide”) attempts to distil these good practices and key principles into a series of recommendations on how a State could devise and regulate a simplified legal form for MSMEs that can best facilitate their success and sustainability, stimulate entrepreneurship and promote participation and the creation of value in the economy. Such simplified legal form could facilitate the economic inclusion of women and other entrepreneurs who may face unfavourable cultural, institutional and legislative frameworks such as youth and ethnic minorities. The commentary that precedes each recommendation relies both on specific legislative efforts to provide for single-member businesses or business entities, as well as broader reforms to assist MSMEs that have been implemented in various States, so as to explain in greater detail the rationale leading to those recommendations. States may

¹ The secretariat has placed “[UNCITRAL Limited Liability Organization (UNLLO)]” in brackets to indicate that this is a temporary name pending a Working Group's decision on this matter, see *infra* footnotes 2 and 3.

adapt and in certain cases even deviate from the guidance provided in the recommendations. However, they should not defeat the purpose of the Guide to create a balanced regime that provides simplicity and flexibility of the MSME form and ensures legal certainty (see para. 13 below).

5. The Guide focuses on the formation and operation of the UNLLO and does not consider other matters that may be relevant to the existence of the business, for example issues of taxation policy. Such matters are left to States when drafting legislation on the basis of the Guide, with the understanding that they might consider their policy options in the broader context of how best to reduce legal obstacles for MSMEs more generally (see also para. 30 below).

1. “Think small first”

(a) Assessing the needs of entrepreneurs

6. A legislative regime for simplified business entities should start with a focus on the actual needs of the smallest business entities and avoid placing unnecessary legal burdens on them (“think small first”). To that end, the Guide considers how MSME entrepreneurs could most benefit from legislation based on its recommendations and be encouraged to conform to the principles they contain. Such entrepreneurs mainly operate the micro and small businesses around the world for which the main characteristics are strong reliance on human capital rather than organizational processes, limited source and number of employees (usually drawn from family and friends), limited range of products or services offered to customers and limited capital. These entrepreneurs could range from individual street vendors, to small family business owners wishing to scale up and formalize their operations, and to small firms seeking to grow and position themselves in more innovative sectors, such as the information technology field. Regardless of the size of their businesses and their gender, those micro and small businesses’ entrepreneurs share several common needs, as discussed below.

(i) *Freedom, autonomy and flexibility*

7. Without prejudice to the rights of third parties, MSME entrepreneurs could be expected to want *freedom and autonomy* to decide for themselves how they operate their business without being constrained by rigid and formalistic rules and procedures or be subject to detailed mandatory requirements on the conduct of their activities. They also would want the *flexibility* to adapt to changing circumstances that may impact MSMEs more than larger companies and consider how their business might evolve and develop over time, including the ability to establish branches or representative offices without having to change their legal form.

(ii) *Simplicity and accessibility*

8. MSME entrepreneurs are likely to want *simplicity and accessibility* to characterize the rules on the legal establishment of their business, and on its administration and operation. These rules should be in simple and *accessible* terms, and the use of modern technology, such as mobile applications to complete payments or prepare balance sheets, should be encouraged.

(iii) *Identity and visibility*

9. MSMEs need an *identity and visibility* in order to more successfully compete in domestic and globalized markets and to attract more and better quality clients. In addition to the obvious protections and advantages associated with taking on a legally recognized identity and operating within a recognized legal framework, the business can also use such legally recognized identity to develop its reputation and “brand” and increase its value.

(iv) Certainty and protection of property rights

10. Regardless of the size of their business, all entrepreneurs need *certainty in and protection of their property rights*. MSME entrepreneurs will thus wish to control the assets of their business and be able to take advantage of asset partitioning to protect their personal assets from claims of business creditors. Conversely, personal creditors of business owners and managers should not be able to seize business assets in order to satisfy personal debts.

(v) Control and management

11. Finally, MSME entrepreneurs generally want *to control and to manage their business*, rather than leave administrative and strategic decisions to a professional manager.

(b) Drafting the Guide from a “think small first” perspective

12. In keeping with the desire to create a legal text that can accommodate the needs of micro entrepreneurs, the Guide proposes a legal business form that moves away from the more traditional, hierarchical and formal governance models usually associated with public companies, which may not be appropriate for smaller businesses. For example, the Guide acknowledges the MSME entrepreneurs’ need for freedom and flexibility and stresses the importance of freedom of contract in the governance of the business. However, the Guide recognizes through many default provisions that such entrepreneurs may also require protection against unforeseeable circumstances or events. Simplicity and accessibility characterize all aspects of the formation and operation of the business, as well as the terminology used in the Guide. To provide MSMEs with identity and visibility, the Guide sets out a simple vehicle for the entrepreneur to create a legally recognized business with its own legal personality. Limited liability protection for the members of the business entity and rules on the transfer of rights of its members are some of the mechanisms that provide certainty and protection for the property rights of MSME entrepreneurs. Finally, control by MSME entrepreneurs over the operation and management of their business is assured through an emphasis on management by the members of the business entity as the default governance approach and the horizontal organizational structure that characterizes the UNLLO.

13. At the same time, the Guide recognizes that the needs of micro entrepreneurs must be balanced against the needs of the State, creditors and other third parties doing business with them. Lack of transparency about the operations of the UNLLO could result in a lack of legal certainty that would undermine the effectiveness of this new legal form. The Guide therefore contains a number of provisions that cannot be derogated from by contractual agreement.

(c) Creating a stand-alone regime

14. The Guide also takes the view that the optimal solution for the creation of an appropriate simplified legal regime for MSMEs should not be to reform and simplify existing company law regimes, but rather to develop a separate legal regime that focuses on the needs of MSMEs. The structure envisioned in this text is thus neither dependent upon nor specifically linked to existing partnership, corporation or company law in any State.

15. One clear advantage of that approach is that it enables States to more easily adopt a regime that implements the recommendations of the Guide and permits them to craft appropriate legislative measures using a clean slate method. Furthermore, a separate legal regime for MSMEs can provide internationally recognized standards for the formation of simplified business entities, which would limit problems arising from the lack of international recognition of the legal form of the business thus facilitating cross-border transactions.

16. In pursuit of this approach to MSME law reform, the Guide does not rely on company, corporate or partnership law terminology and favours neutral terminology. Instead, the Guide sets out a new entity: the “UNCITRAL Limited Liability Organization (UNLLO)”.² The term is an indication that the business form created through the Guide’s recommendations is innovative and independent from existing company law regimes and their more prescriptive rules. The creation of the UNLLO aims to fulfil the desired goals and considerations outlined above.

17. In order to help micro entrepreneurs to craft their agreements on the structure and governance of the UNLLO, it would be desirable for States to clarify in their legislation prepared on the basis of this Guide which provisions can be derogated from by the UNLLO members (see para. 24 below). To assist States in this regard, the recommendations in the Guide identify those provisions with the phrase “unless otherwise agreed” or other similar phrases.

18. Finally, in developing legislation based on the Guide, States may consider introducing certain limits, such as maximum capital, annual turnover, number of employees, in order to avoid any abuse of the flexibility of the UNLLO form (see para. 7 above). Once such limits are exceeded, the legislation may provide for the conversion of the UNLLO into another legal form.

B. Terminology

19. The definitions provided below are intended to guide the reader and assist in ensuring that the concepts discussed in the Guide are clear and widely understood. It should be noted that whenever terms such as “data”, “documents”, “agreements”, “tax returns”, “financial statements”, “records” and other similar expressions are used, reference is intended to include both their electronic and paper versions unless otherwise indicated in the text.

- *Financial statement*: “Financial statement” means the report that presents information on the financial activities and conditions of the UNLLO.
- *Designated manager*: “Designated manager” means the person or one of the persons responsible for managing the UNLLO when the UNLLO is not managed by all of its members exclusively. A “designated manager” can be either a non-member or a member of the UNLLO.
- *Majority*: “Majority” means more than half of the UNLLO members determined by the number of the members.
- *Member(s)*: “Member(s)” means the owner(s) of the UNLLO (cf. “UNLLO”).
- *Organization rules*: “Organization rules” means the set of rules agreed by members and binding on all members on the formation and operation of the UNLLO and the rights and obligations of the members between themselves and the UNLLO.
- *Qualified majority*: “Qualified majority” means a percentage [*to be specified by the State*] of the UNLLO members by number that is greater than the threshold required for majority.
- *Restructuring*: “Restructuring” means modifying the structure or operation of the UNLLO through mergers, split-ups or other fundamental changes qualified as restructuring in domestic legislation.

² At its twenty-seventh session, the Working Group agreed to use the term “UNLLO” on an interim basis until it could decide on a preferred term to denote the simplified business entity being discussed (para. 43, [A/CN.9/895](#)).

- *UNCITRAL limited liability organization [UNLLO]*:³ “UNCITRAL limited liability organization [UNLLO]” means the legal business form with legal personality and limited liability protection for its members discussed in the Guide.

II. Formation and operation of the UNLLO

A. General provisions

(a) Legislative framework

20. Although the legal forms for businesses that are not publicly traded may vary from State to State, one of their characteristics is that they tend to function as independently as possible from the strict rules that govern publicly traded companies. For example, such businesses tend to receive waiver from the rules governing public companies in the form of simpler formation rules; nominal or no minimum capital requirement; greater freedom of contract; and fewer disclosure requirements.

21. For this reason (see also para. 14 above), rather than proposing adjustments or variations to the company structures that exist in most States, the Guide sets out recommendations for the enactment of legislation intended to be stand-alone and to provide for a legal business form which, while sharing some features of existing corporate forms, is distinct from them. Legislation enacted on the basis of the Guide would not operate independently from the legal tradition of the State. General principles of law would apply to fill any gaps.

(b) Flexibility through freedom of contract

22. As noted above (see paras. 2 and 3), to date the main focus of many legislative reforms to assist the creation of businesses that are not publicly traded has been on the creation of flexible legal business forms that permit the separation of the business assets of an entity from the personal assets of its members without resort to legal personality. This allows asset partitioning for MSMEs and their members by way of a legal structure that stops short of full limited liability and legal personality.

