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Draft Legislative Guide on an UNCITRAL Limited Liability Organization

Note by the Secretariat

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I. Introduction

1. At its forty-sixth session in 2013, the United Nations Commission on International Trade Law (UNCITRAL) requested that work be commenced aimed at reducing the legal obstacles and barriers encountered by micro, small and medium-sized enterprises (MSMEs) throughout their life cycle, with a particular focus on their context in developing economies.¹ The life cycle of a business could be said to consist of several stages, which would include starting a business, operating a business, restructuring a business and dissolving a business. The mandate granted to Working Group I by the Commission was that work should focus on the first stage in that life cycle, i.e. starting a business.²

2. To that end, Working Group I commenced its deliberations at its twenty-second session in February 2014 and from its twenty-third session, in November 2014 to its thirtieth session, in March 2018, it proceeded to consider two main topics, one of which is a discussion of a simplified business entity suited to the needs of MSMEs.³ These deliberations had been taking place on the basis of the framework of issues drawn from the key features of simplified business regimes (outlined in [A/CN.9/WG.I/WP.86](#)), and as illustrated in the draft model law on a simplified business entity ([A/CN.9/WG.I/WP.89](#)), as well as other possible models (for example, that contained in the annex to [A/CN.9/WG.I/WP.83](#)).

3. Following its discussion of the framework of issues that might be considered in a simplified business entity regime, at its twenty-sixth session (New York, 4 to 8 April 2016), the Working Group decided that the legislative text it was preparing on a simplified business entity should be in the form of a legislative guide. To that end, the Working Group requested the Secretariat to prepare for discussion at a future session a draft legislative guide (consisting of recommendations and commentary) that reflected its policy discussions to date.⁴ This draft legislative guide has been prepared by the Secretariat in response to that request.

4. The Working Group commenced discussion on the draft guide at its twenty-seventh session (Vienna, 3 to 7 October 2017) and continued such work at its twenty-eighth session (New York, 1 to 9 May 2017). To date, the Working Group has considered all sections of the guide save for sections G to L. The Working Group devoted its twenty-ninth and thirtieth sessions to review the draft legislative guide on key principles of a business registry;⁵ the Secretariat has thus prepared a revised draft of the legislative guide on an UNLLO, with the view to assisting the Working Group in resuming its consideration of these materials. The current revision includes changes arising from the deliberations of the Working Group at its twenty-seventh and twenty-eighth sessions: guidance to the changes made is reflected in footnotes

¹ *Official Records of the General Assembly, Sixty-eighth Session, Supplement No. 17 (A/68/17)*, para. 321; reiterated at subsequent sessions of the Commission: *ibid.*, *Sixty-ninth Session, Supplement No. 17 (A/69/17)*, para. 321 and *Seventieth Session, Supplement No. 17 (A/70/17)*, paras. 220, 225, 340 and 321.

² The Commission stated that “such work should start with a focus on the legal questions surrounding the simplification of incorporation” and confirmed in subsequent sessions Working Group I’s approach that such work should proceed on two relevant issues: legal questions surrounding the creation of a simplified business entity and key principles in business registration. *Supra*, note 1, and *ibid.*, *Seventy-first Session, Supplement No. 17 (A/71/17)*, para. 224.

³ Report of Working Group I (MSMEs) on the work of its twenty-sixth session, [A/CN.9/866](#), paras. 22 to 47.

⁴ *Ibid.*, paras. 48 to 50.

⁵ The draft legislative guide was finalized and adopted by the Commission at its fifty-first session in 2018. See *Official Records of the General Assembly, Seventy-third session, Supplement No. 17 (A/73/17)*, para. 111.

throughout the text.⁶ The Secretariat has also made editorial adjustments necessary to facilitate the cohesion and consistency of the text.⁷

A. Purpose of the draft legislative guide

5. The vast majority of businesses in the world are MSMEs.⁸ As recognized by the Commission through its decision to grant Working Group I its current mandate, in the light of the forces of globalization and economic integration, it is important to strengthen the economic role and position of MSMEs. The Working Group has thus sought to establish the best practices of States, policymakers and practitioners to create a simplified legal business form tailored to facilitate the operation of MSMEs, thereby also stimulating entrepreneurship and innovation.

6. In its discussions to date, the Working Group has considered a number of different simplified business forms on which legislation has been enacted in various jurisdictions representing different legal traditions around the world. A selection of such business forms included in the comparative analysis that the Working Group first considered in this regard (A/CN.9/WG.I/WP.82) was drawn from 11 different States from different regions of the world and included 16 different legal regimes in total.⁹ The Working Group has also received documentation and information in respect of several other simplified business forms that have been adopted in certain States to provide the benefits to business entities of, inter alia, asset partitioning, in a less complex form that may not necessitate the granting of legal personality.¹⁰

7. Other information in respect of different approaches to creating simplified business forms has been provided by delegations to Working Group I. These reforms have included specific legislative efforts to provide for single member businesses or business entities,¹¹ as well as broader reforms to assist MSMEs that have been implemented in various States.¹²

8. Discussion in the Working Group on this topic has also provided a rich source of information relevant to the present topic. Many delegations have intervened to share the benefit of their considerable experience in creating an appropriate national legislative framework to deal appropriately with key issues in respect of the various corporate business forms in their State.

⁶ To assist the Working Group in resuming its consideration of the draft guide, the current text maintains several footnotes included in former documents A/CN.9/WG.I/WP.99 and Add.1.

⁷ The Working Group may wish to note that once a first reading of this draft guide is completed, the Secretariat will implement a thorough editorial revision of the text.

⁸ In keeping with previous decisions of the Working Group during its deliberations on the draft Legislative Guide on key principles of a business registry, the Secretariat has deleted references to “developing” and “developed” States and has made appropriate adjustments throughout the text (see para. 48, A/CN.9/928).

⁹ Those States were Colombia, France, Germany, India, Japan, New Zealand, Singapore, South Africa, the United Arab Emirates, the United Kingdom of Great Britain and Northern Ireland, and the United States of America. See footnote 4, A/CN.9/WG.I/WP.82.

¹⁰ See the alternative legislative models for micro and small businesses described by Italy and France in A/CN.9/WG.I/WP.87 and A/CN.9/WG.I/WP.94.

¹¹ Information shared with the Working Group has included, for example, that in respect of the “auto-entrepreneur”, in force both in France (see paras. 22 to 23 of A/CN.9/WG.I/WP.87) and the Member States of the Organisation for the Harmonization of Business Law in Africa (known by its French acronym, OHADA) (Acte Uniforme Révisé Portant Sur Le Droit Commercial Général, adopted 15 December 2010, see www.ohada.com/actes-uniformes/940/999/titre-2-statut-de-l-entreprenant.html). Other efforts to create particular regimes for single member businesses have included those of the European Union (Proposal for a Directive of the European Parliament and of the Council on single-member private limited liability companies, European Commission, Brussels, 9.4.2014 (COM (2014) 212 final)), as well as a draft model law on a single member business entity prepared by the Secretariat (A/CN.9/WG.I/WP.86/Add.1).

¹² Information in this respect has been shared in the Working Group in respect of such reform efforts in a number of States, including Chile, China, Colombia, El Salvador, Mexico, the Philippines, Rwanda, Thailand, and others.

9. Many of these business forms, simplified and otherwise, have enjoyed economic success in their respective jurisdictions. Moreover, the Working Group's combined experience regarding the various domestic approaches to creating and reforming legal business forms — both MSME-specific and otherwise — has highlighted that States' good practices share a number of key principles which could thus be said to be international in their application.

10. This draft legislative guide has attempted to distil these good practices and key principles into a series of recommendations on how a State could institute and regulate a legal form for MSMEs that can best facilitate their success and sustainability. The draft commentary that precedes each recommendation relies on discussions that have taken place in the Working Group and on documentation it has considered at its sessions to explain in greater detail the rationale leading to those recommendations.¹³

1. “Think small first”

11. As emphasized in materials previously considered by the Working Group,¹⁴ and in keeping with its desire to create a legal text that can accommodate the evolution of a MSME from a very small single member model to a more complex multi-member entity,¹⁵ a “think small first” approach has also been taken in this draft legislative guide. To that end, this draft text has been prepared with a focus on the actual needs of MSMEs. Consideration has also been given to how those entrepreneurs who operated MSMEs could most benefit from legislation based on these recommendations and be encouraged to conform to the rules they contain. Such entrepreneurs could range from individual street vendors, to small family business owners wishing to scale up and formalize their operations, to small firms seeking to grow and position themselves in more innovative sectors, such as the information technology field, and to women entrepreneurs facing unfavourable institutional and legislative frameworks.¹⁶

12. In order to “think small first” and assess how best to design these draft legislative recommendations to meet the needs of entrepreneurs operating MSMEs, the Working Group may wish to consider what those needs might be. These could include a number of items, but it is suggested that, at a minimum, such needs might be the following.

(a) Freedom, autonomy and flexibility

13. Most entrepreneurs could be expected to want *freedom and autonomy* to decide for themselves how they may want to operate their business. 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, without the need to resort to rigid and formalistic rules and procedures or have detailed requirements dictated to them regarding how they must carry out their activities.¹⁷

(b) Speed and simplicity

14. MSME entrepreneurs are likely to want *speed and simplicity* to characterize the rules on the legal establishment of their business, and on its administration and operation. The rules governing the business should be in simple and accessible terms,

¹³ The Working Group may wish to note that the Secretariat has made every effort to ensure that each issue that has been considered in discussions in the Working Group to date, as well as any agreement that has been reached on such issues, has been reflected in this draft legislative guide.

¹⁴ See paras. 1 and 5 of [A/CN.9/WG.I/WP.86/Add.1](#); para. 3 (iii) of [A/CN.9/WG.I/WP.90](#); and paras. 2 and 39 of [A/CN.9/WG.I/WP.89](#).

¹⁵ As agreed by the Working Group at its previous sessions (see paras. 24, 32 and 42 to 43, [A/CN.9/800](#), paras. 67 and 74, [A/CN.9/825](#), and para. 19, [A/CN.9/831](#)).

¹⁶ In keeping with the approach of the UNCITRAL Legislative Guide on Key Principles of a Business Registry and of [A/CN.9/941](#), the Secretariat has added reference to women entrepreneurs.

¹⁷ The Secretariat has made editorial adjustments to this paragraph (para. 12 of [A/CN.9/WG.I/WP.99](#)) for further clarity.

and the use of modern technology, such as the use of mobile applications to complete payments or prepare balance sheets, should be encouraged to assist such entrepreneurs.

(c) Identity and visibility

15. MSMEs need an *identity and visibility* in order to successfully compete in the market and to attract clients. These features facilitate their recognition in the market and permit third parties to more easily locate the business and its products. In addition to the obvious protections and advantages associated with taking on a legally recognized identity and operating within a framework of statutory laws,¹⁸ the business can also use its identity to develop its reputation and “brand” and increase its value.¹⁹

(d) Certainty and protection

16. Such entrepreneurs need *certainty in and protection of their property rights*. As such, MSME operators may be expected to want to control the ownership rights in their business and to be able to take advantage of asset partitioning, so as to protect their personal assets from claims that creditors may have against the business. It is also important that personal creditors of business owners and managers cannot seize business assets in order to satisfy such personal debts.

(e) Control and management

17. Finally, MSME operators generally want *to control and to manage their business*, rather than leaving administrative and strategic decisions concerning their business to a third-party manager.

2. Satisfying business needs and expectations

18. Through “thinking small first” and considering the above-described real world business needs, this draft legislative guide aims to assist States to create legal rules that satisfy those needs and expectations. For example, MSME entrepreneurs’ need for freedom, autonomy and flexibility is woven throughout this draft legislative guide in its recognition of the importance of freedom of contract and avoidance of formalistic and rigid corporate law rules. However, it is acknowledged through many default rules that such entrepreneurs may also require protection against circumstances or events that may not be foreseeable.

19. Speed and simplicity characterize not only the recommendations for rules on the establishment of the business entity (see also para. 14 above), but this guide as a whole also uses accessible terminology, clearly acknowledges technological innovation and welcomes its use. In addition, to provide MSMEs with identity and visibility, the draft recommendations provide the business entity with legal personality and provide a simple vehicle for the entrepreneur to create a legally recognized business. Further, limited liability protection for 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 operators. Finally, control by MSME entrepreneurs over the operation and management of their business is assured through an emphasis on member-management as the default governance

¹⁸ Such protections and advantages have been enumerated in para. 31 of A/CN.9/941, and include, inter alia, asset partitioning, protection against potential administrative abuse and other abuse of rights, easier access to credit, labour law protection for employees, and similar features.