23. The UNLLO is intended to be added to the list of existing flexible business forms. The flexibility in business form has been achieved in part by allowing the UNLLO to be formed for a wide range of activities (see paras. 26 and 27 and rec. 2 below) and by recognizing the importance of freedom of contract for these businesses. In this respect, freedom of contract has been made the guiding principle in establishing the internal organization of the UNLLO (see paras. 61 and 62 below).

24. The Guide permits the members of the business to agree through contractual mechanisms (i.e., organization rules) on the internal governance of the enterprise, to derogate from certain requirements, and to tailor rights and obligations that are more consistent with the needs of smaller businesses (see para. 12 above).

25. However, the Guide also includes certain recommendations for provisions that cannot be derogated from by agreement between the members, as well as default provisions to fill any gaps in the organization rules. These default provisions can be particularly important for smaller or less-experienced entrepreneurs who may not foresee every eventuality required for the successful operation of the UNLLO.

³ The Commission may wish to note that the term “UNLLO” is defined only in order to facilitate consideration of these materials, in accordance with the Working Group decision that such term be used on an interim basis (see *supra* footnote 2).

Recommendation 1: The law should provide that an UNCITRAL Limited Liability Organization (“UNLLO”) is governed by this law⁴ and by the organization rules.

26. Recommendation 2 permits an UNLLO to be formed for any lawful business or commercial activity. A very broad approach is taken to the permitted activity of an UNLLO in order to provide maximum flexibility to the MSMEs that are anticipated to use this business form. In keeping with the traditional approach of UNCITRAL texts (for example, article 1(1) of the Model Law on International Commercial Arbitration and article 1 of the Model Law on Electronic Commerce), the Guide supports the view that States should give the terms “commercial” and “business” broad interpretation to avoid unwarranted narrowing of the permitted scope of the UNLLO. Moreover, the Guide follows the approach adopted by several legislative reforms of excluding the use of general purpose clauses so that business entities can engage in all lawful activities under domestic laws. The Guide thus leaves it open to the members of the UNLLO to decide whether or not they wish to include a more restrictive purpose clause in the organization rules. States requiring business entities to list all of their activities may wish to consider waiving that requirement for UNLLOs.

27. States wishing to prohibit an UNLLO from engaging in certain regulated industries, such as banking, microcredit and insurance industries, could enumerate the industries and activities in which an UNLLO may not engage. For additional clarity, States may expressly permit participation of the UNLLO in specific activities which might include activities in the agricultural, artisanal and cultural sectors.

Recommendation 2: The law should provide that an UNLLO may be formed for any lawful business or commercial activity.

28. The Guide recommends the granting of legal personality to the UNLLO in order for it to be a legal entity separate from its members. Legal personality in this context confers upon the UNLLO the legal rights and duties necessary for it to function within a legal system, including the ability to acquire rights and assume obligations in its own name.

29. Legal personality provides a means through which the UNLLO’s assets can be separated from the personal assets of its members, a process which has been referred to as affirmative asset partitioning. A distinct legal personality permits the UNLLO to be shielded from potential claims by the personal creditors of its members. Conversely the personal assets of the UNLLO members are protected in the event that the UNLLO is unable to satisfy its debts or meet its obligations or becomes involved in legal disputes. Providing for the separation of the UNLLO assets from the personal assets of its members through legal personality of the organization and limited liability protection for its members (see rec. 4) is a fundamental aspect of the structure of the UNLLO.

30. As noted above (see para. 5), domestic taxation policy in respect of the legal form of an UNLLO is not considered in the Guide and is left to other applicable laws of the State.

Recommendation 3: The law should provide that the UNLLO has a legal personality distinct from its members.

31. Recommendation 4 states one of the essential consequences of conferring legal personality to a business, which is that the members of the UNLLO are not personally

⁴ The term “this law” refers to the domestic legislation that will be enacted on the basis of this Legislative Guide (the “Guide”).

liable for the obligations and debts of the UNLLO. As such, the recommendation includes a provision that cannot be derogated from by the members of the UNLLO.

32. Limited liability permits entrepreneurs to take business decisions without concern that they may jeopardize their personal assets if the business entity does not perform well or becomes involved in legal disputes. This is important both for the protection of the members of the organization and for the promotion of innovation and business creation, as it allows entrepreneurs to take business risks without fear of being personally liable for the possible failure of the organization. However, members of many MSMEs do not currently enjoy the benefits of limited liability protection. In some States, limited liability protection is not offered to MSMEs' members because of concerns that it would encourage opportunism by the entrepreneurs and provide insufficient protection for third parties dealing with the MSME. Other States, however, grant members of MSMEs access to limited liability protection, since this is considered to promote entrepreneurship and facilitate capital formation. As such, and in order to offer this important and attractive feature to such economic actors, the legislative regime establishing the UNLLO offers limited liability protection to UNLLO members.

33. The presence of such a liability shield generally protects the members of an UNLLO from incurring direct or indirect personal liability as a result of the activities of the UNLLO. In effect, the financial liability of a member of the UNLLO is limited to a fixed sum, usually the value of the member's contribution to the UNLLO. As noted above (see paras. 28 and 29), limited liability of members and distinct legal personality of the organization often go hand in hand (see rec. 3). Granting both attributes to the UNLLO will assist in promoting the stability of the organization and access by it to lower cost credit.

34. The UNLLO itself is liable to its general creditors and all of the assets of the UNLLO are available to satisfy those claims. In addition, it is important to note that the limitation on the liability of a member for the obligations of the UNLLO refers to liability that results solely from that person's status as a member of the UNLLO. Members of the UNLLO may still have personal liability for personal tort or for example, a member may be liable for a personal guarantee given in respect of the obligations of the UNLLO.

35. Notably, a contract entered into with a third party before the formation of the UNLLO (see rec. 8) may also give rise to personal liability of the members or managers of the UNLLO who entered into that contract. In certain States, the law may permit the UNLLO to take over all or some of the obligations incurred by the founding members on its behalf before its formation.

36. Of course, it will remain open for courts to lift the limited liability protection and impose personal liability on members and managers in cases of fraud, misuse of the legal personality of the UNLLO or other wrongful acts committed in the name of the UNLLO. Such abuse of the UNLLO legal form could arise, for example, where a member makes use of UNLLO assets as though they were that member's personal assets.

37. It is, therefore, important to avoid confusion between personal assets of the members and business assets of the UNLLO. The Guide recognizes, however, that it may be difficult for a micro or small UNLLO to segregate its assets from those of its members, in particular when the UNLLO has only one member. It would thus be important for States to clearly address the issue of separation of personal and business assets in their laws, for example by requiring the UNLLO (in particular single-member UNLLOs) to set up a bank account separate from those of its members.

Recommendation 4: The law should provide that a member is not personally liable for the obligations of the UNLLO solely by reason of being a member of that UNLLO.

38. Some States maintain the view that a minimum capital requirement is a reasonable *quid pro quo* for members of a business that is not publicly traded to receive the benefit of limited liability. However, many of those States have significantly reduced minimum capital requirements for these businesses to nominal or initially low but progressively increasing amounts. It has been suggested that even in a nominal or progressive form, minimum capital requirements can be conducive to business growth, since they function not only to protect third parties, but also to assist in terms of the soundness, effectiveness and productivity of the business and provide information in respect of financial and decision-making rights. On the other hand, concerns have been raised that capital requirements, including progressive capital requirements, could have a negative impact upon small start-up enterprises. The first three years of an enterprise's life cycle are the most critical and yet it would be required to progressively build up its reserves during that period in spite of possible financial fragility. Moreover, since the minimum capital required to create a business, along with the accounting rules of the required capitalization, is often one of the most important considerations for new businesses, its elimination may be a factor that can positively affect the rate of formation of business entities. Further, as a matter of State policy, one particular problem related to establishing minimum capital requirements is the difficulty of quantifying an appropriate amount, and the rigidity inherent in making such a choice.

39. The issue of minimum capital requirements should be dealt with in the context of general mechanisms for the protection of creditors and other third parties dealing with the UNLLO. The more important of such mechanisms are included in the Guide as provisions that cannot be derogated from by the UNLLO members, while others may be found elsewhere in a State's legislative framework. These mechanisms include:

(a) Making members of the UNLLO liable for improper distributions and obligating them to repay the UNLLO for any such distributions (see recs. 23 and 24, which include provisions that members cannot derogate from);

(b) Prescribing standards of conduct, including good faith and fiduciary responsibilities (see rec. 20, which includes a provision that members cannot derogate from);

(c) Requiring transparency and accessibility in the keeping and sharing of UNLLO records and information (see recs. 30 and 31, which include provisions that members cannot derogate from);

(d) Requiring that the entity's business name contain an indicator of its limited liability status (for example, "UNLLO") and that its name be set out in contracts, invoices and other dealings with third parties (see rec. 6, which includes a provision that members cannot derogate from);

(e) Permitting exceptions to the limited liability protection of members of the UNLLO in certain circumstances (see para. 36 above);

(f) Establishing requirements in respect of the transparency, quality and public availability of registered information on the UNLLO and its managers (this could be expected to be a function of the business registry law of a State);⁵

(g) Establishing a supervisory role for commercial registries or specialized agencies (this could also be expected to be a function of the business registry law of the State);

(h) Establishing credit bureaux (this would be a policy decision of the State); and

(i) Requiring corporate governance oversight (this would be a policy decision of the State).

⁵ See the UNCITRAL Business Registry Guide for relevant recommendations.

40. In keeping with the nature of the UNLLO as a legal form to assist MSMEs, as well as several legislative reforms that have replaced the minimal capital requirement with other mechanisms to protect third parties dealing with the MSME, the Guide does not recommend a minimum capital requirement for the formation of an UNLLO. As noted above, the main mechanisms included in the Guide to protect third parties dealing with the UNLLO are the provisions in recommendations 6, 20, 23, 24, 30 and 31, which members cannot derogate from as outlined in subparagraphs 39 (a) to (d).

41. Even where a State has policy reasons (other than the protection of third parties) to require a minimum capital, the Guide recommends against imposing such a requirement on the UNLLO, even if the amount is nominal or progressively increasing. Instead, other mechanisms may be considered, such as the establishment of a maximum size (for example, based upon the number of employees) or level of profitability of the UNLLO, which could then be required to convert to another legal form (for which the State might require minimum capital) upon exceeding that maximum. It should be noted, however, that these other mechanisms could unnecessarily restrict the growth of UNLLOs.