¹⁹ On the importance of business registration to provide a commercial identity to a business, see the UNCITRAL Legislative Guide on Key Principles of a Business Registry [*The Working Group may wish to note that the final version of the Guide is currently being edited in order to incorporate a few revisions agreed upon at the fifty-first session of UNCITRAL. Therefore, any reference in this commentary to specific paragraphs or recommendations in the Guide is to be intended to document A/CN.9/940 that includes the text of the Guide as transmitted to the Commission for adoption*].

approach and on the more horizontal governance structure that characterizes this draft legislative guide.

20. The Working Group has also considered different approaches that could be taken to achieving its goal of creating a specific and simplified legal form to facilitate the operation of MSMEs. There was broad agreement in the Working Group that its goal should not be to reform and simplify outdated company law regimes, but rather to develop a separate and innovative approach based on the collective domestic experience of delegations, and to specifically tailor it to MSMEs.²⁰

21. In view of that objective and recognizing that more formalistic and rigid corporate-style rules may not be appropriate for such businesses, this draft legislative guide has taken the view that the optimal solution for the creation of an appropriate simplified legal regime for MSMEs is to build on the good practices in corporate law reform identified by the Working Group to date, while creating an innovative legal regime for MSMEs capable of standing on its own. The structure envisioned in this draft legislative guide is thus neither dependent upon nor specifically linked to existing partnership, corporation or company law in any State.

22. One clear advantage of that approach is that it enables States to more easily adopt a regime that implements the legislative recommendations. Perhaps more important, however, is that this approach permits States to craft appropriate legislative measures using a clean slate approach, allowing them to step away from existing business forms and to respond to the real needs of the types of businesses that such a structure seeks to serve. The approach favoured in this draft legislative guide is intended to acknowledge and focus on the real nature of many micro and small businesses around the world for which 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 usually represent the main characteristics.²¹ The recommendations in this draft legislative guide create a legal business form that moves away from more traditional, hierarchical and formal governance model towards less rigid and formalistic structures based on the actual needs and expectations of entrepreneurs. This approach may also present the best possible opportunity for the Working Group to achieve a unified text capable of being used in a cross-border context, and not dependent on the legal regime of any particular State, but rather representing a product of good practices drawn from legal regimes around the world.

23. Further, in addition to reducing barriers to MSMEs registering and operating their businesses within statutory frameworks and helping them to maximize their economic potential, the simplification of business incorporation and registration could have additional international effects.²² In particular, an internationally recognized simplified business form could facilitate cross-border trade for MSMEs, since it would provide a recognizable basis for such business forms and avoid problems that might arise due to a lack of international recognition of the business form of the enterprise.²³

24. In pursuit of this informed and innovative approach to MSME law reform, this draft legislative guide has adopted terminology that is intended to be as neutral as possible. In order to assist the Working Group in considering the real issues facing MSMEs and to learn from existing company law solutions but not to rely on their more rigid rules, “corporate” and “company” terminology is not used. Nor is the

²⁰ As agreed by the Working Group at its twenty-fourth session (para. 54, [A/CN.9/831](#)). See, also different approaches to legal reform as outlined in paras. 5 to 7 of [A/CN.9/WG.I/WP.82](#).

²¹ The Secretariat has redrafted this sentence in keeping with previous decisions of the Working Group on the use of “developing” and “developed” (see also *supra*, footnote 8). With regard to the characteristics of MSMEs, see also para. 12 of [A/CN.9/941](#).

²² The Secretariat has deleted the phrase “such an approach... MSME work” between “Further” and “in addition” to avoid redundancy in the paragraph (para. 21 of [A/CN.9/WG.I/WP.99](#)).

²³ See Note by the UNCITRAL Secretariat, para. 10 of [A/CN.9/780](#).

previous term “simplified business entity” used.²⁴ Instead, this guide describes a new entity: the “UNCITRAL Limited Liability Organization” (the “UNLLO”), a term which is meant to act as a reminder of the innovative and independent goal to which the Working Group aspires.²⁵

25. Similarly, this draft text has dispensed with other corporate-related terminology in favour of more neutral terms, as previously agreed by the Working Group. The section on “Terminology” (see para. 27 below) includes a list of such terms and their definitions.²⁶

26. The UNLLO approach in this draft legislative guide has been taken in an effort to fulfil each of the desired goals and considerations outlined above.²⁷ In addition, this text is intended to include all of the business law concepts considered by the Working Group to date, using them to create an innovative but informed legal business form based upon the actual needs of MSMEs in emerging markets.

B. Terminology²⁸

27. As noted above (see paras. 24 and 25), this draft legislative guide adopts neutral terminology unencumbered by existing corporate law regimes. In order to ensure that those terms and concepts are widely understood, this paragraph provides an explanation of their meaning and use.

- *Formation document*:²⁹ “Formation document” means the document containing the set of data (whether in electronic, paper-based or mixed form) that must be submitted to the designated State authority in order to create the UNLLO.³⁰

²⁴ The Working Group may wish to recall its previous discussions on what might be the best and most neutral term for the business entity being created. Although there was support for the use of the term “simplified business entity”, a view was expressed that the phrase “simplified company” should be used, and the Working Group agreed to use the former term in the draft model law but to place it in square brackets (see para. 68, [A/CN.9/825](#); and para. 38, [A/CN.9/831](#)).

²⁵ 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](#)).

²⁶ The Secretariat has deleted the second part of para. 25 (para. 23 of [A/CN.9/WG.I/WP.99](#)), since definitions of the terms used in the draft legislative guide have been included in the “Terminology” section in para. 27.

²⁷ This draft legislative guide also takes into account those considerations said by some delegations to be key (see para. 66, [A/CN.9/825](#) and para. 2 of [A/CN.9/WG.I/WP.89](#)) including: (i) permitting the simplified business entity to have one or more members; (ii) providing for full-fledged limited liability; (iii) establishing simple registration (see the UNCITRAL Legislative Guide on Key Principles of a Business Registry) and formation requirements; (iv) enabling maximum freedom of contract for members while establishing clear default rules to fill any gaps in rule-making; (v) providing for a flexible organizational structure; (vi) making minimum capital optional; (vii) not requiring a statement of the entity’s purpose; (viii) permitting the optional use of intermediaries; (ix) providing for fiscal transparency and simplified accounting; and (x) building on the presumption that a ready-made business form statute should focus on the needs of the smallest entities first (the “think small first” principle).

²⁸ The Secretariat has added a “Terminology” section further to a request of the Working Group at its twenty-seventh session (para. 19, [A/CN.9/895](#)).

²⁹ At its twenty-seventh session the Working Group agreed to revert to the use of the phrase “formation document” (see [A/CN.9/WG.I/WP.89](#) and the annex to [A/CN.9/WG.I/WP.83](#)) in lieu of “formation information” which was used in [A/CN.9/WG.I/WP.99](#) and Add.1 (para. 52, [A/CN.9/895](#)).

³⁰ The Secretariat suggests that in future revisions of the draft guide, the definition of “formation document” should include reference to public availability of the information listed in the document, subject to the Working Group deliberations on this matter (para. 52, [A/CN.9/895](#)).

- *Majority decision*:³¹ “Majority decision” means a decision agreed to by more than half of the members or by more than half of the ownership of the UNLLO if members have a different percentage of ownership of the UNLLO.
- *Manager*: “Manager” means the person responsible for controlling or administering the UNLLO. As used in this draft legislative guide it includes both a member-manager and a manager-manager.
- *Manager-managed*:³² “Manager-managed” means an UNLLO that is managed by a designated third-party manager or managers.
- *Member(s)*: “Member(s)” means the owner(s) of the UNLLO (cf. “UNLLO”).³³
- *Member-managed*: “Member-managed” means an UNLLO that is managed by its member(s) or some of them.
- *Members’ agreement*:³⁴ “Members’ agreement” means the internal rules, set out in writing, orally or implied through course of conduct, that govern the organization of the UNLLO.
- *Ownership*:³⁵ “Ownership” means the member’s or members’ legal share in the UNLLO.
- *Qualified majority*:³⁶ “Qualified majority” means a decision agreed to by [percentage to be included subject to the Working Group decision] of the UNLLO members.
- *UNCITRAL limited liability organization [UNLLO]*:³⁷ “UNCITRAL limited liability organization [UNLLO]” means the legal business form with limited liability and legal personality discussed in this draft legislative guide.

³¹ The Secretariat has included this definition and that of “qualified majority” in keeping with the comments of the Working Group at its twenty-seventh session (para. 63, [A/CN.9/895](#)). The definition of majority has been made consistent with the current drafting of rec. 12(a) (rec. 13(a) in [A/CN.9/WG.I/WP.99/Add.1](#)).

³² The Working Group may wish to consider whether the draft legislative guide should include a definition (and a discussion) of an UNLLO that is jointly managed by a third-party manager(s) and an UNLLO member(s).

³³ At its twenty-fourth session, the Working Group agreed to use the term “member” rather than “shareholder”, since it was thought to be more system-neutral and inclusive (see para. 48, [A/CN.9/831](#)).

³⁴ Although the terms “formation document” and “operating document” were chosen as neutral terms in previous iterations of the materials before the Working Group, concern was expressed since the legal regime in some States did not recognize two separate documents that corresponded to the functions as indicated. The Working Group agreed that the important feature to be preserved in a future iteration was not necessarily regarding the terminology, but rather in respect of the contents or information contained therein and which aspects of that information would be made public (see paras. 39 and 68, [A/CN.9/831](#)).

³⁵ At its twenty-sixth session, the Working Group agreed that the term “share” should be replaced with an alternative and more neutral term such as “ownership” or “interest” (see para. 25, [A/CN.9/866](#)).

³⁶ At its twenty-seventh session the Working Group agreed that matters requiring a qualified majority were included in the non-exhaustive list of para. 72 (para. 10 of [A/CN.9/WG.I/WP.99/Add.1](#)) and that such matters should be further specified at a later stage (para. 63, [A/CN.9/895](#)).

³⁷ The Working Group 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 25).

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

A. General provisions

28. As noted above (see para. 21), the approach taken in this draft legislative guide on an UNLLO is to create a legal business form that does not depend on and is not specifically linked to any existing law in an enacting State³⁸ for its establishment, definition or operation. Instead, the UNLLO is intended to be a distinct product of legislation that has been prepared on the basis of the recommendations in this draft legislative guide.³⁹

(a) Legislative framework

29. Although the legal forms for privately held businesses may vary from State to State, one of their hallmarks could be said to be to function as independently as possible from the strict rules that govern public companies. For example, privately held businesses tend to have specific relief from the rules governing public companies, resulting in: simpler formation rules; nominal or no minimum capital requirement; greater freedom of contract; and fewer disclosure requirements.⁴⁰

(b) Flexibility through freedom of contract

30. The main focus of legislative reforms to assist the creation of privately held business entities to date has been on the creation of flexible business forms that can be tailored to the needs of certain types of closely held businesses, including: MSMEs wishing to formalize and segregate personal and business assets; family firms; joint ventures; and professional service firms.⁴¹ It should also be noted that, in some States, reforms have resulted in legislative models that permit the separation of business assets of an entity from the personal assets of its members without resort to legal personality. This would allow asset partitioning for MSMEs and their members by way of a legal structure that stops short of full limited liability and legal personality.^{42,43}

31. The UNLLO is intended to be added to this list of flexible business forms. The flexibility in business form has been achieved in part by allowing the UNLLO to be organized for a wide range of activities (see paras. 35 and 36 and rec. 2 below) and mainly by recognizing the importance of freedom of contract for these privately held

³⁸ At its twenty-seventh session, the Working Group agreed that it would revert to discussion on linkage of the draft legislative guide to existing domestic company law at a later stage (para. 22, [A/CN.9/895](#)).

³⁹ The Secretariat has deleted the final phrase of this paragraph (para. 25 of [A/CN.9/WG.I/WP.99](#)), “and which ... enacting State”, to eliminate redundancy in the text.

⁴⁰ International Encyclopedia of Comparative Law, Volume XIII, Business and Private Organizations (1998), Detlev Vagts ed., Chapter 2, Limited Liability Companies and Private Companies, pp. 2 and 13.

⁴¹ See paras. 8 to 11 of [A/CN.9/WG.I/WP.82](#).

⁴² See, for example, the mechanisms described in paras. 47 to 49 of [A/CN.9/WG.I/WP.92](#), as reported to the Working Group in [A/CN.9/WG.I/WP.87](#), and referred to in para. 29 of [A/CN.9/800](#), paras. 56 to 61 of [A/CN.9/825](#) and para. 20 of [A/CN.9/831](#). An additional such legislative mechanism is described in [A/CN.9/WG.I/WP.94](#).