Recommendation 5: The law should not require a minimum capital for the formation of an UNLLO.

42. In order to signal to third parties that they may be dealing with an UNLLO, the law should require the name of the UNLLO to include a phrase or abbreviation (such as “UNLLO”)⁶ that would enable it to be distinguished from other types of businesses. The use of the same or a similar phrase or abbreviation in different States would assist UNLLOs engaging in cross-border trade as the defining characteristics of the entity would be immediately ascertainable upon recognition of the phrase or abbreviation, even in the cross-border context. Since the UNLLO is proposed as a legal form specifically tailored to MSMEs in addition to existing models, it is best identified by a phrase or abbreviation that is independent from the local legal context.⁷

43. Some States may wish to require the UNLLO to use its distinctive phrase or abbreviation in all correspondence with third parties in order to signal its legal personality. Courts will rule on the appropriate imposition of sanctions for failure to do so on the basis of the facts and circumstances of the case, and according to the law. While States may decide not to make it mandatory for the UNLLO to use this distinctive phrase or abbreviation in its business dealings in order to enhance legal certainty, they should encourage UNLLOs to use it as much as possible. Practically speaking, since the distinctive phrase or abbreviation forms part of the name of the UNLLO, it would likely be included in all correspondence involving the UNLLO, in any event.

44. In terms of the name chosen for the UNLLO, all mandatory requirements concerning registration (and approval) of company names in the jurisdiction in which the UNLLO is doing business will have to be satisfied.

Recommendation 6: The law should provide that the name of the UNLLO must include a phrase or abbreviation that identifies it as an UNLLO.

B. Formation of the UNLLO

45. The Guide recommends permitting the formation and operation of an UNLLO by a sole member, including an individual entrepreneur engaged in relatively simple business activities, or multiple members. This permits the UNLLO to evolve from a single-member entity to a more complex multi-member one. In order to protect creditors and third parties dealing with the UNLLO and to provide legal certainty,

⁶ In keeping with footnotes 2 and 3, *supra*, the term “(“UNLLO”)” is used here by way of example.

⁷ In light of the discussion in the commentary to rec. 6, the Commission may wish to agree on a suggested unified phrase or abbreviation to be used for the identification of the UNLLO.

recommendation 7(a) establishes that an UNLLO should have at least one member at all times (see also para. 136). As an additional feature to enhance the flexibility of the UNLLO, the recommendation does not specify a maximum number of members for the UNLLO.

46. An important issue for States to consider in the legislation establishing the UNLLO is whether a member of an UNLLO may be a legal person or whether only natural persons are permitted to be members. When a legal person is permitted to be a member of the UNLLO, it is desirable that States ensure a wide understanding of the concept of “legal person”, which should include any entity that has been granted a legal personality. Permitting a legal person to be a member of an UNLLO may facilitate the transition of the UNLLO to a more sophisticated type of business. Moreover, it may help the UNLLO access greater resources (monetary, technological, and skill sets) and new markets, as well as build credibility. This will be valuable not only for UNLLOs operating in States with lower levels of infrastructure, but also for UNLLOs aiming to expand their activities in the domestic market and abroad.

47. However, States may wish to limit participation in an UNLLO to natural persons only, particularly in the case of a single-member UNLLO. Permitting a legal person to be a single-member of an UNLLO might give rise to concerns about the possible misuse of the UNLLO, for risk of money-laundering, fraud or other illicit behaviour. If legal persons are permitted to be members of UNLLOs, States should introduce appropriate safeguards to prevent those illicit activities. For example, they could establish that only natural persons can be involved in the UNLLO management (see para. 89), or that a legal person might acquire member status only in a multi-member UNLLO where the other members are natural persons. These measures may prevent the creation of an UNLLO without active business operations (a “shell organization”).

48. In light of the above considerations, recommendation 7(b) invites States, when enacting legislation based on this Guide, to specify whether an UNLLO may only have natural persons as members. The phrase “the extent to which legal persons are permitted” in recommendation 7(b) allows States to set forth the limitations (if any) on legal persons becoming members of an UNLLO.

49. The Guide acknowledges that the ability of an UNLLO itself to become a member of another UNLLO or legal person or otherwise be involved in the formation thereof largely depends on the legal tradition and domestic needs of a State. The Guide thus leaves it to States to impose restrictions, if any, on the type of investments that an UNLLO can make.

Recommendation 7: The law should:

(a) Provide that an UNLLO must have at least one member from the time of its formation until its dissolution; and

(b) Specify whether an UNLLO may only have natural persons as members and if not, the extent to which legal persons are permitted.

50. In order to provide legal certainty as to when the UNLLO comes into existence, the Guide recommends that an UNLLO should be formed once it is registered with the business registry. Through formation, the UNLLO acquires its essential attributes, including its legal personality, and limited liability for its members. As noted above (see para. 35), the law of certain States may permit a registered UNLLO to take over all or some of the obligations incurred by the founding members on its behalf before its formation.

51. In the interest of predictability and transparency of registration, it is highly desirable that States specify the moment at which the registration of the business is effective.⁸ In keeping with international best practices, as outlined in the UNCITRAL Legislative Guide on Key Principles of a Business Registry (the “UNCITRAL

⁸ See the UNCITRAL Business Registry Guide, para. 142 ff.

Business Registry Guide”), States may wish to specify when the legal existence is conferred upon the UNLLO, which, for example, can be (a) at the time of the entry of the information on business registration into the registry record, (b) when the application for registration is received by the registry or (c) upon issuance of a certificate confirming the registration.

52. Regardless of the system used to register an UNLLO (electronic, paper-based or a mixed business registry), upon fulfilling the applicable requirements, the UNLLO should receive a notice of registration from the designated State authority. In keeping with the recommendations of the UNCITRAL Business Registry Guide and in order to accommodate the simple nature of the UNLLO, issuance of the notice of registration should be as fast and as streamlined as possible.

Recommendation 8: The law should provide that the UNLLO is formed once it is registered.

53. Depending on the type of business entity being created, States typically require different types and a varying level of detail for business formation. Consistent with the intended simplicity of the UNLLO, the information required for the formation of the UNLLO should be limited to the minimum necessary for its formation and operation, as well as for the protection of third parties. In addition, recommendation 9 respects the principle that it should be as simple as possible for an MSME to provide the required information to the business registry so as to avoid creating unnecessary burdens and to encourage compliance with the law.

54. The minimum information necessary for the formation of the UNLLO pursuant to recommendation 9 includes the name of the UNLLO as well as the address at which the business is to be deemed to receive correspondence. Where the business does not have a standard form address, a precise description of its geographic location should be provided instead of the business address. The business address or geographic location of the UNLLO would be used for service or mailing purposes. The Guide does not require evidence of a member’s identity for the formation of the UNLLO, but in keeping with standard practice (see also the UNCITRAL Business Registry Guide), it requires evidence of the identity of the person(s) that submit(s) the prescribed application form and documents to the business registry.

55. In addition, the Guide requires evidence of the identity of each person who manages the business. If the business is managed by all of its members exclusively (see paras. 81 and 82), the effect of recommendation 9(a)(iv) will be that the information on the identity of each member must be included. If the business is managed by one or more designated managers, only information on the identity of each designated manager must be included, whether or not the managers are members of the UNLLO. Requiring the UNLLO to disclose the identity of each person managing the business provides greater transparency to State authorities and third parties dealing with the UNLLO. For these reasons, the approach in recommendation 9(a)(iv) differs from that of the Business Registry Guide (rec. 21(d)), which requires information on the business’s legal representatives or those authorized to sign for the business to make third parties aware of any limitations in the managers’ authority. This Guide ensures protection of third parties through other mechanisms such as recommendation 19(b) pursuant to which restrictions upon the authority of an UNLLO manager will not be effective against third parties without proper notice. Information on the residential address of each manager is not required for the formation of the UNLLO since this information is not essential for the protection of third parties. For that purpose, as well as for the State monitoring of the UNLLO management, the business address of the UNLLO should be sufficient. Moreover, the business address of the UNLLO can also function as the official correspondence address of the persons managing the UNLLO.

56. Finally, the Guide recommends that information for the formation of the business should include the UNLLO's unique identifier⁹ if that identifier has already been assigned. A unique identifier greatly simplifies the formation and operation of the business since entrepreneurs do not have to manage different identifiers from different authorities nor are they required to provide the same or similar information to different authorities.

57. Depending on the domestic context and legal tradition, States might require other information in addition to that listed in recommendation 9. For example, information on the identity of the founding members of the UNLLO, the members' rights in the UNLLO, the authority to represent it and any limitations on the power of managers to bind the UNLLO might be considered of particular relevance by some States for the valid formation of an UNLLO. In the case of micro and small businesses, as most UNLLOs would be, States, however, should remain mindful that requesting complex and extensive information may discourage a business from registering. States may also leave it open to the UNLLO to include any additional information deemed appropriate, in particular if such information can assist it in accessing credit or attracting investors.

58. The Guide does not require that information on beneficial ownership be made public, as the information requirements under recommendation 9, although of limited scope, should be sufficient to meet international standards on disclosure of beneficial ownership¹⁰ (see also rec. 30). These information requirements should thus assuage any concerns that the UNLLO legal form could be misused for illicit purposes, including money-laundering and terrorist financing. Such an approach also strikes an appropriate regulatory balance, since it provides sufficient legal and commercial certainty for the State and for the protection of third parties dealing with the UNLLO.

59. Regardless of the different types and amounts of information to be submitted for formation, States may wish to ensure that their business registration law requires any changes to information initially required pursuant to recommendation 9 to be updated with the business registry. Recommended methods for keeping information current are set forth in the UNCITRAL Business Registry Guide.

60. For transparency and the protection of third parties, most States provide that all registered information should be publicly available unless it is protected by the law. Consistent with this approach, the Guide takes the view that the information required for the formation of the UNLLO should be publicly available. That information would at least include the requirements listed in recommendation 9 below and any other requirements that should be made public pursuant to domestic laws (see also para. 142). Since the UNLLO must be registered in order to be formed, that information will be disclosed through publication on the business registry.

⁹ A unique identifier is a single unique business identification number that is allocated only once to businesses and can be used in all interactions of the business with public authorities, other businesses and banks (see the Terminology section in the Business Registry Guide).

¹⁰ Financial Action Task Force (FATF) Recommendation 24 in respect of transparency and beneficial ownership of legal persons encourages States to conduct comprehensive risk assessments of legal persons and to ensure that all companies are registered in a publicly available company registry. The basic information required is: (a) the company name; (b) proof of incorporation; (c) legal form and status; (d) the address of the registered office; (e) its basic regulating powers; and (f) a list of directors. In addition, companies are required to keep a record of their shareholders or members. See International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation: The FATF Recommendations, Part E on Transparency and Beneficial Ownership of Legal Persons and Arrangements (www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%202012.pdf). In addition, it should be recalled that business entities, in order to conduct activities, usually must open bank accounts that require the submission of taxation and other identification numbers, and financial institutions may remain the most suitable parties to prevent and combat money-laundering and other illicit activities.

Recommendation 9: The law should:

(a) Require the following information and supporting documents for the registration of the UNLLO:

- (i) The name of the UNLLO;**
- (ii) The business address or, when the business does not have a standard form address precise geographical location of the UNLLO;**
- (iii) The identity of the registrant(s);**
- (iv) The identity of each person who manages the UNLLO; and**
- (v) Its unique identifier, if such an identifier has already been assigned; and**
- (b) Keep additional information required, if any, to a minimum.**

C. Organization of the UNLLO

61. As noted above in respect of recommendation 1 (see paras. 23 and 24), freedom of contract should be the guiding principle in establishing the internal organization of the UNLLO. As a consequence of that principle, the operation of the UNLLO is governed by the agreement of its members, except for certain aspects governed by provisions that cannot be derogated from by the members. Such provisions are those that establish the necessary legal framework of the UNLLO and provide legal certainty, or those that are necessary to protect the rights of the UNLLO and of third parties dealing with it. When the organization rules are silent on an issue that can be derogated from, the default provisions in the Guide are intended to fill any gap.

62. In order to help members manage the UNLLO fairly, effectively and transparently, States may wish to provide model rules that members may use, where appropriate, on the following issues:

(a) Maintenance of timely records of the members' decisions as well as the form in which those records should be maintained;

(b) Any requirement in respect of members' meetings, including:

(i) Their frequency and location, as well as any limitation thereon;

(ii) Any requirement regarding who can call a meeting;

(iii) The means by which a meeting may be held, including whether it may be held by technological means or by written consent;

(iv) Any notice period required prior to the holding of a meeting;

(v) The form of any notice required for a meeting (for example, whether it must be in writing), and the information (if any) that should be attached to the notice (for example, the UNLLO's financial information); and

(vi) Whether waiver of any required notice is permitted and the form that waiver may take;

(c) Any deviations from the default decision-making requirements in recommendations 13 and 15; and

(d) Mechanisms to resolve situations in which a decision cannot be reached (for example, granting certain member(s) more voting power in case of a tie or referring the matter to an internal or external "tie-breaker"), whether the decision falls within the purview of the managers or the members. If a status quo cannot be maintained, failure to provide such mechanisms may result in disputes and require submission to alternative dispute resolution (see paras. 145 and 146 and rec. 32).

63. The organization rules should be agreed upon by all members of the UNLLO (see para. 72 (a) and rec. 12(a)) and may not contradict the provisions of the State's legislation enacted on the basis of the Guide which cannot be derogated from or other domestic laws that apply to the UNLLO. Further, the organization rules should be consistent and coherent in order to ensure the smooth management of the UNLLO.

64. The Guide leaves States the option to permit the members of the UNLLO to establish some or all organization rules orally or through a course of conduct, or to require the members to record their organization rules, whether in writing or in electronic form or by any other appropriate technological means. Broad flexibility for the form of the organization rules recognizes that, because of legal tradition in many States, MSMEs may have no formal written agreement on the organization rules, and that, in such cases, States may wish to enable members to rely on other agreement forms.

65. It may be in the best interests of members to record the organization rules of the UNLLO, since oral agreements and agreements implied by conduct are more difficult to prove in the event of a dispute. In addition, when amendments by conduct to recorded organization rules occur in practice, States would need to rely on other laws for resolution of the evidentiary disputes which may arise.

66. A requirement for an UNLLO to document its rules would assist in record-keeping, and provide evidence of the internal governance for creditors and other interested third parties to make informed decisions about who they wish to do business with. These advantages would apply equally to single-member and multi-member UNLLOs. Recorded organization rules would further mitigate the risk that the UNLLO be misused for illicit purposes, such as money-laundering.

67. However, States that consider requiring recorded organization rules should balance the need for transparency and traceability of UNLLO's operations against the cost imposed on the members, and should take into account factors such as technological and financial capabilities, literacy rates, and model forms.

68. The Guide does not require that an UNLLO's organization rules be made public. This approach protects the privacy of members and adds to the ease of the UNLLO's operations by avoiding the need to file amendments with the business registry or other public authority each time a change is made to the organization rules (see para. 59). States may, however, decide to require the UNLLO to disclose its organization rules to increase accountability and transparency of the UNLLO, or the UNLLO itself might decide to make them available to the public in order to strengthen its reputation on the market. When an UNLLO's organization rules include provisions that modify the default provisions applicable to the UNLLO, notice of such changes to third parties is required in order to be effective against them (see para. 94 and rec. 19(b)). To accommodate the different legal tradition and practices of the States, the Guide leaves States the option to decide how that information should be disclosed to the third parties.

Recommendation 10: The law should:

- (a) Specify the allowable forms of the organization rules; and**
- (b) Provide that the organization rules may address any matters relating to the UNLLO subject to the law.**

D. Members' rights and decision-making in the UNLLO

69. In keeping with the intended simplicity of the UNLLO form, the Guide leaves to members to determine how to acquire member status and it sets out a default provision in recommendation 11 that the members have equal rights in the UNLLO irrespective of their contribution (see also paras. 101 to 105). Members may vary this default provision, but they should record their agreement in the organization rules, as the change will affect core aspects of the structure and governance of the UNLLO.

70. Members of an UNLLO can exercise certain rights regardless of whether or not they manage the UNLLO. Those rights include: rights to make decisions on certain aspects of the UNLLO, rights to receive distributions during the existence (paras. 106 and 107) and after dissolution and liquidation of the business (see paras. 134 to 139), rights to receive information on the operation of the UNLLO and its financial status and to inspect the UNLLO records (see paras. 143 and 144 and recs. 30 and 31). Members may also bring derivative actions on behalf of the UNLLO (see para. 97) to protect it against illicit behaviour of the managers or members.

71. UNLLO members must also comply with certain obligations. They must make the agreed contributions to the UNLLO, if any, and reimburse any improper distribution made to them by the UNLLO (recs. 23 and 24). As noted above (see para. 36), members should also refrain from any abuse of the UNLLO legal form and any other rights granted to them. These are the minimum obligations required of members, in order to ensure the regular operations of the UNLLO. Members are, however, free to establish additional obligations in their organization rules consistent with the features of the business.

Recommendation 11: The law should establish that unless otherwise agreed in the organization rules, members have equal rights in the UNLLO irrespective of their contributions, if any.

72. With regard to decision-making rights, the Guide recommends that, at a minimum, the members retain authority on the following matters that affect the structure or existence of the UNLLO:

- (a) Adoption and any amendment of the organization rules (rec. 12);
- (b) Conversion or restructuring of the UNLLO (rec. 27); and
- (c) Dissolution of the UNLLO (rec. 28(a) and (b)).

73. Decisions concerning the adoption and amendment of the organization rules in subparagraph (a) above should address core aspects of the governance of the UNLLO such as: its management structure and any modifications (recs. 14 and 16); determination of the members' contribution to the UNLLO, if any (rec. 21) and allocation of their rights in the UNLLO if these are not equal.

74. When an UNLLO is managed by all of its members exclusively (see rec. 15) it would be necessary to differentiate the decisions made as members from the managerial decisions, since the former would usually require a higher decision-making quantum.

75. The list of matters in paragraphs 72 and 73 above is not exhaustive and the Guide leaves States the option to include additional matters to better accommodate their domestic policies and legal tradition. Consistent with the principle of freedom of contract that is at the basis of the UNLLO, the Guide also permits the members to include in the organization rules additional matters over which they would retain decision-making authority (see rec. 13). In this regard, the members may choose to include the admission of new members as a matter reserved to their decision by unanimity so as to avoid potential conflict among themselves in such cases. The organization rules could also set forth the conditions for the admission of new members, for example their contributions to the UNLLO if any (see paras. 101 and 102), and their rights and obligations, if not equal. Finally, members may specify in the organization rules how their rights could be exercised in the event of permanent incapacitation or disability of a member, as long as the rules are in compliance with the domestic laws on this issue (see also para. 121 below).

Recommendation 12: The law should:

Specify the decisions on the UNLLO to be reserved to the members, which, at a minimum, should include decisions on:

- (a) Adoption and amendment of the organization rules, in particular:**
 - (i) Management structure of the UNLLO and its modification;**
 - (ii) Allocation of rights of the members in the UNLLO if not equal; and**
 - (iii) Member's contributions;**
- (b) Conversion and restructuring; and**
- (c) Dissolution.**

76. Since the matters indicated in recommendation 12 are essential for the existence and operation of the UNLLO, recommendation 13(a) provides that decisions on those matters should require the unanimous consent of the members, unless they have agreed otherwise in the organization rules. This decision-making system may be particularly suitable for an UNLLO as it is fair, straightforward, gives equal weight to all members and encourages the members to find a compromise when disagreement arises. In practice, however, requiring unanimity gives dissenting members the power to veto any decision, thus affecting the ability of the UNLLO to operate effectively and efficiently. For this reason, recommendation 13(b) suggests that decisions on matters that are not essential for the existence of the UNLLO should be taken by a majority of members by number. This system will also allow the members to resolve their differences on the daily operations of the UNLLO more expeditiously.

77. Although the Guide has taken the approach that unanimity should be required for decisions that affect the existence and operation of an UNLLO, the legal tradition in some States may not require unanimous consent on such matters. Furthermore, as noted above (see para. 76), the dissatisfaction of one UNLLO member may present challenges for the effective governance of the business operations. States may therefore decide to deviate from recommendation 13 and create a standard that only requires a qualified majority to take the decisions listed in the recommendation. Legislation prepared on the basis of the Guide should clearly indicate the quantum necessary for any decisions that depart from those listed in recommendation 13.