⁴³ At its twenty-seventh session, the Working Group agreed to move the second sentence of para. 37 of [A/CN.9/WG.I/WP.99](#) (“However, it should be noted ... legal personality.”) to a more appropriate section of the draft legislative guide and to delete the phrase “limited liability” after “without resort to legal personality” (paras. 31 and 32, [A/CN.9/895](#)). The Secretariat has relocated that sentence in para. 30 above, with additional editorial adjustments.

businesses. In this respect, freedom of contract has been made the guiding principle in establishing the internal organization of the UNLLO (see paras. 64 and 65 below).⁴⁴

32. The draft guide permits the members of the business to agree through contractual mechanisms (i.e. members' agreement) on the internal governance of the enterprise, to contract around the more superfluous and cumbersome protective requirements traditionally associated with public companies, and to tailor rights and duties that are more consistent with the needs of privately held businesses.

33. However, the draft guide also includes certain recommendations for mandatory rules that cannot be contracted out of by agreement among the members, as well as default provisions to fill any gaps in their agreement.⁴⁵ These default rules can be particularly important for smaller or less-experienced business persons who may not foresee every eventuality required for the successful operation of the UNLLO.⁴⁶

34. The fact that the UNLLO is established through an independent legislative approach on the basis of the recommendations contained in this draft guide that permits extensive freedom of contract to organize the UNLLO's operations is reflected in draft recommendation 1.⁴⁷

Recommendation 1: The law should provide that an UNCITRAL Limited Liability Organization ("UNLLO") is governed by this law and by the members' agreement.⁴⁸

35. Draft recommendation 2 permits an UNLLO to be organized for any lawful business or commercial activity. A very broad approach to the permitted activity of an UNLLO is taken in order to provide maximum flexibility to the MSMEs that are anticipated to use this business form. In keeping with current and previous UNCITRAL texts, the guide supports the view that States should give the terms "commercial" and "business" wide interpretation to avoid unwarranted narrowing of the permitted scope of the UNLLO.⁴⁹ Moreover, no mention is made of general purpose clauses; the modern trend in that respect is to allow business entities to engage in all lawful activities under the law of the relevant State and to leave it open to the members of the UNLLO to decide whether or not they wish to include a more restrictive purpose clause in the members' agreement.⁵⁰ In keeping with this approach, States requiring business entities to list all of their activities may wish to consider removing that requirement for UNLLOs.⁵¹

36. States wishing to enumerate the industrial sectors and activities in which an UNLLO may participate could prohibit an UNLLO from engaging in certain regulated

⁴⁴ In that regard, the Working Group also observed that MSMEs could find it difficult to establish such rules, and that standard forms could be useful to assist such businesses (see para. 63, A/CN.9/800 and para. 23 of A/CN.9/WG.I/WP.86). Once the Working Group has advanced its work on this draft legislative guide, it may wish to consider whether it would be useful to prepare such standard form members' agreements to assist MSMEs in this regard.

⁴⁵ See paras. 10 and 11 of A/CN.9/WG.I/WP.82 and para. 22 of A/CN.9/WG.I/WP.86.

⁴⁶ The Secretariat has revised paras. 30 to 34 of this draft guide (paras. 27 to 30 of A/CN.9/WG.I/WP.99) for improved clarity of the text.

⁴⁷ The fact that the operation of the UNLLO will in large part be governed by the principle of the freedom of contract of its members is also reflected in draft rec.10 (rec. 11 in A/CN.9/WG.I/WP.99/Add.1).

⁴⁸ At its twenty-seventh session, the Working Group agreed to delete "if any" at the end of rec. 1 (para. 24, A/CN.9/895) and to defer decision on rec. 1 and its commentary until it had considered rec. 10 and the accompanying commentary (para. 28, A/CN.9/895). See also infra footnote 113.

⁴⁹ The Secretariat has redrafted this paragraph (paras. 31 and 32 of A/CN.9/WG.I/WP.99) for consistency with revised rec. 2 and further to a request of the Working Group at its twenty-seventh session that the terms "commercial" and "business" should be given a broad interpretation (para. 30, A/CN.9/895).

⁵⁰ The Working Group agreed at its twenty-third session during a discussion of whether purpose clauses were necessary that a very broad approach should be taken in this regard in order to provide maximum flexibility for MSMEs wishing to use the legal form being established (see para. 70, A/CN.9/825, para. 27 of A/CN.9/WG.I/WP.86, and para. 9 of A/CN.9/WG.I/WP.89).

⁵¹ The Secretariat has included this last sentence to emphasize the concept that an UNLLO should be provided with maximum flexibility.

industries, such as in the banking, microcredit or insurance industry.⁵² Similarly, for additional clarity, participation in specific activities could also be expressly permitted, and might include activities in the agricultural, artisanal and cultural sectors,⁵³ or participation by cooperatives and funds.⁵⁴

Recommendation 2: The law should provide that an UNLLO may be organized for any lawful business or commercial⁵⁵ activity.

37. This draft legislative guide recommends the granting of legal personality in order to give clear expression to the nature of the UNLLO as a legal entity separate from its members.⁵⁶ 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.

38. 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.⁵⁷ A distinct legal personality permits the UNLLO to be shielded from potential claims by the personal creditors of its members. This, in turn, facilitates defensive asset partitioning by an UNLLO that has been granted limited liability, which can then protect the personal assets of the UNLLO members from exposure in the event that the UNLLO is unable to satisfy its debts or meet its obligations or becomes involved in legal disputes.⁵⁸ Legal personality and limited liability protection (see draft rec. 4) thus provide a convenient legal mechanism for the UNLLO to separate its assets from the personal assets of its members.⁵⁹

39. It should be noted that domestic taxation policy in respect of the legal form of an UNLLO is not considered in this legislative guide. Such policy matters should be left to States drafting legislation on the basis of this guide, with the understanding that those States might consider their policy options in the broader context of how best to reduce legal obstacles for UNLLOs, and MSMEs more generally.⁶⁰

Recommendation 3: The law should provide that the UNLLO has a legal personality distinct from its members.⁶¹

⁵² The Working Group agreed that it might be useful to establish what the scope of application of the legal text would be, for example, that it might exclude enterprises in certain highly regulated sectors (see para. 24, A/CN.9/800, para. 68, A/CN.9/825 and para. 8 of A/CN.9/WG.I/WP.89).

⁵³ The Working Group agreed on such an inclusion at its twenty-fourth session (para. 36, A/CN.9/831).

⁵⁴ The Working Group agreed on the possibility of such an inclusion at its twenty-second and twenty-third sessions (para. 25, A/CN.9/800 and para. 69, A/CN.9/825).

⁵⁵ At its twenty-seventh session, the Working Group agreed to insert the phrase “business or commercial” before “activity” (para. 30, A/CN.9/895).

⁵⁶ At its twenty-second session, the Working Group expressed general support for the view that limited liability and legal personality offered MSMEs important advantages in doing business and that it was important to provide access to these advantages to such enterprises (see para. 28, A/CN.9/800). Legal personality was also considered by the Working Group at its twenty-third and twenty-fourth sessions (see para. 10 of A/CN.9/WG.I/WP.89, para. 72, A/CN.9/825 and paras. 42 to 49, A/CN.9/831), including key aspects that should be included in the concept of legal personality.

⁵⁷ See, for example, Henry Hansmann and Reinier Kraakman, “The Essential Role of Organizational Law”, 110 Yale L.J. 387 (2000) (www.yalelawjournal.org/article/the-essential-role-of-organizational-law).

⁵⁸ The Secretariat has switched the order of the sentences “Such distinct ... legal disputes” for improved consistency of the paragraph.

⁵⁹ For improved consistency of the draft text, the Secretariat has included here (para. 36 of A/CN.9/WG.I/WP.99) the opening sentence of para. 37 of A/CN.9/WG.I/WP.99. See also supra, footnote 43.

⁶⁰ The Working Group was encouraged at its twenty-fourth session to avoid an overemphasis on tax-related issues and focus on developing a system-neutral legal instrument, and it was suggested that although tax issues need not be directly addressed in the draft text, they should be noted in the commentary (see paras. 18 and 50, A/CN.9/831).

⁶¹ At its twenty-seventh session, the Working Group agreed to insert the phrase “distinct ... members” at the end of the recommendation (para. 33, A/CN.9/895).

40. Draft recommendation 4 establishes the default rule that members of the UNLLO will enjoy limited liability for the obligations of the UNLLO.⁶²

41. Limited liability is a legal concept that permits entrepreneurs to take business decisions without concern that their personal assets will be jeopardized in case of failure. This is important both for the protection of the members of the organization and for the promotion of innovation and business creation. However, many MSMEs do not currently enjoy the benefits of limited liability protection. In some States, limited liability protection is not offered to MSMEs because of concerns that it would encourage opportunism by entrepreneurs and provide insufficient protection for third parties dealing with the MSME. Other States, however, grant MSMEs access to limited liability protection, since this is considered to promote entrepreneurship and facilitate capital formation.⁶³ 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.⁶⁴

42. The presence of such a liability shield generally prevents 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, limited liability of members and distinct legal personality of the organization often go hand in hand (see draft recs. 3 above and 8 below). Granting both attributes to the UNLLO will assist in promoting the stability of the organization and access by it to lower cost credit.

43. The UNLLO itself has unlimited liability 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 tort⁶⁵ or for example, a member may be liable for a personal guarantee that has been undertaken in respect of the obligations of the UNLLO. Moreover, in the event that a contract with a third party was entered into before the formation of the UNLLO, members or managers of the UNLLO who entered in that contract may incur personal liability if the third party did not expect to be entering into a contract with an UNLLO. The law should permit a reasonable time period for subsequent action by the members to cure the lack of legal formation and to alert third parties of the change in legal status.⁶⁶

44. Of course, it will remain open for courts to lift the limited liability protection of an UNLLO ("piercing the corporate veil") and impose personal liability on members and managers in cases of fraud or other wrongful acts committed in the name of the UNLLO.⁶⁷ 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.

⁶² In keeping with a request of the Working Group at its twenty-seventh session, the Secretariat has deleted the phrase "in the ... business", after "UNLLO" (para. 34(b), A/CN.9/895). Moreover, the Secretariat has: (a) relocated this paragraph (para. 42 of A/CN.9/WG.I/WP.99) at the beginning of the commentary to rec. 4; and (b) deleted its second sentence ("It would also ... member's contribution") for consistency with revised rec. 4. The Secretariat has included the concept of how members can apportion liability among themselves in para. 77. See also footnote 68 infra.

⁶³ The Secretariat has added the sentences "In some States ... capital formation" to the paragraph (para. 39 of A/CN.9/WG.I/WP.99) for improved clarity of the draft text.

⁶⁴ As agreed by the Working Group at its previous sessions (paras. 25, 28 to 30, A/CN.9/800; paras. 51, 69 and 71, A/CN.9/825; and paras. 51 to 60, A/CN.9/831).

⁶⁵ At its twenty-seventh session, the Working Group agreed to delete the phrase "or liability ... UNLLO", before "or for example", since it concerned liability matters of a different nature from those discussed in this paragraph (para. 34(a), A/CN.9/895).

⁶⁶ At its twenty-seventh session, the Working Group agreed to include in the commentary a paragraph in respect of contracts entered into prior to the legal formation of the UNLLO (para. 51, A/CN.9/895).

⁶⁷ See, also, para. 47(e) in relation to draft rec. 5, as well as draft recs. 13, 19 and 20.

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.^{68,69}

45. Some States maintain the view that a minimum capital requirement is a reasonable quid pro quo for members of a privately held business to receive the benefit of limited liability protection. However, many of those States have significantly reduced minimum capital requirements for privately held businesses to nominal or initially low but progressively increasing amounts. In this respect, it has been stated 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 voting rights. On the other hand, concerns have been raised that capital requirements, including progressive capital requirements, could negatively impact small enterprises that are starting up, since 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 its possible financial fragility.⁷⁰

46. The modern trend in simplified business forms is that a minimum capital amount is not typically required, or if it is required, it is only for a nominal amount, thus reducing the initial financial burden on smaller entrepreneurs wishing to create legally recognized business forms.⁷¹ Since the minimum capital required to create such a business, along with the accounting rules of the required capitalization, is often one of the most important considerations for new businesses, its elimination or reduction may be expected to be one factor that can positively affect the rate of establishment of legally recognized business entities.⁷² Furthermore, 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.

47. 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.⁷³ The more important of such mechanisms are included in this draft legislative guide as mandatory rules, while others may be found elsewhere in a State's legislative framework. These mechanisms include:⁷⁴

(a) Making members of the UNLLO liable for improper distributions and obligating them to repay the UNLLO for any such distributions (see draft recs. 19 and 20, which are mandatory rules);⁷⁵

⁶⁸ At its twenty-seventh session, the Working Group agreed to retain the text of rec 4.1 and to delete draft rec. 4.2 as they appeared in footnote 37 of [A/CN.9/WG.I/WP.99](#), but to reflect the content of proposed rec. 4.2 elsewhere in the text possibly in relation to the members' agreement (para. 37, [A/CN.9/895](#)). The Secretariat has implemented that suggestion in para. 77 of the current revision.