Recommendation 13: The law should specify that unless otherwise agreed in the organization rules:

- (a) Decisions concerning the UNLLO which are reserved to the members under recommendation 12 are to be taken by unanimity; and**
- (b) Any other decisions which are reserved to the members pursuant to the organization rules are to be taken by majority.**

E. Management of the UNLLO

78. An UNLLO will likely have a relatively small number of members, and those members will be interested in substantial participation in the management and operation of the business. Appointing a non-member manager (which is common in publicly traded companies) to administer the UNLLO may not fit the governance needs of the members, particularly when the UNLLO is a micro or small business. Recommendation 14 thus makes an UNLLO managed by all of its members exclusively the default approach.

79. However, the default rule may not be suitable for every UNLLO. For example, there may be instances where a member is not willing or eligible to serve as a manager. Therefore, recommendation 14 permits members of an UNLLO to agree to a management structure where not all members act as managers. In such instances,

the UNLLO will be managed by one or more designated managers. Alternative management structures may involve management by: (i) only some of the UNLLO members; (ii) only non-member managers; (iii) a combination of some of the UNLLO members and non-member manager(s); or (iv) all of the UNLLO members and non-member manager(s). Designated managers will manage the day-to-day operations of the UNLLO pursuant to recommendation 17. Recommendation 14 only applies to the deviations from the default rule on the UNLLO's management (para. 78) by members' agreement. The Guide leaves to domestic laws to specify alternative management structures when not all members are eligible to serve as managers.

80. Where there is only one member of an UNLLO, that member will be the manager, unless that member designates someone else as a manager.

Recommendation 14: The law should provide that the UNLLO is managed by all of its members exclusively, unless members agree in the organization rules that one or more designated managers shall be appointed.

1. When the UNLLO is managed by all of its members exclusively

81. When the UNLLO is managed by all of its members exclusively, the members will have equal management powers and decision-making rights on matters concerning day-to-day operations of the UNLLO, unless they agree otherwise in the organization rules.

82. Furthermore, unless there is agreement to the contrary, differences that arise between members as to managerial decisions would be resolved by a majority of the members. Such decisions would likely include: opening and closing bank accounts, disposing of certain assets owned by the UNLLO, accessing credit for the UNLLO, buying and selling equipment and hiring employees. As noted above (see paras. 72, 73 and 75), decisions that affect the UNLLO's existence or structure would not be considered managerial in nature, and would therefore require the approval by the members in their capacity as members (see recs. 12 and 13).

83. In this regard, it should be noted that the removal of management duties of one member in an UNLLO managed by all of its members exclusively is a non-managerial decision, as it would affect the management structure of the UNLLO. Such a decision would thus be taken by the members in their capacity as members (see paras. 72 and 84). The member whose management duties have been removed would retain the right to participate in decision-making as a member (see rec. 12).

84. As a practical matter, in an UNLLO managed by all of its members exclusively, it might be difficult to differentiate managerial decisions from those made as members (see also para. 74). Recommendation 12 therefore presents a list of decisions that require member action, whereas recommendation 15 reflects the default approach to managerial decision-making of the members in an UNLLO managed by all of its members exclusively.

Recommendation 15: The law should provide that when the UNLLO is managed by all of its members exclusively and unless otherwise agreed in the organization rules, differences among members on matters concerning day-to-day operations of the UNLLO should be resolved by a majority decision of the members.

2. When the UNLLO is managed by one or more designated managers

85. As noted above (see para. 79), members of an UNLLO may agree on a management structure that differs from the default provided for in recommendation 14. When members agree on an alternative management structure, the organization rules should include rules for the appointment and removal of a designated manager. In the absence of such rules, recommendation 16 provides that such decisions should be made by a majority of the members. A designated manager

could be a member of the UNLLO, provided that it is not managed by all of the members exclusively.

86. Should a designated manager become unavailable (through death or otherwise), the members could be required to appoint another designated manager under the terms of the organization rules. Some States might require the identity of the designated manager to be provided to the business registry (see para. 59). Appointing another designated manager could be important to ensure continuity of the regular operations of the UNLLO.

Recommendation 16: The law should provide that, when the UNLLO is not managed by all of its members exclusively, designated manager(s) may be appointed and removed by a majority decision of the members, unless otherwise agreed in the organization rules.

87. As noted above (see paras. 70, 72 and 73), even when members of the UNLLO appoint one or more designated managers to manage the business, members will still retain the authority to decide on certain matters that are outside the daily operation of the business and may affect its existence, structure or the members' rights and obligations. The Guide enumerates certain matters that should be decided by the members. To facilitate the operation of the UNLLO, it would be desirable for the organization rules to specify all other matters, if any, that are retained for decision-making by members (see para. 75). Typical managerial decisions are described in paragraph 82 above, but the Guide takes the view that when the organization rules are silent, the default provision of recommendation 17(a) will apply, which provides designated managers with the authority to make decisions independent of involvement of the members.

88. The organization rules should also determine how disputes among designated managers on matters within their authority should be resolved. In the absence of such rules, recommendation 17(b) provides that disputes should be decided by a majority of the managers. The recommendation, however, does not address any deadlock that might occur when an equal number of managers fail to reach a decision. As noted above (see para. 62 (d)), it is desirable that criteria to resolve situations in which a decision cannot be made should be included in the organization rules.

Recommendation 17: The law should provide that when the UNLLO is managed by one or more designated manager(s):

(a) Such managers are responsible for all matters that are not reserved to the members of the UNLLO pursuant to this law¹¹ and, where applicable, to the organization rules; and

(b) Disputes among themselves should be resolved by a majority decision of the managers, unless otherwise agreed in the organization rules.

3. Provisions applicable to all persons in a management position regardless of the management structure of the UNLLO

89. The persons who manage an UNLLO, regardless of whether the UNLLO is managed by all of its members exclusively or by one or more designated managers, must meet the legal requirements (e.g., minimum age, absence of disqualification) established under the domestic law of the State for those in a management role. Recommendation 18 leaves to the States to decide what such legal requirements should be. If the domestic law (in particular company law) is silent about the legal requirements for those in a management position, it is advisable for States to specify such requirements in the legislation enacted on the basis of this Guide. In this respect,

¹¹ The term "this law" refers to the legislation that will be enacted on the basis of the Guide.

the law should also specify whether a legal entity that is a member of an UNLLO can be involved in its management (see para. 47).

90. In legal systems where there is no prohibition on management by legal persons, there may still exist requirements and restrictions: legal persons may be required to name in turn a natural person to deal with matters concerning day-to-day operations on their behalf; there may always have to be at least one natural person in the management; and different details may need to be disclosed and filed for legal persons managing an UNLLO.

91. In addition to the requirements of the applicable law, the organization rules may prescribe other qualifications for those managing an UNLLO.

Recommendation 18: The law should provide that persons who manage the UNLLO shall meet the legal requirements for those in a management position.

92. Regardless of whether an UNLLO is managed by all of its members exclusively or by one or more designated managers, the Guide applies certain provisions, such as the power to act on behalf of the UNLLO and fiduciary duties, to all managers. This approach is reflected in recommendations 19 and 20. For additional clarity, it should be noted that the term “manager” as used in those recommendations and the related commentary (see paras. 92 to 98, 113 and 144) applies to all those in a management position, regardless of whether they are members or non-member managers.

93. Each manager of the UNLLO has the authority to act on behalf of the UNLLO and legally bind it. Restrictions may be agreed upon in the organization rules in respect of the extent of each manager’s authority to bind the UNLLO (for example, only up to a certain monetary threshold), or to vary the default provision that each manager has the authority to legally bind the UNLLO. Such modifications of the default provisions will be effective between the members of the UNLLO.

94. However, such restrictions or variations will not be effective against third parties dealing with the UNLLO unless those third parties have notice of that restriction or variation of the manager’s authority. If third parties dealing with the UNLLO do not have notice of any limitation that the organization rules have placed on the authority of a manager, the UNLLO will nonetheless be bound by a decision of that manager, regardless of whether that decision exceeds the manager’s authority as limited by the organization rules. The Guide leaves to States to determine how notice to third parties should be provided (in this regard, see also para. 68), including dealing with knowledge of third parties of any restriction or variation of a manager’s authority.

Recommendation 19: The law should provide that:

(a) Every manager has the authority to bind the UNLLO, unless otherwise agreed in the organization rules; and

(b) Restrictions upon such authority will not be effective against third parties dealing with the UNLLO without proper notice.

95. The authority of any manager to represent and bind the UNLLO must be contained in a manner that reduces the risk of managers acting opportunistically and encourages them to promote the welfare of the UNLLO and, indirectly, its members. Fiduciary duties offer protection against a manager’s pursuit of personal interest and any grossly negligent behaviour on its part. Such duties may be separated into a duty of care and a duty of loyalty, including a duty to refrain from self-dealing transactions, personal use of business assets, usurpation of business opportunities, and competition with the UNLLO. The inclusion of such duties tends to be a standard feature of business associations law; for example, fiduciary duties are found in many of the simplified corporate forms resulting from States’ reforms in this domain. The Guide notes that States may have an understanding of fiduciary duties that range beyond the duties listed in recommendation 20. It would be up for the State to decide to include

additional duties, including creating fiduciary duties to the UNLLO of members who are not managers.

96. A claim for breach of fiduciary duty is a serious matter and should not be too easily available as means to challenge ordinary business decisions. Managers who, in the performance of their official duties, make a good faith decision they believe to be in the best interest of the UNLLO should not be exposed to liability for breach of fiduciary duties merely due to disagreement with their business judgment.

97. Legal claims against managers in breach of their fiduciary duties may be brought directly before a court or by way of an alternative dispute settlement mechanism (see rec. 32). Generally,¹² it will be the UNLLO itself, rather than an individual member acting as a manager, that would have a cause of action for a breach of a fiduciary duty by a member or manager. Ordinarily, managers would be responsible for bringing an action on behalf of the UNLLO. However, in instances in which a manager has breached its own fiduciary duty, a member should have the right to bring a derivative claim on behalf of the UNLLO. In doing so, the member must fairly and adequately represent the other similarly situated members.

98. The provision establishing a manager's duties to the UNLLO in recommendation 20 cannot be varied or eliminated by agreement of the members. No internal agreement could eliminate or limit the liability of a manager: (a) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; or (b) for any transaction from which the manager derived an improper personal benefit.

99. Members could also agree to include in their organization rules a provision that they owe fiduciary duties to each other. Similarly, they could agree on how to apportion liability or whether they should forego limited liability protection. Members can also agree that a manager must adhere to a standard that is higher than that established in recommendation 20.

100. Members cannot derogate from recommendation 20, however they may specify in their organization rules that certain activities are permitted for managers which do not constitute a breach of the duties established in such recommendation. Permitting freedom of contract of the members to this extent could be useful in the context of UNLLOs, given the simplicity of this legal form.

Recommendation 20: The law should provide that any manager of the UNLLO owes a duty of care and a duty of loyalty to the UNLLO.

F. Members' contributions to the UNLLO

101. The Guide does not require members to make contributions. However, members may choose to require contributions in their organization rules and to establish what each member will provide to the UNLLO by way of contribution. In this respect, the law should permit members maximum flexibility to decide upon the value, type and timing of their agreed contributions to the UNLLO, including the flexibility to determine that members are not required to make contributions in order to be members of the UNLLO (see also rec. 11).

102. In specifying in the organization rules the types of contributions that members of the UNLLO may make, members may wish to consider tangible and intangible property as well as other benefits to the UNLLO, including money, services performed, promissory notes, other binding agreements to contribute money or property and contracts for services to be performed. Although maximum flexibility with respect to contributions to the UNLLO is encouraged, in some cases, other laws of the enacting State may restrict the types of contribution that may be made. For

¹² The exception is the possibility for a member to bring a derivative claim on behalf of the UNLLO.

example, in some States, the provision of services is not permitted as a contribution to the formation of a business entity. In such cases, those restrictions should be specified in the law prepared on the basis of the Guide.

103. The determination of the value of each non-monetary contribution should be left to the members of the UNLLO, as they are in the best position to determine that value. In this regard, it would be desirable for members of the UNLLO to provide the criteria on how to value non-monetary contributions in the organization rules. Members wishing to set forth obligations concerning the accurate value of their respective contributions may include them in the organization rules. Any other mechanism, such as requiring an audit or other external valuation method, is likely to be too burdensome for MSMEs. It is recommended that the UNLLO maintain a record (see also recs. 30 and 31) of the amount, type and timing of contribution of each member to ensure that the rights of the members are respected.

104. Recommendation 21 does not provide any default provision for instances where members agree to make contributions to the UNLLO, but do not agree upon the value of the contributions. The recommendation, however, highlights the importance of members to agree on the value of their contributions to ensure transparency and facilitate the operation of the business. Such an agreement may also help prevent disputes among the members, as it provides certainty and may limit the potential for distrust. It would be equally desirable that members reach an agreement on the value of their contributions when a new member joins the UNLLO after its formation.

105. As noted above (see para. 69), the value of a member's contribution will not determine the member's rights and obligations in the UNLLO, which should be deemed equal if members have not agreed otherwise in their organization rules. Given the "freedom of contract" principle that governs the Guide, members should also be permitted to agree on more complex ownership structures in their organization rules.

Recommendation 21: The law should establish that members may agree in the organization rules on the type, timing and value of their contributions.

G. Distributions

106. The Guide applies the principle that distributions should be made in proportion to a member's rights in the UNLLO. This recognizes that when the members have equal rights in the UNLLO, distributions will also be made evenly. However, when members have decided to deviate from the default rule of having equal rights in the UNLLO (see rec. 11), recommendation 22 provides that distributions should be adjusted accordingly, that is, to the same extent and in the same proportion as the deviation from the default rule. Members may deviate from this default provision and opt for a different distribution method that better suits their needs or the structure of the UNLLO. For example, they might decide that members who have contributed money to the UNLLO should receive a higher percentage of the distribution.

107. The members of the UNLLO may also agree on the type of distribution (for example, including cash or property of the UNLLO) as well as the timing of such distributions in conformity with recs. 23 and 24. It is advisable for States that do not permit non-monetary distributions to specify those restrictions in the UNLLO law.

Recommendation 22: The law should provide that distributions are made to members in proportion to their rights in the UNLLO unless otherwise agreed in the organization rules.

108. Although the amount, type and timing of distributions may be subject to the members' decision, the Guide includes provisions that cannot be derogated from by the members set out in recommendations 23 and 24 aimed at protecting third parties dealing with the UNLLO from any dissipation of the UNLLO's assets through improper distributions to its members. Accordingly, recommendation 23 provides that

distributions may be permissible only if the UNLLO's total assets exceed its total liabilities.

109. Distributions would also be prohibited if they would cause the UNLLO to be unable to pay its debts as they fall due or should become due in the course of ordinary business operations, provided that at the time of the distribution the debts are known to the UNLLO or the UNLLO can anticipate they would become due. If, following the distribution, an unanticipated debt arises, this recommendation provides protection and legal certainty to the members who received the distribution, and prevents the application of the clawback provision found in recommendation 24, provided that the new debt was unforeseeable at the time the distributions were made.

110. Pursuant to recommendation 23, distributions would not be allowed when either one of the standards listed therein and elaborated in paragraphs 108 and 109 above are met. Depending on the domestic context, States may choose one or both standards in their legislation, and specify that distributions would be prohibited if either standard is met. States may also decide to use both standards.

Recommendation 23: The law should prohibit distributions to any member if upon giving effect to such distribution:

(a) The UNLLO's total assets would be less than the sum of its total liabilities; or

(b) The UNLLO would not be able to pay its foreseeable debts as they become due.

111. In keeping with the rule on improper distributions established in recommendation 23, recommendation 24 permits the amount of any such distribution to be clawed back from each member who received that distribution, or any improper portion of a distribution. Such a rule is intended both to protect third parties dealing with the UNLLO and to disincentivize members from accepting improper distributions, which may leave the UNLLO insolvent. To assist the UNLLO in recovering the improper distributions and minimize any disruption in its operations, States may consider setting a deadline by which the member should repay the amount received in violation of recommendation 23, or may already have in place such a deadline on the basis of other laws of the State that apply to the UNLLO, e.g., laws on unjust enrichment.

112. To protect third parties harmed by an improper distribution, recommendation 24 provides that a member of the UNLLO is required to reimburse the UNLLO even if the member did not have actual knowledge that the distribution received was in violation of recommendation 23. States may decide to deviate from the default rule, but should do so in a manner that protects the rights of third parties. For example, States may establish that creditors and other third parties harmed by the improper distribution may bring a derivative claim against the UNLLO's member(s) who received the distribution or any member or manager liable for the improper distribution. States should also consider any possible defences to such actions, such as lack of knowledge of the impropriety.

113. Regardless of whether the UNLLO is managed by all of its members exclusively or by one or more designated managers, the duties set out in recommendation 20, with recommendations 23 and 24, should provide an adequate basis on which to find those who took the decision to pay distributions liable for any improper distributions they made. A determination of impropriety of a distribution could be made on the basis of the UNLLO's available records concerning its activities, operations and finances or its financial statements, if any (see rec. 30). Personal liability will not be affected by the removal of the management duties of the manager after the time the improper distribution was made (see rec. 20).

114. It should be noted that payments of reasonable compensation for services rendered and for bona fide debts owed by the UNLLO to a member should not be

considered distributions, and would thus not be subject to the clawback provision in recommendation 24.

Recommendation 24: The law should provide that each member who received a distribution, or any portion thereof, made in violation of recommendation 23 is liable to reimburse the UNLLO for this distribution or portion thereof.

H. Transfer of rights

115. As noted above (see para. 70), being a member in an UNLLO entitles it to exercise financial rights to receive distributions, as well as decision-making rights including rights to decide on the management structure of the UNLLO and its modification, on the conversion, restructuring and dissolution of the UNLLO, on contributions by the members and on internal governance matters.

116. Because the UNLLO legal form is expected to be used mainly by micro and small businesses, their members are likely to attach great importance to interpersonal relationships with other members. Further, in an UNLLO managed by all of its members exclusively, members might not easily consent to modifying the existing management structure. For these reasons, members may resist transfers of rights in the UNLLO without the approval of other members.

117. Accordingly, the default provision set out in the Guide permits members of the UNLLO to transfer their rights, subject to the agreement of the other members. The transferee will enjoy the financial and decision-making rights resulting from its status as a member of the UNLLO (see rec. 11).

118. While the laws of some States may permit the transfer of the whole or a part of financial rights with the retention of other rights or the transfer of only a portion of all rights including financial and decision-making rights, the laws of other States may not envisage such partial transfer whatsoever. In that latter instance, members are still generally able to make use of their financial rights in the UNLLO through various contractual agreements with third parties concerning the whole or any part of their financial rights. Such agreements would not by themselves entitle the third party to interfere in the management of the UNLLO. Members can also enter into a derivative contract with another party over their financial rights or use those rights as collateral for other obligations or business opportunities. The Guide recognizes that pursuant to domestic legal systems, rules on the issue of partial transferability of rights in a legal entity similar to the UNLLO may differ by State. States may thus wish to clarify in their legislation based on the Guide whether members may transfer a part of their rights, considering that partial transfer may result in adding a new member to the business and may modify the governance structure of the UNLLO.

119. As a transfer of rights in the UNLLO may affect the operations of the UNLLO and its relationship with creditors and other third parties, it is important to determine the time at which it takes effect. States might have different policy needs in this respect, and the Guide thus leaves them to establish the criteria to apply in order to determine when a transfer is effective.