⁶⁹ The Working Group may wish to consider whether two additional recommendations and attendant commentary could be added in this part of the draft guide to address the legal consequences on the UNLLO's and its members' liability of contracts and other acts that a member-to-be concludes or performs for the benefit of the UNLLO prior to its formation.

⁷⁰ The Secretariat has redrafted this paragraph (para. 44 of [A/CN.9/WG.I/WP.99](#)) further to the request of the Working Group at its twenty-seventh session, that the commentary should reflect the considerations raised by the Working Group during its twenty-seventh and previous sessions in regard to policy choices for and against minimum capital requirements (para. 42, [A/CN.9/895](#)).

⁷¹ See paras. 29 and 51 to 59 of [A/CN.9/800](#); paras. 56 and 75 to 76 of [A/CN.9/825](#); paras. 26 to 29 of [A/CN.9/WG.I/WP.85](#) and paras. 10 to 12 of [A/CN.9/WG.I/WP.86/Add.1](#).

⁷² See para. 30 of [A/CN.9/WG.I/WP.86](#).

⁷³ See paras. 55 to 59 of [A/CN.9/800](#) and paras. 77 to 78 of [A/CN.9/825](#) concerning the agreement of the Working Group on this approach. The Working Group may wish to consider including this paragraph under a separate section relating to the protection of creditors and other third parties.

⁷⁴ See the general discussion of these issues by the Working Group in para. 32 of [A/CN.9/WG.I/WP.86](#) and paras. 77 to 78 of [A/CN.9/825](#).

⁷⁵ The Working Group may wish to consider the following aspects for future discussion:
(a) whether the UNLLO members should be liable to creditors or just to the UNLLO and
(b) whether creditors can force the UNLLO to act against its members.

(b) Prescribing standards of conduct, including good faith and fiduciary responsibilities (see draft rec. 13(a), which is a mandatory rule);

(c) Requiring transparency and accessibility in the keeping and sharing of UNLLO records and information (see recs. 25 and 26, which are mandatory rules);

(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 draft rec. 6, which is a mandatory rule);

(e) Permitting exceptions to the limited liability protection of members of the UNLLO in certain circumstances (a rule on "piercing the corporate veil" is a judicial remedy in respect of corporations that is available in some States but that should not necessarily be imported in respect of the UNLLO, where it might better be characterized in terms of mandatory rules prohibiting a member's abuse of the UNLLO legal form; such mandatory rules are found in draft recs. 13(a), 19 and 20);⁷⁶

(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 and relevant recommendations are included in the UNCITRAL Legislative Guide on Key Principles of a Business Registry);

(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).

48. In keeping with the nature of the UNLLO as a mechanism to assist MSMEs, as well as the modern trend away from minimum capital requirements and the inclusion of other mechanisms to protect third parties dealing with the UNLLO, this draft legislative guide does not contain a minimum capital requirement for the establishment of an UNLLO. As noted above, the main mechanisms included in the draft legislative guide to provide protection to third parties dealing with the UNLLO are by way of the mandatory rules in draft recommendations 6, 13(a), 19, 20, 25 and 26, as outlined in subparagraphs 47 (a) to (e) above.⁷⁷

49. Should a State's policy considerations necessitate the imposition of a minimum capital requirement, even of a nominal or progressively increasing amount, it is not recommended that that requirement be placed on the UNLLO. 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 would then be required to convert to another legal form (of which the State might require minimum capital) upon exceeding that maximum. It should be cautioned, however, that such an approach could unnecessarily restrict the growth of UNLLOs.

⁷⁶ The Working Group may also wish to recall that it has previously considered the issue of "piercing the corporate veil", reaching general agreement that "rules on piercing the corporate veil were quite detailed and could vary widely from State to State, such that it might not be productive to attempt to establish such standards in the draft text, outside of noting the potential importance of such a remedy in the commentary and leaving the establishment of standards on it to enacting States." (paras. 56 and 58, [A/CN.9/831](#)). In any event, courts may still "pierce the corporate veil" under State law if the UNLLO legal form is abused by its members, and such a tool need not be specifically inserted into the text of the draft legislative guide. At its twenty-seventh session, the Working Group agreed with the approach outlined in this footnote (para. 35, [A/CN.9/895](#)).

⁷⁷ See also para. 16 of [A/CN.9/WG.I/WP.89](#).

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

50. In order to signal to third parties dealing with the UNLLO that they are dealing with such an entity, the law should require that the name of the UNLLO must include a phrase or abbreviation (such as “UNLLO”)⁷⁸ that would enable it to be distinguished from other types of business entity.⁷⁹ The use of the same or a similar phrase or abbreviation in different States would assist UNLLOs engaging in cross-border trade in that the defining characteristics of the entity would be immediately known upon recognition of the phrase or abbreviation, even in the cross-border context. Since the UNLLO legal form is intended as an innovative legal form specifically tailored to MSMEs and created through an independent legislative approach delinked from existing models,⁸⁰ the choice of an appropriate identifying phrase or abbreviation need not be dependent on the local legal context.⁸¹

51. While 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 the UNLLO’s limited liability to those parties, specifying in the UNLLO legislation that a failure to do so would result in a sanction such as denial of the benefit of limited liability protection might be too harsh a penalty to impose on MSMEs. Instead, States may wish to encourage the UNLLO to use its distinctive phrase or abbreviation in all correspondence in order to enhance legal certainty, but not make it mandatory so as to avoid creating an additional burden on the UNLLO by potentially increasing its administrative costs of compliance and verification.⁸² 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.

52. In terms of the name chosen for the UNLLO, the UNLLO will clearly have to comply with all mandatory requirements concerning registration (and approval) of company names in the jurisdiction in which it is doing business.⁸³

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 UNLLO⁸⁴

53. This draft legislative guide takes a flexible approach and recommends that the law should permit an UNLLO to be established and operated with a single member or with multiple members. This is to accommodate the creation of an UNLLO by a sole member, including by an individual entrepreneur engaged in relatively simple business activities, and to permit the UNLLO legal form to evolve from a very small

⁷⁸ In keeping with footnotes 25 and 37, supra, the term (“UNLLO”) is used here by way of example.

⁷⁹ The Working Group agreed on this approach at its twenty-seventh (para. 43, A/CN.9/895) and previous sessions (see para. 69, A/CN.9/825 and paras. 61 to 63, A/CN.9/831).

⁸⁰ As generally agreed upon by the Working Group at its twenty-fourth session (para. 54, A/CN.9/831).

⁸¹ In light of the discussion in the commentary to rec. 6, the Working Group may wish to agree on a suggested unified term to be used for the identification of the UNLLO.

⁸² As agreed by the Working Group at its twenty-fourth session (para. 62, A/CN.9/831).

⁸³ Further to a request of the Working Group at its twenty-seventh session, the Secretariat has deleted paras. 50 to 52 of A/CN.9/WG.I/WP.99 and replaced them with a reference to the UNCITRAL Legislative Guide on Key Principles of a Business Registry (para. 46, A/CN.9/895). The Secretariat suggests the inclusion of a footnote in para. 52 supra that would read as follows: “The UNCITRAL Legislative Guide on Key Principles of a Business Registry discusses registration and prior reservation of business names, the importance of such names being unique, State’s criteria on business names requirements and the role of the business registry in assisting entrepreneurs choosing a name for their business”.

⁸⁴ For improved consistency of this section, the Secretariat has: (a) merged paras. 53 and 55 of A/CN.9/WG.I/WP.99 (para. 53 supra); and (b) included the second part of para. 53 of A/CN.9/WG.I/WP.99 (“Moreover ... for the UNLLO”) in a new para. 54 with some editorial adjustments.

single member model to a more complex multi-member entity.⁸⁵ In order to protect creditors and third parties dealing with the UNLLO and provide legal certainty, draft recommendation 7 establishes that an UNLLO should have at least one member at all times.⁸⁶ In the case of a single-member UNLLO, States should consider establishing a reasonable time period for the replacement of the member, if the members' agreement does not contain appropriate provisions in this regard (see rec. 21), so as to avoid an automatic dissolution of the UNLLO.⁸⁷

54. A member of an UNLLO may be any legal or natural person.⁸⁸ States should ensure a wide understanding of the concept of "legal person", which should include any legal entity capable of making an investment.⁸⁹ As an additional feature to enhance the flexibility of the UNLLO, draft recommendation 7 does not specify a maximum number of members for the UNLLO.⁹⁰

55. It should be noted that should a State have a strong policy preference that⁹¹ a legal person may not be a member of an UNLLO, these restrictions should be made clear in the legislation.

Recommendation 7: The law should provide that the UNLLO must have at least one member from the time of its formation until its dissolution, and that any legal or natural⁹² person may be a member of the UNLLO.

56. In order to provide legal certainty as to when the UNLLO comes into existence, this draft legislative guide recommends that the law should specify the time of formation of the UNLLO.⁹³ The time of formation is the time at which the UNLLO acquires its essential attributes, including legal personality, and, inter alia, limited liability of its members. Registering an UNLLO with the business registry⁹⁴ will confer such legal existence to the business entity. The State may choose the specific time, during the registration procedures, at which the UNLLO is formed. In keeping with international best practices,⁹⁵ the State may wish to specify that the time of formation of the legal personality of the UNLLO is the moment of issuance of the notice of the UNLLO's registration by the business registry, or after a specified period of time following the issuance of such notice.

57. Regardless of the system used to register an UNLLO (electronic, paper-based or a mixed registration system), upon fulfilling the necessary requirements, the UNLLO

⁸⁵ As agreed by the Working Group at its previous sessions (see paras. 24, 32 and 42 to 43, A/CN.9/800, paras. 67 and 74, A/CN.9/825, and para. 19, A/CN.9/831).

⁸⁶ The Secretariat has added this sentence further to the decision of the Working Group at its twenty-seventh session that emphasis should be placed on the requirement that an UNLLO should have at least one member at all times (para. 49, A/CN.9/895).

⁸⁷ The Secretariat has replaced the two final sentences ("Such a requirement ... easily enforceable") of this paragraph (para. 53 of A/CN.9/WG.I/WP.99) in order to be more consistent with: (a) the purpose of the commentary to rec. 7; and (b) the new drafting of rec. 9 that no longer requires to include the names and addresses of the UNLLO members in the formation document.

⁸⁸ As agreed by the Working Group at its twenty-fourth session (para. 64, A/CN.9/831).

⁸⁹ The Secretariat has added this sentence in keeping with a suggestion of the Working Group at its twenty-seventh session (para. 47, A/CN.9/895).

⁹⁰ See also para. 20 of A/CN.9/WG.I/WP.89.

⁹¹ At its twenty-seventh session, the Working Group agreed to delete the phrase "an UNLLO may have a maximum number of members, or that" before the phrase "a legal person" (para. 54 of A/CN.9/WG.I/WP.99) (para. 48, A/CN.9/895).

⁹² In keeping with a decision of the Working Group at its twenty-seventh session, the Secretariat has included the phrase "legal or natural" in the recommendation (para. 47, A/CN.9/895). The Working Group may wish to note that it also agreed to leave the issue of whether or not to divide rec. 7 into two for future consideration (para. 49, A/CN.9/895).

⁹³ The Working Group may wish to note that this draft legislative guide also deals with the dissolution and winding-up of an UNLLO in draft rec. 23 (rec.24 in A/CN.9/WG.I/WP.99/Add.1).

⁹⁴ This draft legislative guide supports the importance of the one-stop shop approach for business start-up and recognizes that the business registry may also function as a one-stop shop to support simultaneous registration with other relevant authorities (e.g. taxation and social security). The draft guide, however, takes the view that an UNLLO acquires its legal personality only upon registration with the business registry.