120. The UNLLO should not be dissolved automatically by the death of one of its members. Rather, the rights of the deceased member in the UNLLO should be transferred to any successor(s) in accordance with the laws of the enacting State, including, but not limited to, inheritance law. For clarification, organization rules may specify whether the rights of the deceased member can be transferred and what criteria should apply as set out in the applicable law(s). In a single member UNLLO, given the importance to ensure the continuity of the business, any successor(s) of the single member may decide whether the UNLLO should continue or be dissolved. In a multi-member UNLLO, the death of an UNLLO member may result in the surviving members of the business being forced to accept the successor(s) of the deceased member as a new member. In order to safeguard the rights of the surviving members, domestic law may require the consent of the surviving members for the successor(s)

to join the UNLLO, permit a buyout of the successor(s)' rights in the UNLLO, or allow the surviving members to resort to dispute resolution mechanisms (see rec. 32), for example if disputes arise on the buyout price. Domestic law may also provide the possibility for the successor(s) to seek purchasers other than the surviving members. Finally, where the deceased member held the majority of rights in the UNLLO, certain domestic laws may require the consent of the minority members, while others may not consider it necessary. In this respect, States may wish to provide the minority members with appropriate safeguards, such as the right to exit the UNLLO under certain conditions.

121. A transfer of rights would not occur in the situation in which members are no longer able to exercise their rights because of permanent incapacitation or disability. Domestic laws will apply to those cases and may require appointing a legal representative to exercise the rights of the incapacitated member. Members may include in the organization rules provisions on how the UNLLO should deal with the permanent incapacitation or disability of a member in the context of transfer of rights, as long as such rules are in compliance with the domestic law (see also para. 75 above).

Recommendation 25: The law should provide that unless otherwise agreed in the organization rules:

(a) A member of an UNLLO may transfer its rights in the UNLLO, when the other members, if any, agree to the transfer; and

(b) The death of a member shall not cause the dissolution of the UNLLO. In the case of the death of a member, its rights in an UNLLO shall be transferrable to any successor(s) in accordance with the law(s) of the State.

I. Withdrawal

122. The default approach throughout the Guide is that members of an UNLLO will have equal financial and decision-making rights unless otherwise agreed in the organization rules (see rec. 11). This approach is supported by default provisions for decisions retained by the members as a result of their status as members to require either the unanimous consent of the members or a majority of members. Furthermore, in an UNLLO managed by all of its members exclusively, the default provision for resolving differences among members on matters concerning day-to-day operations of the UNLLO is that they may be decided by a majority of members, thus providing a convenient way to resolve more routine differences of view among the members. These two default provisions provide a reasonable and coherent decision-making system to resolve basic disputes in the UNLLO and to continue to conduct the affairs of the UNLLO, while at the same time allowing for members to dissent.

123. However, members of the UNLLO may not find these default decision-making mechanisms adequate once dissatisfaction or distrust disrupts their relationship. Members may not have foreseen the possibility of intractable disputes and may be unable to settle them internally. Although recommendation 25 permits members to transfer their rights upon agreement of other members, there may be difficulty in reaching such an agreement, and there might not be a ready market for the transfer. As such, the Guide includes a provision providing an exit right for members involved in such disputes.

124. A provision that permits one or more dissatisfied members to compel the dissolution of the UNLLO and the liquidation of its assets would not permit the continuation of the UNLLO which may run counter the wish of the remaining members to continue the UNLLO without the dissatisfied member. On the other hand, a provision that requires unanimous consent of all the members could prolong an intractable dispute and result in increased inefficiencies in the operation of the UNLLO.

125. The Guide therefore shows a preference for facilitating the continued existence of the UNLLO, thus preserving its economic stability and value, by permitting a member to withdraw from the UNLLO upon agreement or reasonable cause, as set out in recommendation 26(a). The Guide leaves it to States to decide the moment at which the withdrawal becomes effective and when the rights of that member should cease.

126. The Guide does not provide a definition of reasonable cause and leaves it to domestic laws to specify which events could constitute reasonable cause that would allow a member to withdraw in the absence of agreement of other members. Examples of such reasonable cause may include: (a) any actual or proposed act by the UNLLO that is oppressive to, unfairly prejudicial to, or unfairly discriminatory against a member or members; (b) failure by the UNLLO to distribute profits under certain circumstances (e.g., not to distribute profits for some consecutive years where the UNLLO has been profitable); (c) any material change in the management or control of the UNLLO not imposed by the creditors; (d) a member's or members' lack of capacity to manage affairs due to mental restraints caused by disease or other reasons; (e) the members' failure to reach a decision which would cause a deadlock to the UNLLO (see also para. 88); and (f) the denial of transfer of a member's rights in the UNLLO by the remaining members. To help the UNLLO manage instances of withdrawal in the most effective way, States could encourage the members to include this issue in the organization rules.

127. Members cannot exclude the withdrawing member's compensation for its rights in the UNLLO. The default provision in recommendation 26(b), however, permits the payment of the fair value of a withdrawing member's rights in the UNLLO over time, which avoids a situation where the withdrawing member may hold the UNLLO and its remaining members to ransom by demanding immediate payment of the entire amount. Complying with a demand of that sort might not be possible for the UNLLO or its remaining members and might effectively force its dissolution if it is rendered insolvent. The Guide leaves to States to determine what constitutes a reasonable period of time for payment. In setting this period, States should balance the ability of the UNLLO to satisfy its debts with the right of the member to receive payment without undue delay after withdrawal. For example, States could set a period of time after the member's withdrawal over which the payment should be made and allow the UNLLO members to shorten or lengthen it and to specify the terms of payment.

128. The default provision in recommendation 26(b) may present challenges in terms of assessing the fair value of the withdrawing member's rights in the UNLLO, which is necessary to protect a member against abuse by other members. In the scenario in which a transfer of a withdrawing member's rights to a third party is denied by the remaining members, the minority could be left to sell their rights for whatever price the majority was willing to offer. The starting point for a fair valuation should be that in a buyout the withdrawing members would receive the same amount that the member would have received if the UNLLO had been dissolved. However, the value of the UNLLO's goodwill should also be included in the calculation, and the buyout price for the withdrawing members should thus be that member's share of the liquidation value of the UNLLO, or a value based on the sale of the entire UNLLO as a going concern, if permissible under the laws of the State. While it will be the UNLLO itself and not its members to bear the burden of the withdrawal payment, the payment of any procedural cost should be apportioned pursuant to the domestic law of the State.

129. It would also be prudent for members to decide in their organization rules to use alternative dispute resolution mechanisms (see rec. 32) for matters that cannot be resolved through the application of the organization rules or the default provisions. Determining the fair valuation of a withdrawing member's rights' or its terms of payment, could be one of the issues that might be resolved through alternative dispute resolution, such as mediation, expedited arbitration or a request for redress by a referee or other neutral third party.

130. Finally, while the Guide does not address issues concerning expulsion of members, members of the UNLLO may decide in their organization rules that a member may be expelled by other members under certain circumstances. In case of expulsion, the expelled members should also receive compensation for their rights in the UNLLO over a reasonable period of time, although depending on the circumstances of expulsion, the payment may not necessarily have to reflect the fair value of their rights.

Recommendation 26: The law should provide that:

(a) Members may withdraw from the UNLLO upon agreement or reasonable cause; and

(b) Be paid over a reasonable period of time the fair value of their rights in the UNLLO, unless otherwise agreed in the organization rules.

J. Conversion or restructuring

131. As noted above (see para. 45) in respect of recommendation 7, the Guide envisages legislation that permits the UNLLO to evolve from a very small enterprise to a more complex multi-member entity. Therefore, UNLLOs seeking to expand their activities can accommodate their growing needs, including through the establishment of branches and representative offices without having to modify their legal form. In certain circumstances, however, regardless of this flexibility the UNLLO form may no longer meet the needs of its members, who may find a different legal form more appropriate for their business activities. Recommendation 26 thus permits the members of the UNLLO to agree to convert the UNLLO into a different legal form or to restructure it. The Guide takes the view that members should also be permitted to agree on mergers, split-ups and any other types of restructuring.

132. Furthermore, as noted above in paragraph 72 in connection with recommendation 12, a decision on the conversion or restructuring of the UNLLO would be a decision retained by the members, and would require unanimity unless otherwise indicated in the organization rules.

133. Conversion of the UNLLO into another legal form would require the new entity to re-register with the business registry or other designated State's authority. States should also provide adequate mechanisms to ensure the universal transfer of all assets and liabilities of the UNLLO to the new entity. Moreover, the State in which the UNLLO would convert to another legal form or restructure may wish to ensure that adequate safeguards are in place to protect third parties dealing with the UNLLO from any adverse effects on their rights that could arise from such a restructuring or conversion of the UNLLO. Such safeguards may already exist in legislation providing for conversion into other legal business forms, and could consist, for example, of notice periods, publication requirements or rules on the transfer of third-party rights to the new legal form.

Recommendation 27: The law should provide the necessary legal mechanisms to:

(a) Facilitate members of the UNLLO to convert it into another legal form or to restructure it; and

(b) Ensure protection of third parties affected by a conversion or restructuring.

K. Dissolution¹³

134. Recommendation 28(a)(i) provides that the members of the UNLLO may decide in their organization rules that the UNLLO will be dissolved on the occurrence of an event specified in the organization rules. In order to limit the risk of an automatic dissolution, UNLLOs should be encouraged to indicate in the rules events that can be easily verified such as specific dates or the withdrawal of a certain number of members. Should the members of the UNLLO not have established terms under which the UNLLO would be dissolved, they may decide to dissolve the entity as indicated in recommendation 28(a)(ii). The level of required consent for decisions to dissolve the UNLLO is commensurate with the default approach for decisions retained by the members on matters that are outside of the day-to-day operation of the business as indicated in recommendations 12 and 13.

135. Recommendation 28(a)(iii) includes a provision that members may not vary by agreement. An administrative or judicial decision (for example, a decision by an insolvency court) ordering the dissolution of the UNLLO must be respected by its members. Such decisions may also include administrative or judicial decisions rendered to resolve a situation when the surviving members cannot agree on how the UNLLO should continue after the death of a member (see rec. 25(b)). Domestic law will vary as to the mechanisms by which such decisions are rendered.

136. Recommendation 28(a)(iv) emphasizes a fundamental requirement for the continuity of existence of an UNLLO, namely that an UNLLO must have at least one member with appropriate legal capacity throughout its life cycle (see also rec. 7(a)). This would ensure legal certainty and transparency in the operation of the UNLLO. This requirement is not satisfied when the UNLLO is left with no member with appropriate legal capacity due to, for example, death or permanent incapacitation of member(s) without legal successors or representatives. As noted above (para. 45), in the case of a single-member UNLLO, it would thus be important for States to establish a reasonable time period for the replacement of the member so as to avoid an automatic dissolution of the UNLLO.