⁹⁵ As agreed by the Working Group at its twenty-fourth session (see para. 65, A/CN.9/831).

will receive a notice of registration from the designated State authority. The UNCITRAL Legislative Guide on Key Principles of a Business Registry considers, *inter alia*, the optimal approach for the registration of all businesses, including for an UNLLO.⁹⁶ In keeping with the recommendations of that 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.⁹⁷

58. Different States adopt different methods to administer business registration that vary according to the level and type of verification of the registration requirements performed by the business registry. The method chosen by a State, however, would not affect the recommendation in this draft legislative guide that the law should specify the time of formation of the UNLLO. In effect, regardless of the approach used by a State, the most appropriate time of formation is likely to be at the moment of issuance of the UNLLO's notice of registration with the business registry.^{98,99}

Recommendation 8: The law should specify when the UNLLO acquires its legal personality.¹⁰⁰

59. Depending on the type of business entity being created, States typically require different types and amounts of information to be submitted for valid formation.¹⁰¹ In a reflection of the intended simplicity of the UNLLO, this draft legislative guide limits the information required for the formation of the UNLLO to the minimum information necessary for its establishment and operation, as well as for the protection of third parties. In addition, draft recommendation 9 respects the principle that it should be as simple as possible for an MSME to provide the information required so as to avoid creating unnecessary burdens and to encourage compliance with the law.¹⁰² It is open to the UNLLO to include in its formation document any additional information it deems appropriate for inclusion, in particular if such information can assist it in accessing credit or attracting investors.¹⁰³

60. Draft recommendation 9 sets out the minimum mandatory information that must be submitted for the formation of the UNLLO. That information must include the name of the UNLLO as well as its business address. Where the business does not have a standard form address, a precise description of its geographic location should be inserted instead of the business address. In any event, the business address or geographic location of the UNLLO would be used for service or mailing purposes. The formation document should also include a statement of whether the UNLLO is managed by its member or members ("member-managed"), which may be expected

⁹⁶ This draft legislative guide takes the view that, outside of the specific information required for the valid registration of an UNLLO with the business registry (see draft rec. 9), matters relating to the operation of the business registry should be dealt with by legislation prepared on the basis of the UNCITRAL Legislative Guide on Key Principles of a Business Registry.

⁹⁷ See the UNCITRAL Legislative Guide on Key Principles of a Business Registry, rec. 23 and the relevant commentary.

⁹⁸ The Secretariat has redrafted this paragraph (para. 59 of A/CN.9/WG.I/WP.99) to reflect changes in the UNCITRAL Legislative Guide on Key Principles of a Business Registry and for improved consistency of this draft text on the UNLLO.

⁹⁹ The Secretariat has revised the commentary to draft rec. 8 to avoid redundancy and duplication of concepts.

¹⁰⁰ The Secretariat has revised the text of the recommendation as requested by the Working Group at its twenty-seventh session (paras. 53 and 54, A/CN.9/895).

¹⁰¹ The Secretariat has revised the commentary to draft rec. 9 in keeping with deliberations of the Working Group at its twenty-seventh session that the discussion on that recommendation should only consider the information required for the valid formation of the UNLLO (para. 52, A/CN.9/895), since the Working Group would discuss at a later stage which information on the formation and organization of the UNLLO should be publicly disclosed (see also *infra*, footnote 109). Moreover, the Secretariat has removed descriptions of terms that are now included in the list of definitions in para. 27 and eliminated redundancy in this part of the commentary.

¹⁰² The Working Group reached agreement on this point at its twenty-fourth session (see para. 69, A/CN.9/831).

¹⁰³ This approach is in keeping with the view expressed by the Working Group at its twenty-fourth session (see para. 74, A/CN.9/831). See also the discussion in footnote 169, *infra*.

to be the case in most instances, or whether it is to be managed by a designated manager or managers (“manager-managed”) (see rec. 11 below).¹⁰⁴

61. The final piece of mandatory information that must be provided for formation of the UNLLO is the name of each manager. If the business is member-managed, the name of each member must be included; if the business is manager-managed, the name of each designated manager must be included. Information on the residential address of each manager is not required in the formation document; the rationale for this is that a service address would be sufficient for the State to monitor the maintenance of the UNLLO’s books and records.¹⁰⁵

62. This draft guide’s approach to the information that an UNLLO must provide to State authorities would be expected to meet the requirements of the international standards on beneficial ownership. These information requirements¹⁰⁶ should thus assuage any concerns that the UNLLO legal form could be misused for illicit purposes, including money-laundering and terrorist financing.¹⁰⁷ 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.

63. In order to ensure that the formation document of the UNLLO is kept as current as possible, the law should permit each manager to make any necessary amendment to it. While the business registry law in the State will contain provisions on any requirements for the amendment of the formation document, managers will have an incentive to keep at least the public information of the UNLLO current so as to avoid potentially misleading third parties dealing with the UNLLO (see also rec. 14 below).¹⁰⁸

¹⁰⁴ As agreed by the Working Group at its twenty-fifth session (para. 84(b), [A/CN.9/860](#)).

¹⁰⁵ The Secretariat suggests that the UNLLO should be required to disclose information on the name of the each manager in order to provide protection for third parties since the manager is the person with legal authority to bind the UNLLO in its dealings with such parties. Information on the residential address of the managers should not be required for the reason indicated in para. 61 and in order to prevent any risk to the personal safety of the managers. Moreover such information would not be essential to fulfil the objective of protection of third parties. Other information that could be made public are the name and address of the UNLLO.

¹⁰⁶ See, also, draft recs. 25 and 26 on record-keeping, inspection and disclosure of UNLLO information to its members.

¹⁰⁷ 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_Recommendations.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. For consideration of these issues by the Working Group, see paras. 27 and 41 of [A/CN.9/800](#) and paras. 47 to 55, of [A/CN.9/825](#), as well as information contained in paras. 26 to 32 of [A/CN.9/WG.I/WP.82](#) and paras. 21 and 26 of [A/CN.9/WG.I/WP.89](#).

¹⁰⁸ Further to the request of the Working Group at its twenty-seventh session, the Secretariat has deleted rec. 10 in [A/CN.9/WG.I/WP.99](#) since the goal of keeping information current is dealt with in the UNCITRAL Legislative Guide on Key Principles of a Business Registry (see, for example, recs. 4, 10 and 30 and relevant commentary) (para. 57, [A/CN.9.895](#)).

Recommendation 9: The law should provide that only the following information is required for the valid formation of the UNLLO:¹⁰⁹

- (a) The name of the UNLLO;
- (b) The business address or precise geographical location of the UNLLO;
- (c) A statement of whether the UNLLO is managed by its members (member-managed) or by a designated third-party manager (manager-managed); and
- (d) The name of each manager.

C. Organization of the UNLLO

64. As noted above in respect of draft recommendation 1 (see paras. 31 and 32 and 34), 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 those cases in which the law is mandatory and cannot be modified by member agreement. The rules that are mandatory 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 the UNLLO. When the members' agreement is silent on a non-mandatory issue, the provisions in the default rules in this draft legislative guide are meant to fill any gap.

65. Where an UNLLO has only one member, the member's agreement will still be required, and may be in writing or implied by conduct.¹¹⁰ The broad flexibility permitted for the form of the members' agreement recognizes that in the case of many MSMEs there may be no formal written agreement, and that, in such cases, members should be able to rely on oral agreements and agreement implied by conduct. However, it may be in the best interests of members to have a written agreement, since oral members' agreements and agreements implied by conduct are more difficult to prove in the event of a dispute.¹¹¹

66. This draft legislative guide does not require that an UNLLO members' agreement be made public.¹¹² 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 registration authorities each time a change is made to the members' agreement.

Recommendation 10: The law should provide that the members of the UNLLO may adopt a members' agreement in any form, including an agreement that is written, oral or implied by conduct. The members may agree in their members' agreement on any matter relating to the UNLLO, except in respect of the

¹⁰⁹ In keeping with deliberations of the Working Group at its twenty-seventh session, the Secretariat has: (a) deleted rec. 9(a) ("information that will be made public") (see also, *supra*, footnote 101) and rec. 9(b) ("Information that will not be made public") in [A/CN.9/WG.I/WP.99](#) (paras. 52 and 54, [A/CN.9/895](#)); and (b) further clarified rec. 9(c) (rec. 9(a)(iii) in [A/CN.9/WG.I/WP.99](#)) (para. 53, [A/CN.9/895](#)).

¹¹⁰ The Secretariat has removed reference to an "oral agreement" from the sentence relating to a sole-member UNLLO.

¹¹¹ As the term "member agreement" now appears in the list of definitions in para. 27, the Secretariat has removed descriptions of the term from the commentary. The Secretariat has also included the phrase "implied by" to the text of the commentary and rec. 10 (rec. 11 in [A/CN.9/WG.I/WP.99/Add.1](#)) in their discussion of conduct.

¹¹² In keeping with deliberations of the Working Group at its twenty-seventh session (see footnote 101, *supra*), the Secretariat has eliminated references to public disclosure in the commentary to rec. 10 (rec. 11 in [A/CN.9/WG.I/WP.99/Add.1](#)) and made some modifications in terms of drafting.

mandatory rules set out in recommendations 1, 2, 3, 6, 7, 8, 9, 13(a), 14, 19, 20, 23(c), 25 and 26.¹¹³

67. The organization of the UNLLO should account for problems that may occur in multi-member privately held companies with a relatively small number of members who have substantial participation in its management and operation, as will likely be the case for most UNLLOs.

68. Draft recommendation 11 permits members of an UNLLO to determine by way of their members' agreement how the UNLLO should be managed. Members could agree that the UNLLO will be manager-managed, in which case one or more managers will be elected by the members in accordance with the members' agreement (see draft rec. 15), and those managers will take on the management of the regular course of business of the UNLLO.

69. A professional manager approach (which is common in public companies), however, may not fit the governance needs of many privately held companies, particularly when they are micro and small enterprises, and, as noted above, where members most often take on management roles. Draft recommendation 11 therefore also permits members to agree that the UNLLO be managed by members.

70. Where there is only one member of an UNLLO, that member will be the manager, unless the member appoints a manager. Enacting States could provide that UNLLOs with only a few members would also be subject to the default rule of member-management. In such cases, the State should specify in the law prepared on the basis of this draft legislative guide the threshold number of members at which the default rule would no longer apply.¹¹⁴

Recommendation 11: The law should provide that the UNLLO may be member-managed or manager-managed. A single member UNLLO will be member-managed unless otherwise agreed.¹¹⁵

71. When the UNLLO is member-managed, its members will have equal voting rights, unless they agree otherwise in the members' agreement. However, this draft legislative guide also enables a voting structure based on percentage of ownership by the UNLLO members (see draft rec. 16).¹¹⁶

72. Further, unless there is agreement to the contrary, matters that arise in the ordinary course of business of the UNLLO will be decided by a majority¹¹⁷ of its members, and decisions that are outside of the ordinary course of business of the UNLLO would require the approval of its members by qualified majority. Decisions

¹¹³ At its twenty-seventh session, the Working Group agreed to defer consideration of rec. 10 (rec. 11 in [A/CN.9/WG.I/WP.99/Add.1](#)) in order to be able to ascertain correctly the mandatory recommendations (para. 58, [A/CN.9/895](#)). See also, *supra*, footnote 48.

¹¹⁴ At its twenty-seventh session, the Working Group deliberated the default rule and some delegations supported the view of adding commentary indicating that it was also recommended that enacting States should provide that UNLLOs with only a few members would also be subject to the default rule of member-management (see para. 69, [A/CN.9/895](#)).

¹¹⁵ At its twenty-seventh session, the Working Group agreed to change rec. 11 (rec. 12 in [A/CN.9/WG.I/WP.99/Add.1](#)) as indicated (see paras. 62 and 69, [A/CN.9/895](#)). The Secretariat has redrafted the commentary to make it align with the modifications in the recommendation.

¹¹⁶ The Secretariat has deleted the sentence "This is also ... otherwise agreed" (para. 9 of [A/CN.9/WG.I/WP.99/Add.1](#)) and replaced it with a cross-reference to rec. 16 to suggest to the Working Group that the discussion of the percentage of ownership be placed before the discussion of voting rights. If the Working Group determines to retain the current structure, then the Secretariat would suggest including additional information regarding percentages in the commentary to rec. 12.

¹¹⁷ At its twenty-seventh session, the Working Group agreed that the rule for decisions on matters outside of the ordinary course of business should instead be that of a "qualified majority" such as, for example, a two-thirds majority. It was also agreed that the phrase "simple majority" as used in the text should be modified by referring either to "majority" or "absolute majority" (para. 63, [A/CN.9/895](#)). The Secretariat has made the necessary changes to references to "majority" throughout the text. Additionally, the Secretariat has included in the terminology section definitions of the terms (para. 63, [A/CN.9/895](#)).

outside of the ordinary course of business would include decisions such as those relating to dissolution and winding-up of the UNLLO, to its conversion to another business form, or to changing its organization from a member-managed to a manager-managed model, or vice versa (see also recs. 22 to 24).

73. This draft legislative guide takes the view that it is unnecessary for the UNLLO legislation to specify every aspect of the UNLLO's operations, and instead leaves it to members to decide in their members' agreement on the management of the UNLLO. In order to manage the UNLLO fairly, effectively and transparently, members may wish their agreement to include rules in respect of the following issues:¹¹⁸

(a) Maintenance of timely records of the members' decisions, both inside and outside of the ordinary course of business of the UNLLO, as well as the form in which those records should be maintained;¹¹⁹

(b) Any requirement in respect of members' meetings, including their frequency and location, as well as any limitation thereon;

(c) Any requirement in terms of who can call a members' meeting;

(d) The conduct of members' meetings, including whether they may be held by technological means or by written consent;

(e) Any notice period required prior to the holding of a members' meeting;

(f) The form of any notice required of the members' meeting (for example, in writing or in any other form), and the information (if any) that should be attached to the notice (for example, the UNLLO's financial information);

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

(h) Any decisions that would require a majority that differs from the default rule of a majority vote for decisions in the ordinary course of business or unanimity for decisions outside of the ordinary course of business of the UNLLO.¹²⁰

Recommendation 12: The law should provide that, unless otherwise agreed in the members' agreement:^{121,122}

(a) The members of the UNLLO have voting rights¹²³ in proportion to their respective percentage of ownership of the UNLLO, as stated in the members' agreement. When the percentage of ownership of the UNLLO is not so stated, the members of the UNLLO have equal voting rights;

(b) Any difference arising between members as to matters in the ordinary course of business shall be decided by a majority; and

¹¹⁸ As agreed by the Working Group at its twenty-sixth session (paras. 39 to 47, [A/CN.9/866](#)).

¹¹⁹ As agreed by the Working Group at its twenty-sixth session (para. 44, [A/CN.9/866](#)). For additional detail or the form in which such records should be maintained, see paras. 119 and 120 and draft rec. 25 (rec. 26 in [A/CN.9/WG.I/WP.99/Add.1](#)).

¹²⁰ The Secretariat has made some editorial modifications to para. 73 and would suggest placing the content of the paragraph before rec. 10.

¹²¹ The Secretariat has included the phrase "in the members' agreement" to the chapeau of rec. 12 (rec. 13 in [A/CN.9/WG.I/WP.99/Add.1](#)) to avoid a situation in which a majority agrees ex post facto to abandon the default rule present in rec. 12(c).

¹²² The Secretariat suggests placing the discussion of ownership of the UNLLO before rec. 12, which presents voting rights in proportion to percentage of ownership. See also, supra, footnote 116.

¹²³ Changes to rec. 12 (rec. 13 in [A/CN.9/WG.I/WP.99/Add.1](#)) were made pursuant to the drafting suggestions made by the Working Group at its twenty-seventh session (para. 67, [A/CN.9/895](#)), and modified by the Working Group at its twenty-eighth session to indicate proportional ownership (para. 159, [A/CN.9/900](#)). In addition, the Working Group provided the Secretariat with the flexibility to use the term "voting rights" instead of "rights of control" (para. 67, [A/CN.9/895](#)). That suggestion has been implemented throughout the text of the draft legislative guide.

(c) Any difference arising between members as to matters outside of the ordinary course of business shall be decided by a qualified majority.

D. Management by managers or members¹²⁴

74. Fiduciary duties are broad standards of conduct that reduce the risk of members and managers acting opportunistically, and encourage members and managers to act in favour of promoting the welfare of the UNLLO, and, indirectly, its members. Such duties may be separated into: (1) a duty of care; (2) 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; (3) a duty to disclose information to all members of the UNLLO;¹²⁵ and (4) a duty of good faith and fair dealing. While the draft legislative guide is not modelled on any specific legal tradition, the inclusion of such duties tend to be a standard feature of business associations law; for example, fiduciary duties are found in each of the simplified corporate forms examined by the Working Group when it first took up its mandate.¹²⁶

75. Fiduciary duties offer protection against a manager's and fellow member's pursuit of personal interest and any excessively negligent behaviour on their part. Fiduciary duties cannot be used *ex post facto* to subject the business judgment of managers to criticism when the decisions are made in the performance of their official duties.

76. The rule establishing a manager's duties in draft recommendation 13(a)¹²⁷ is mandatory and cannot be varied or eliminated by agreement. No internal agreement could eliminate or limit the liability of a manager: (i) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; or (ii) for any transaction from which the manager derived an improper personal benefit.¹²⁸

77. Members could, however, agree to include in their members' agreement a provision that they do not owe fiduciary duties to each other.¹²⁹ Similarly, members could agree among themselves how to apportion liability or whether to forego limited liability protection.¹³⁰ Members can also agree that a manager must adhere to a standard that is higher than that established in draft recommendation 13(a).

78. Finally, members may specify in their agreement that certain activities are permitted for managers and do not constitute a breach of the duties established in draft recommendation 13(a). Permitting freedom of contract of the members to this extent could be useful in the context of UNLLOs, since it would allow members to derogate from a rigid corporate legal framework which may not be necessary, while

¹²⁴ The Secretariat has slightly modified the title of this section to make it more consistent with the commentary and the recommendation.

¹²⁵ See also, para. 117 and rec. 25 (rec. 26 in [A/CN.9/WG.I/WP.99/Add.1](#)) for more details on the duty to disclose.

¹²⁶ See, *supra*, para. 6 and paras. 24 and 25 and the corresponding tables in [A/CN.9/WG.I/WP.82](#), considered at the twenty-second session of the Working Group. At its twenty-eighth session, the Working Group agreed to continue to use "fiduciary duty" in the legislative guide, but suggested to note that the term was not intended to import law from one legal tradition into another (para. 147, [A/CN.9/900](#)).

¹²⁷ Draft rec. 14 in [A/CN.9/WG.I/WP.99/Add.1](#).

¹²⁸ Similar approaches may be found in various legislative enactments in respect of fiduciary duties. For example, the United States Revised Uniform Limited Liability Act of 2006 clarifies the ability of members to define and limit the duties of loyalty and care that members owe to each other and to the business entity. See, also, the Delaware General Corporation Law, Section 102(b) (7), which allows the members to limit the duty of care by agreeing to eliminate or limit the personal liability of a manager to the business entity or its members in such cases.

¹²⁹ See, *infra*, footnote 135.

¹³⁰ At its twenty-seventh session, the Working Group agreed to include reference to proportional liability and to consider adding reference to foregoing limited liability protection entirely. (para. 36, [A/CN.9/895](#)).

still requiring appropriate protection for the UNLLO, its members and third parties dealing with it.¹³¹

79. Legal claims against managers or members in breach of their fiduciary duties may be brought directly before a court or by way of an alternative dispute settlement mechanism (see rec. 26). Often it will be the UNLLO itself, rather than an individual member, that would have a cause of action for a breach of a fiduciary duty by a member or manager. Ordinarily, the manager would be responsible for bringing an action on behalf of the UNLLO. However, in instances in which the 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.¹³²

Recommendation 13: The law should provide that:

(a) A manager of the UNLLO owes: (i) a duty of care; (ii) a duty of loyalty; (iii) a duty to disclose information to all members of the UNLLO;¹³³ and (iv) a duty of good faith and fair dealing;¹³⁴ and

(b) Unless otherwise stated in the member's agreement, fiduciary duties also apply to members of the UNLLO.¹³⁵

80. Each manager of the UNLLO has the authority to legally bind the UNLLO. Restrictions may be agreed upon in the members' agreement in respect of the extent to which each manager can bind the UNLLO (for example, only up to a certain monetary threshold), or to vary the default rule that each manager can legally bind the UNLLO. Such modifications of the default rules will be effective between the members of the UNLLO.

81. However, such restrictions or variations will not be effective against third parties dealing with the UNLLO in the ordinary course of its business 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 a members' agreement has placed on the authority of a manager, the UNLLO will nonetheless be bound by a decision of that manager in the ordinary course of business

¹³¹ The Secretariat has adjusted the commentary in former paras. 15 and 16 of [A/CN.9/WG.I/WP.99/Add.1](#) for improved clarity. The Working Group may wish to consider how the first sentence of paragraph 78 should be read in light of the mandatory nature of rec. 13(a).

¹³² At its twenty-eighth session, the Working Group agreed to include in the commentary a paragraph on the enforcement of fiduciary duties that should include how legal claims can be brought individually and collectively against managers in breach, and including alternative dispute resolution (para. 149, [A/CN.9/900](#)). The Secretariat has removed former para. 15 of [A/CN.9/WG.I/WP.99/Add.1](#) from the draft legislative guide to eliminate redundancy with para. 74 (para. 12 of [A/CN.9/WG.I/WP.99/Add.1](#)) and the redrafted rec. 13 (rec. 14 in [A/CN.9/WG.I/WP.99/Add.1](#)).

¹³³ The Working Group may wish to decide whether reference to the duty to disclose information is necessary in the text of the recommendation, and if so, to determine the extent of the discussion it receives, including whether to describe types of information that must be disclosed, the timeline for disclosure, and any exceptions to the requirements.

¹³⁴ At its twenty-eighth session, the Working Group considered whether the standard should be subjective or rather whether the manager must act in the best interests of the UNLLO. Good faith was included in the recommendation to better reflect the commentary found in para. 74 (para. 12 of [A/CN.9/WG.I/WP.99/Add.1](#)) (para. 150, [A/CN.9/900](#)). In the alternative, the Secretariat suggests that the previous versions of the recommendation could also be redrafted to something along the lines of:

“The law should provide that a manager must act in good faith, with the care that a person in a like position would reasonably exercise under similar circumstances and in a manner that the manager reasonably believes to be in the best interests of the UNLLO.”

¹³⁵ The Working Group at its twenty-eighth session agreed that the approach should be changed from an “opt in” fiduciary duty to one owed to all other members unless otherwise agreed (para. 147, [A/CN.9/900](#)). The Secretariat has therefore made adjustments to the commentary and to the recommendation. The Working Group may also wish to consider whether the recommendation should provide for a legal cause of action, particularly with regard to derivative suits.

regardless of whether that decision exceeds the manager's authority as limited by the members' agreement.

Recommendation 14: The law should provide that each manager¹³⁶ individually has the authority to bind the UNLLO unless otherwise agreed. Restrictions upon this authority will not be effective against third parties dealing with the UNLLO in the ordinary course of business without proper notice.¹³⁷

82. The members may establish rules in their members' agreement for the appointment and removal of a manager.¹³⁸ In the absence of such agreement, draft recommendation 15¹³⁹ provides a default rule that such decisions should be made by a majority of the members.

83. In the case of a manager-managed UNLLO, should a manager become unavailable (through death or otherwise), the members would be required to appoint another manager under the terms of the members' agreement, and to list the name of the manager pursuant to recommendation 9(d). Appointing another manager would be important to ensure that amendments to the UNLLO's formation document can validly be made (see also para. 63 above).

Recommendation 15: The law should provide that, unless otherwise agreed by the members, a manager or managers may be elected and removed by a majority decision of the members.

E. Percentage of the ownership of the UNLLO and contribution by members¹⁴⁰

84. Most UNLLOs are unlikely to require a complex organizational structure. Recommendation 16¹⁴¹ therefore provides a default rule to establish the percentage of ownership of the UNLLO equally. However, given the "freedom of contract" principle that governs the draft legislative guide, it should be permissible for members to decide the percentage of ownership among themselves in the members' agreement.

85. It should also be noted that more complex ownership structures could be established by the members in their members' agreement, including different classes

¹³⁶ The Working Group agreed at its twenty-eighth session that deletion of the phrase "publicly disclosed" from rec. 14 (rec. 15 in [A/CN.9/WG.I/WP.99/Add.1](#)) was necessary to reflect the intention of the recommendation (para. 153, [A/CN.9/900](#)).

¹³⁷ At its twenty-eighth session, the Working Group agreed that rec. 14 should reflect commentary in paras. 80 and 81, *supra* (paras. 17 and 18 of [A/CN.9/WG.I/WP.99/Add.1](#)) to clarify that members could agree to vary the default rules, but that notice of the change to third parties was mandatory to be effective (para. 153, [A/CN.9/900](#)). The commentary has therefore been adjusted accordingly and has removed reference to publicly disclosed information. The Working Group may wish to further discuss how the UNLLO could properly provide notice. Given that the commentary to rec. 14 permits members of the UNLLO to deviate from the default rule, the Secretariat has added the phrase "unless otherwise agreed." in the text of the recommendation. The Working Group may wish to remove rec. 14 from the list of mandatory rules when it considers rec. 10.

¹³⁸ As agreed by the Working Group at its twenty-fifth session (para. 84(d), [A/CN.9/860](#)).

¹³⁹ Draft rec. 16 in [A/CN.9/WG.I/WP.99/Add.1](#).

¹⁴⁰ At its twenty-eighth session, the Working Group decided to modify the title to part E and provided the Secretariat with draft text for recs. 16 and 17 (recs. 17 and 18 in [A/CN.9/WG.I/WP.99/Add.1](#)) (para. 158, [A/CN.9/900](#)). Consequently, the Secretariat placed recs. 16 and 17 together and made changes to the commentary to reflect the concepts of both ownership and contributions.