137. Finally, recommendation 28(a)(v) recognizes that in light of a State's legal tradition other events may trigger the dissolution of an MSME. It thus leaves States the option to indicate additional causes of dissolution, provided that such causes be included in the legislation in an exhaustive manner.

138. An UNLLO will not immediately cease its operations upon the occurrence of any of the circumstances specified in recommendation 28(a), but it will continue to exist in order to wind-up its affairs, such as settling its activities and discharging its debts and other liabilities vis-à-vis third parties, before its existence is formally terminated. Members may wish to consider including provisions in the organization rules on how the UNLLO should wind-up in case of voluntary dissolution by a decision of the members, unless prohibited by the domestic law of the State. Moreover, certain State's mandatory procedures for winding-up, which the members cannot derogate from by agreement, might also apply to the UNLLO, such as the obligation to file a statement with the relevant authority once the winding-up is completed, or the universal transfer of assets and liabilities.

139. Again, the State in which the UNLLO would be terminated may wish to ensure that adequate safeguards are in place to protect third parties from any adverse effects that could arise from the dissolution process of the UNLLO (including winding-up). Such safeguards may already exist in other legislation dealing with the dissolution process (including winding-up) of legal business forms and could consist

¹³ In certain legal traditions, dissolution is the initial stage of the process to formally terminate a business and followed by winding-up, while in others dissolution comes after winding-up. The Guide refers to "dissolution" to describe the process to terminate a business without reference to a particular tradition.

of, for example, notice periods, publication requirements (see also para. 133) or rules to establish an order of priority in receiving payments.

Recommendation 28: The law should:

(a) Provide that the UNLLO shall be dissolved in the following circumstances:

- (i) The occurrence of any event that is specified in the organization rules as causing the dissolution of the UNLLO;**
- (ii) A decision by the members;**
- (iii) The rendering of a judicial or administrative decision that the UNLLO is dissolved;**
- (iv) The UNLLO is left without any member with appropriate legal capacity; or**
- (v) Any other event specified in this law;¹⁴ and**

(b) Establish the necessary provisions and procedures for the protection of third parties.

Recommendation 29: The law should provide that the UNLLO shall continue after the occurrence of any of the circumstances specified in recommendation 28(a) only for the purpose of winding-up.

L. Record-keeping, inspection and disclosure

140. Open communication and transparency are important issues for any business entity, but they are arguably of even greater importance in respect of the UNLLO. Members of the UNLLO are likely to have equal rights in the UNLLO, and establishing and maintaining trust among them is of great importance. Access to and proper dissemination of information to all members will further enhance trust among members and will permit them to be meaningfully involved in decision-making processes, thus providing a strong basis for the positive performance of the UNLLO. In this regard, the importance of keeping records of the organization rules should be again highlighted (see para. 65).

141. The importance of sharing and disseminating information on the UNLLO among its members is also emphasized by the provisions set out in recommendations 30 and 31 which members cannot derogate from. Recommendation 30 requires the UNLLO to keep certain records, and members can agree that the UNLLO should retain additional information. Recommendation 31 ensures that each member has the right to inspect this information, as well as the right to access any other information regarding the UNLLO that would be reasonable for the member to access, which may include information on the activities, operations and financial situation of the business.

142. While some States apply broad disclosure requirements to businesses that are not publicly traded, others limit mandatory disclosure to publicly traded businesses. Disclosure requirements for large corporations could be overly burdensome and impracticable for small businesses. However, requiring an MSME to make certain information public, such as information concerning its working capital and capital needs, would serve to ensure accountability and transparency in their operations, which would also serve to protect the interest of third parties. Micro and small businesses wishing to improve their access to credit or to attract investments may have strong incentives for making such information public, particularly as they develop and progress. States opting to make public certain records that the UNLLO is required to maintain could require the UNLLO to submit them to the business

¹⁴ The term “this law” refers to the legislation that will be enacted on the basis of the Guide.

registry or the designated State authority for business registration (see rec. 9). In keeping with the intended simplicity of the UNLLO, however, the Guide takes the view that States should aim at striking a balance between promoting transparency and accountability and hindering the operations of an UNLLO with public disclosure requirements. For this reason, States may wish to permit voluntary submission of records by the UNLLO and allow it to decide on an annual basis whether to opt for disclosure or not. Even when the information to be retained by the UNLLO further to recommendation 30 is not required to be publicly disclosed, it should be shared with all members and subject to their inspection.

143. As noted above (see para. 142), the list of records that must be kept pursuant to recommendation 30 should not be particularly burdensome for UNLLOs, even when they are micro and small businesses, in that it consists of basic information necessary for entrepreneurs of all levels of sophistication to run their businesses. In this respect, the reference to financial statements in recommendation 30(d) indicates profit and loss or cash flow statements that UNLLOs may not be required to keep. The terms “activities and operations” in recommendation 30(f) refer to important business transactions of the UNLLO, for example buying and selling equipment or accessing credits, and not minor daily tasks such as purchasing basic office supplies (e.g. stationery). Moreover, the records that must be kept need only be recorded in a timely fashion and in a medium that could be expected of a similar business operating in a comparable context. The recommendation does not specify when or how that information must be kept, and it would be open to the UNLLO to simply rely on electronic or other records that are reasonable for a business of its size and complexity. For example, many MSMEs use various mobile applications that are available on electronic devices to run their commercial enterprises, and they are thus easily able to track and access all types of information relevant to the business, including inventory, simple balance sheets, and even tax returns. An UNLLO operating in that context could then satisfy the requirements of recommendations 30 and 31 by retaining and permitting access to the information electronically available via that mobile application.

144. As noted above (see paras. 141 and 142), members have the right to receive information on how the UNLLO is managed and to inspect and copy the UNLLO records. Managers, as part of their duty to act in the interest of the UNLLO and its members (see para. 95 above), should take the necessary arrangements to facilitate members’ access to the information maintained by the business entity. On the other hand, members should exercise their right to inspection in accordance with the arrangements set by the managers and without disrupting the daily operations of the UNLLO. For example, they should inspect and copy the records during regular business hours or avoid any such activity when the UNLLO is carrying out its month-end accounting procedures. In order to avoid abuse by the members, access to information should be reasonably related to the rights and obligations of a member in its capacity as a member. In addition, the UNLLO may impose restrictions and conditions on member access to certain information, such as trade secrets, in order to preserve its confidentiality or prohibit access altogether.

Recommendation 30: The law should provide that the UNLLO must keep certain records including of:

- (a) Information provided to the business registry;**
- (b) The organization rules, if and where such rules have been adopted in writing or otherwise recorded;**
- (c) Identity of past and present designated managers, members and beneficial interest owners of legal entities, if any, as well as their last known contact details;**
- (d) Financial statements, if any;**
- (e) Tax returns or reports; and**
- (f) The activities, operations and finances of the UNLLO.**

Recommendation 31: The law should provide that each member has the right to inspect and copy records of the UNLLO and to obtain available information concerning its activities, finances and operations.

M. Dispute resolution

145. Members can usually negotiate among themselves to arrive at an efficient and amicable resolution of disputes concerning the governance and operation of the UNLLO. As noted in paragraphs 123 and 129 above, however, they may not be able to settle a dispute once dissatisfaction or distrust disrupts their relationship and resolution may thus require that they engage in potentially long and expensive litigation. Further, paragraphs 95 to 100 above describe fiduciary duties and the role they play in providing important safety mechanisms to protect members against opportunistic actions of a manager or another member. From the perspective of some legal traditions, however, open-ended fiduciary duties may not be easily enforceable unless they are clearly enunciated as formal legal rules. In both instances, alternative dispute resolution (“ADR”) mechanisms, including arbitration, conciliation, mediation and other extrajudicial methods, can assist members of an UNLLO in reaching an outcome consistent with the nature of the UNLLO, where interpersonal relations play an important role in the management of the business.

146. As ADR mechanisms usually require the agreement of the parties, the UNLLO members may consider including a provision in the organization rules that disputes relating to the governance and operation of the UNLLO should be referred to an agreed ADR method, if they cannot be resolved internally. In fact, arbitration may not be the most suitable ADR mechanism for members of an UNLLO as it can be cost-prohibitive and formal, because it is an adversarial proceeding, and resolution of the dispute may not resolve distrust between the members. Mediation or conciliation may be preferable to arbitration because they are party-driven processes that aim to reach an amicable solution with the assistance of a mediator or conciliator. Those methods may help preserve the underlying relationships between the members once the dispute is resolved. The service of an ombudsman, who investigates the cause of the disputes and provides recommendations on how to eliminate them, is another alternative to litigation or arbitration, and may assist in resolving disputes with third parties (for example, with other businesses or public authorities).

147. ADR mechanisms would also benefit the UNLLO in commercial disputes with third parties dealing with the UNLLO, such as creditors, suppliers or clients, where court processes could also be too lengthy and expensive. UNLLOs involved in legal disputes with those third parties would need to weigh the cost of court processes against the costs of unresolved disputes, which may include unpaid accounts, when deciding how to pursue their disputes. Members of the UNLLO may also face geographic, linguistic and cultural barriers within a court system (for example, women may face formal or practical restrictions in accessing the courts or the UNLLO

members might not be fluent in the official language of the courts). ADR mechanisms will help reduce these obstacles. Not only are they typically faster, but these mechanisms may also be cheaper and permit a more informal and participatory approach to dispute resolution, as well as facilitate parties in working toward a more collaborative outcome than what may be possible through the judicial settlement of the dispute.

148. While recourse to an ADR mechanism would provide a valuable tool for UNLLOs in legal disputes, there may be restrictions within the State's domestic legal framework on the types of cases which may be subject to ADR, including restrictions on the availability of ADR for criminal matters, labour and competition matters, or insolvency.

149. Besides ADR mechanisms, States could consider the involvement of specialized or administrative tribunals with jurisdiction over company law and UNLLO-related disputes. Those tribunals would not only deal with disputes concerning the internal organization and governance of the UNLLO, but could also address disputes between the UNLLO and third parties such as creditorships, which play an important role in the management of the business.

<p>Recommendation 32: The law should facilitate the submission to alternative dispute resolution mechanisms of any dispute concerning the governance and operation of the UNLLO.</p>