¹⁴¹ Draft rec. 17 in [A/CN.9/WG.I/WP.99/Add.1](#).

and types of membership, as well as special rights that might attach to such different classes of membership.¹⁴²

86. Draft recommendation 17 further elaborates on draft recommendation 16 by requiring the law to permit members maximum flexibility to decide upon the amount and type of their agreed contributions to the UNLLO.¹⁴³ It is recommended that members maintain a record of the amount and type of contribution of each member to ensure that the rights of the members are respected (see also draft recs. 25 and 26 below).

87. Since the UNLLO is not required to have a capital structure, it is not necessary that members make contributions to it in order for it to exist. The UNLLO need not necessarily have assets at its formation, since assets would be generated through its operations.¹⁴⁴

88. Where members agree to make contributions to the UNLLO, but do not specify the amount of the contributions, draft recommendation 17 provides that, in keeping with the general approach to ownership¹⁴⁵ and management of the UNLLO, equivalent contributions should be made by each member.

89. In specifying in their members' agreement the types of contribution that members of the UNLLO may make, members may wish to consider the following possibilities: tangible or intangible property or 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, local law may restrict the types of contribution that may be made. For example, in some States, the provision of services is not permitted as a contribution to the establishment of a business entity. In such cases, those restrictions may be specified in the law prepared on the basis of this draft legislative guide.¹⁴⁶

90. Moreover, determination of the value of each contribution should be left to the members of the UNLLO, as they are in the best position to determine that value. Should members wish to include duties to each other in terms of the accurate value of their contribution, this may be accomplished in the members' agreement. Any other mechanism, such as requiring an audit or other external valuation method, is likely to be too burdensome for MSMEs.

Recommendation 16: The law should provide that members of the UNLLO:

(a) Should state in the members' agreement their respective percentage of ownership of the UNLLO; and

(b) Share the ownership of the UNLLO equally when that percentage is not so stated.

¹⁴² The Working Group agreed at its twenty-sixth session that this draft legislative guide should start with the simplest model and should establish the default rule to be one of equal voting rights and equal distributions, unless otherwise agreed in the members' agreement. The Working Group also agreed that this legislative guide should permit the establishment of more complex ownership structures, including special rights, which could be mentioned in the commentary (paras. 27 and 29, [A/CN.9/866](#)).

¹⁴³ As agreed by the Working Group at its previous sessions (para. 29 of [A/CN.9/831](#) and para. 34, [A/CN.9/866](#)).

¹⁴⁴ The Secretariat has removed para. 21 of [A/CN.9/WG.I/WP.99/Add.1](#), given the Working Group's decision at its twenty-eighth session to provide maximum flexibility for enacting States (para. 156, [A/CN.9/900](#)).

¹⁴⁵ The Working Group agreed at its twenty-sixth session that in order to achieve a common understanding, the next draft of the text should explain what was meant by the term "share" and should present possible alternatives for more neutral terms (para. 25, [A/CN.9/866](#)). Since this draft legislative guide attempts to create a system for a legal business form that is not dependent on the corporate model, it refers to "interest" and "ownership" to indicate that portion of the UNLLO that is owned by a particular member.

¹⁴⁶ As agreed by the Working Group at its twenty-sixth session (paras. 34 to 35, [A/CN.9/866](#)).

Recommendation 17: The law should provide that, when deciding the members' respective percentage of ownership of the UNLLO, the members of the UNLLO are permitted to agree upon contributions, if any, made to the UNLLO, including the amount, type and value of such contributions. In the absence of such agreement, contributions that are made to the UNLLO should be equivalent for all members.¹⁴⁷

F. Distributions

91. In keeping with the general default approach of the UNLLO, this draft legislative guide provides that members will share equally in the ownership of the UNLLO and in any distributions made by it unless the members have otherwise agreed in their members' agreement.¹⁴⁸

92. The members of the UNLLO may also agree on the type of distribution (for example, including cash or property of the UNLLO) as well when such distributions may be made. It is important to note, however, that some States may not permit non-monetary distributions and that, in such cases, States should specify those restrictions in the UNLLO law enacted on the basis of this draft legislative guide.

Recommendation 18: The law should provide that distributions be made to members in proportion to their respective percentage of ownership of the UNLLO as stated in the members' agreement. When the percentage of ownership of the UNLLO is not so stated, any distribution by the UNLLO shall be made equally among its members.

93. Although the amount, type and timing of distributions may be subject to the members' decision, this draft legislative guide includes mandatory provisions governing distributions aimed at protecting third parties dealing with the UNLLO. In order to protect such parties, the members of the UNLLO cannot contract out of the rule prohibiting distributions from being made by the UNLLO when such a distribution would violate either an insolvency test, as reflected in draft recommendation 19(a), or a balance sheet test, as reflected in draft recommendation 19(b). Under the insolvency test, the UNLLO must still be able to pay its debts upon giving effect to the distribution, while the balance sheet test ensures that distributions can only be made if the UNLLO's remaining assets exceed its total liabilities.¹⁴⁹

94. This mandatory rule, in conjunction with the clawback provision in draft recommendation 20, is intended to protect third parties and creditors who are dealing with the UNLLO from any dissipation of the UNLLO's assets through improper distributions to its members.

95. In most cases, the UNLLO will be member-managed, and holding each member liable in draft recommendation 20 to return the amount of the improper distribution

¹⁴⁷ Changes to the recommendations reflect the agreement of the Working Group at its twenty-eighth session (paras. 156 and 158, [A/CN.9/900](#), with the additional drafting suggestion in para 159(b)). The Secretariat has modified the phrase "be made in equal amounts" to "be equivalent for all members" for clarity.

¹⁴⁸ The Working Group agreed to adjust the text of rec. 18 (rec. 19 in [A/CN.9/WG.I/WP.99/Add.1](#)) and its commentary to reflect the agreement taken with respect to proportionality in the revised version of rec. 12 (rec. 13 in [A/CN.9/WG.I/WP.99/Add.1](#)) (paras. 159(c) and 160, [A/CN.9/900](#)). The Secretariat has implemented the changes accordingly.

¹⁴⁹ At previous sessions of the Working Group, a concern was expressed as to whether the insolvency and balance sheet tests were appropriate for MSMEs or if they might be too complex, but no decision was reached in that regard. See para. 31, [A/CN.9/831](#) and para. 30, [A/CN.9/866](#). The Working Group may wish to note that, on their face, these tests may appear to be more complex than they are, since most MSMEs are able to track their financial status quite accurately and may even rely on the many simple mobile applications that exist for such purposes.

should act as an adequate disincentive for the member-managed situation.¹⁵⁰ Where the UNLLO is manager-managed, the duties set out in draft recommendation 13(a) along with draft recommendations 19 and 20 should provide an adequate basis on which to find managers liable should they make improper distributions.

Recommendation 19: The law should prohibit distributions from being made to any member if upon giving effect to such distribution:

(a) The UNLLO would not be able to pay its debts as they become due in the ordinary course of business; or

(b) The UNLLO's total assets would be less than the sum of its total liabilities.

96. In keeping with the rule on improper distributions established in draft recommendation 19, draft recommendation 20 provides an operative provision that 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 provide an incentive to members to ensure that any distributions made to them would not leave the UNLLO insolvent or with greater liabilities than assets.

97. It should be noted that payments of reasonable compensation for services rendered¹⁵¹ and for bona fide debt owed by the UNLLO to a member should not be considered as distributions, and would thus not be subject to the clawback provision in draft recommendation 20.

98. In addition, as noted in paragraph 95 above, managers that make distributions in violation of one of the tests in draft recommendation 19 could also be held liable to the UNLLO.¹⁵²

Recommendation 20: The law should provide that each member who received a distribution, or any portion of a distribution, is liable to reimburse the UNLLO for the entire amount of the distribution received if that distribution violates recommendation 19.¹⁵³

G. Transfer of rights

99. Because of the nature of the UNLLO as a privately held MSME, its members are likely to value the composition of its membership and to resist transfers of ownership without the approval of other members. In addition, there is unlikely to be a ready market for the sale and transfer of an ownership interest in an UNLLO.

100. The ownership stake of an UNLLO member entitles it to exercise two sets of rights: financial rights to share in the profits and losses of the UNLLO and to receive distributions, and voting rights to participate in the management and control of the UNLLO, including fiduciary rights and information rights. Moreover, the default rule for most aspects of the UNLLO as established in this draft legislative guide is that members share in rights on an equal basis.

¹⁵⁰ For consistency, the Secretariat has removed the reference to a lack of a specific provision holding managers liable for making improper distributions (para. 32 of [A/CN.9/WG.I/WP.99/Add.1](#)). See the discussion of the Working Group at its previous sessions (para. 32, [A/CN.9/831](#) and para. 33, [A/CN.9/866](#)).

¹⁵¹ See para. 30, [A/CN.9/866](#).

¹⁵² The phrase "to the UNLLO" was inserted into the text of the paragraph (para. 35 of [A/CN.9/WG.I/WP.99/Add.1](#)) as agreed by the Working Group at its twenty-eighth session (para. 162, [A/CN.9/900](#)).

¹⁵³ The Secretariat has modified the text and commentary of recs. 19 and 20 (recs. 20 and 21 in [A/CN.9/WG.I/WP.99/Add.1](#)) to clarify that a member is not liable for the entire distribution if only a portion was received and is not liable for the entire distribution when only a portion was made in violation of rec. 19.

101. Consistent with this general approach, the default rule should be that members of the UNLLO are permitted to transfer their financial rights, unless they have agreed otherwise in their members' agreement. Also bearing in mind the general nature of UNLLOs, the default rule in respect of the transfer of voting rights in the UNLLO should be that such rights are not transferable by members unless they have agreed otherwise in their members' agreement. This latter rule reflects the idea that, given the particular characteristics of the UNLLO, non-transferring members must consent to changes in the management and control of the UNLLO. These rules are reflected in draft recommendation 21.

102. In the situation of the death of a single member of the UNLLO, complications could arise in that the member's financial rights might be transferable, but not the member's governance rights. The members' agreement should contain appropriate provisions to provide any necessary clarity in that circumstance.¹⁵⁴

Recommendation 21: The law should provide that members may transfer their financial rights in the UNLLO, but not their voting rights. Members of the UNLLO may vary this rule in the members' agreement.¹⁵⁵

H. Restructuring or conversion

103. As noted above (para. 53) in respect of draft recommendation 7, this draft legislative guide is intended to permit the UNLLO to evolve from a very small single member enterprise to a more complex multi-member business entity,¹⁵⁶ and possibly to convert into another legal business form altogether. That approach is reflected in draft recommendation 22, which permits the members of the UNLLO to agree to restructure the UNLLO or to convert it into a different legal form.

104. As noted above in paragraph 72 in connection with draft recommendation 12, a decision on the restructuring or conversion of the UNLLO would be a decision outside of the ordinary course of business, and would thus require a decision by qualified majority, unless otherwise agreed by the members.¹⁵⁷

105. The State in which the UNLLO would restructure or convert to another legal form 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. Such safeguards may already exist in legislation providing for conversion into other legal business forms,¹⁵⁸ and could consist, for example, of notice periods, publication requirements or rules on the transfer of third party rights to the new business form.

Recommendation 22: The law should provide that the members of an UNLLO may agree to restructure it or convert it into another business form by qualified majority.¹⁵⁹

¹⁵⁴ The Working Group may wish to consider providing a default rule in the draft legislative guide for such instances.

¹⁵⁵ For greater clarity of the recommendation (rec. 22 in [A/CN.9/WG.I/WP.99?/Add.1](#)), the Secretariat has: (a) replaced "non-financial rights" with "voting rights"; (b) deleted the phrase "in the UNLLO" after "voting rights"; and (c) inserted the phrase "in the members".

¹⁵⁶ See paras. 24 and 32 of [A/CN.9/800](#), paras. 67 and 74 of [A/CN.9/825](#), and para. 19 of [A/CN.9/831](#).

¹⁵⁷ As agreed by the Working Group at its twenty-fifth session, the level of agreement among members for restructure and conversion of the UNLLO should be commensurate with that required for dissolution and winding-up of the UNLLO (para. 90, [A/CN.9/860](#)).

¹⁵⁸ As agreed by the Working Group at its twenty-fifth session (para. 91, [A/CN.9/860](#)).

¹⁵⁹ The Secretariat has added the phrase "agree to" and changed "agreement" to "majority."

I. Dissolution and winding-up

106. Draft recommendation 23, subparagraph (a), establishes that the members of the UNLLO may decide in their members' agreement that the UNLLO will be dissolved and wound up on the occurrence of an event specified in that agreement. Should the members of the UNLLO not have established terms under which the UNLLO would be dissolved and wound up, they may decide by qualified majority to dissolve and wind up the entity as indicated in subparagraph (b) of draft recommendation 23. This level of required consent is commensurate with that required in respect of a decision by members on restructuring the UNLLO or converting it into another legal form, as well as reflecting the default rule for decisions made by members on matters outside of the ordinary course of business.¹⁶⁰

107. Draft recommendation 23, subparagraph (c), is a mandatory rule that members are not entitled to vary by agreement. A judicial or administrative decision made pursuant to the law of the State that the UNLLO is dissolved must be respected by the members of the UNLLO, and could include, for example, a decision by a bankruptcy court.¹⁶¹

108. Again, the State in which the UNLLO would be dissolved or wound up may wish to ensure that adequate safeguards are in place to protect third parties dealing with the UNLLO from any adverse effects that could arise from its dissolution or winding-up. Such safeguards may already exist in other legislation providing for dissolution or winding-up of legal business forms.¹⁶²

Recommendation 23: The law should provide that the UNLLO shall be dissolved and wound up in the following circumstances:

- (a) On the occurrence of any event that is specified in the members' agreement as causing the dissolution of the UNLLO;**
- (b) On a vote by qualified majority of the members; or**
- (c) Upon the rendering of a judicial or administrative decision that the UNLLO is dissolved.**

J. Dissociation or withdrawal

109. Members of an UNLLO will often have equal financial and voting rights; indeed, that is the default rule throughout this legislative guide. It is further reflected in the fact that the default rule requires decisions made outside of the ordinary course of business of the UNLLO to be made by a qualified majority of the members (draft rec. 12(c)). As noted above, such extraordinary matters would include issues relating to the very existence of the UNLLO, such as its restructuring, conversion to a different legal business form, dissolution and winding-up. Similarly, the default rule for resolving differences among members on matters in the ordinary course of business of the UNLLO is that such matters may be decided by a majority of members (draft rec. 12(b)), thus providing a convenient way to resolve more routine differences of view among the UNLLO members. These two default rules provide a reasonable, coherent and stable decision-making system for members to resolve basic disputes and to continue to conduct the affairs of the UNLLO, and allow¹⁶³ any member that does not agree with important decisions that could affect the very existence of the

¹⁶⁰ As agreed by the Working Group at its twenty-fifth session (para. 87, [A/CN.9/860](#)).

¹⁶¹ As agreed by the Working Group at its twenty-fifth session (para. 85, [A/CN.9/860](#)).

¹⁶² As agreed by the Working Group at its twenty-fifth session (para. 86, [A/CN.9/860](#)). See also para. 105 *supra*.

¹⁶³ Given the Working Group's decision to replace unanimity with qualified majority (para. 63, [A/CN.9/895](#)), there would no longer be an effective veto. The Secretariat has therefore amended this paragraph and incorporated the concept of ownership rights from rec. 12 (rec. 13 in [A/CN.9/WG.I/WP.99/Add.1](#)).

UNLLO to dissent. Depending on the percentage of ownership of the UNLLO by that member, the rules may effectively provide the member with a veto.

110. However, once dissatisfaction or distrust disrupts their relationship, members of the UNLLO may not find these default decision-making mechanisms to be adequate. Members may not have foreseen the possibility of such an intractable dispute and they may be unable to settle the dispute internally. As such, the UNLLO legislation should include a default rule for dealing with such disputes.

111. One approach could be to permit one or more dissatisfied members to compel the dissolution of the UNLLO and the liquidation of its assets. This approach, however, could create uncertainty and instability for the members and the UNLLO. Most importantly, perhaps, it would not permit the UNLLO to continue its existence and would thus result in a net loss in economic value.

112. A second approach to dealing with such intractable member disputes would be to facilitate the continued existence of the UNLLO, but permit members to withdraw or to be expelled from the UNLLO and to receive the fair value of their ownership interest. However, the disadvantage of permitting members to expel another member is that such an arrangement could be subject to abuse and result in minority oppression. In the scenario in which a conflict among members could result in a majority of members expelling a minority, the minority would be left to keep its ownership or to sell it back to the majority members for whatever price the majority was willing to offer.

113. Draft recommendation 24 suggests that the preferred approach in creating a default rule to resolve intractable disputes is to permit members to withdraw from the UNLLO and to be paid the fair value of their interest over a reasonable time. In this outcome, unless the members vote otherwise by qualified majority, the UNLLO continues to exist, thus preserving both economic stability and value. Moreover, permitting the payment of the fair value of the withdrawing member's ownership interest over time avoids a situation where the withdrawing member could hold the UNLLO and its remaining members to ransom by demanding immediate payment of the entire amount. Complying with an immediate demand of that sort might not be possible for the UNLLO or its remaining members, and could effectively force the dissolution of the UNLLO by rendering it insolvent.

114. The default rule suggested in draft recommendation 24 may still present challenges in terms of assessing the fair value of the withdrawing member's interest. The starting point for that valuation should be that the dissociating members would receive the same amount in a buyout as that member would receive if the UNLLO were dissolved. However, fair value dictates that the value of the UNLLO's goodwill should also be included in the calculation, and the buyout price for the member withdrawing should thus be the greater of 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.

115. It would also be prudent for members to decide in their members' agreement to use alternative dispute resolution (see draft rec. 27) for matters that cannot be resolved through the application of the members' agreement or the default rules. Agreement on the fair valuation of a withdrawing member's interest could be one of the issues that might be referred for alternative dispute resolution.¹⁶⁴

Recommendation 24: The law should provide that, unless otherwise agreed, members may withdraw from the UNLLO and be paid over a reasonable period of time the fair value of their interest in the UNLLO.¹⁶⁵

¹⁶⁴ See the section on "Conflict resolution", *infra*.

¹⁶⁵ The Working Group may wish to clarify that rec. 24 (rec. 25 in [A/CN.9/WG.I/WP.99/Add.1](#)) does not require an UNLLO to pay upon any request of a member to withdraw, but should require reasonable cause or an agreement among members. The Secretariat suggests modifying the recommendation to something along the lines of: "The law should provide that, upon agreement or reasonable cause, members may withdraw from the UNLLO and be paid over a reasonable period of time the fair value of their interest in the UNLLO."

K. Record-keeping, inspection and disclosure

116. 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 share equal ownership and management rights, 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.

117. Mandatory rules for the establishment of these principles are set out in draft recommendation 25, which requires the UNLLO to keep certain information, and draft recommendation 26, which ensures that each member has the right to inspect the information kept by the UNLLO, as well as the right to access any other reasonable information regarding the UNLLO, including information on its activities, operations and financial situation.¹⁶⁶ The importance of sharing and disseminating information on the UNLLO among its members is emphasized by establishing in draft recommendations 25 and 26 mandatory rules that members cannot contract out of. However, members can agree that the UNLLO should retain information in addition to that required in draft recommendation 25.

118. While the focus of the UNLLO is MSMEs and facilitation of their growth, disclosure and transparency of information are naturally important issues facing any business entity. While some States apply broad disclosure requirements to privately held entities (but allow exceptions to be made for MSMEs), others restrict mandatory disclosure to public business entities. Subject to the deliberations of the Working Group on which information in the formation document should be made public,¹⁶⁷ this legislative guide recommends that only the information required for formation of the UNLLO must be made public, and that the information that must be retained by the UNLLO further to draft recommendation 25 need not be publicly disclosed,¹⁶⁸ although it should be shared with all members and subject to their inspection.

119. The list of records that must be kept pursuant to draft recommendation 25 should not be particularly burdensome for UNLLOs, even when they are MSMEs, in that it consists of basic information necessary for entrepreneurs of all levels of sophistication to run their business. Moreover, the records that must be kept need only be “reasonable records”, i.e. recorded in a timely fashion and in a medium that could be expected of a similar business operating in a comparable context. The draft 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.

120. For example, many MSMEs use various mobile applications that are available on electronic devices to run their commercial enterprises, and are thus easily able to

¹⁶⁶ As agreed by the Working Group at its twenty-fifth session (para. 93(b), [A/CN.9/860](#)).

¹⁶⁷ The Secretariat has slightly modified this sentence, in keeping with the decision of the Working Group at its twenty-seventh session that it would postpone deliberations on which information on the formation and organization of the UNLLO should be made public (para. 52, [A/CN.9/895](#)). See also *supra*, footnote 101.

¹⁶⁸ While privately held businesses, like UNLLOs, are not required to provide the same flow and rate of information as publicly held firms generally, they may have strong incentives for doing so, particularly as they develop and progress. Indeed, businesses wishing to improve their access to credit or to attract investment may wish to signal their accountability by supplying information about: (1) the business’ objectives; (2) principal changes; (3) balance sheet and off-balance sheet items; (4) its financial position and capital needs; (5) the composition of any management board and its policy for appointments and remuneration; (6) forward-looking expectations; and (7) profits and dividends. Such considerations are not likely to trouble the smaller enterprises contemplated as the main users of the UNLLO, but could be important for those businesses as they grow. See, also, the agreement of the Working Group at its twenty-fifth session (para. 84(d), [A/CN.9/860](#)).

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 draft recommendations 25 and 26 by retaining and permitting access to the information electronically available via that mobile application.

Recommendation 25: The law should provide that the UNLLO must keep reasonable records in respect of:

- (a) Its formation document;
- (b) Any record of the members' agreement;
- (c) A current list of managers and members, as well as their contact details;
- (d) Financial statements (if any);
- (e) Tax returns or reports; and
- (f) The activities and operations of the UNLLO, as well as its financial information.

Recommendation 26: The law should provide that each member has the right to inspect and copy any of the records required to be kept by the UNLLO under recommendation 25, and to obtain from the UNLLO information concerning its activities, operations and financial information, as well as any other reasonable information in respect of the UNLLO.¹⁶⁹

L. Conflict resolution

121. Members can usually negotiate among themselves to arrive at an efficient members' agreement. As noted in paragraphs 110 and 115 above, however, members may not be able to settle a dispute once dissatisfaction or distrust disrupts their relationship. A resolution of the conflict may require the intervention of a court or an alternative dispute resolution ("ADR") mechanism, such as arbitration, mediation and other extrajudicial methods.

122. Further, paragraphs 74 to 79 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 this regard, ADR procedures can assist members of an UNLLO in reaching an outcome consistent with the recommendation in this legislative guide.

123. ADR mechanisms would also benefit the UNLLO in disputes with third parties, such as creditors or clients, where court processes would be too lengthy and expensive. UNLLOs involved in legal disputes with third parties would need to weigh the cost of court processes against the costs of unresolved disputes, which may include unpaid accounts. Members of the UNLLO may also face geographic, linguistic and cultural barriers within a court system.

124. While recourse to an alternative dispute settlement mechanism would provide a valuable tool for UNLLOs in legal disputes, there may be limitations within the State's domestic legal framework on the types of cases which may be brought before an ADR mechanism which may include criminal matters, labour and competition issues, or insolvency. Such matters would be beyond the scope of the draft legislative guide and are therefore excluded from the draft recommendation.

¹⁶⁹ As agreed by the Working Group at its twenty-fifth session in respect of its financial information (para. 93(b), A/CN.9/860).

Recommendation 27: The law should provide that any conflict that arises among members of the UNLLO or any third party may be submitted to any alternative dispute resolution mechanism, unless there are restrictions upon such actions within the State's domestic legal framework.¹⁷⁰

¹⁷⁰ At its twenty-eighth session, the Working Group agreed to include a new recommendation in the legislative guide encouraging the use of alternative dispute settlement in respect of the UNLLO (para. 149, [A/CN.9/900](#)). See also *supra* footnote 164 and para. 115.

Annex

Draft recommendations on an UNLLO

I. General provisions

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

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

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

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

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

II. Formation of the UNLLO

Recommendation 7: The law should provide that the UNLLO must have at least one member from the time of its formation until its dissolution, and that any legal or natural person may be a member of the UNLLO.

Recommendation 8: The law should specify when the UNLLO acquires its legal personality.

Recommendation 9: The law should provide that only the following information is required for the valid formation of the UNLLO:

- (a) The name of the UNLLO;
- (b) The business address or precise geographical location of the UNLLO;
- (c) A statement of whether the UNLLO is managed by its members (member-managed) or by a designated third-party manager (manager-managed); and
- (d) The name of each manager.

III. Organization of the UNLLO

Recommendation 10: The law should provide that the members of the UNLLO may adopt a members’ agreement in any form, including an agreement that is written, oral or implied by conduct. The members may agree in their members’ agreement on any matter relating to the UNLLO, except in respect of the mandatory rules set out in recommendations 1, 2, 3, 6, 7, 8, 9, 13(a), 14, 19, 20, 23(c), 25 and 26.

Recommendation 11: The law should provide that the UNLLO may be member-managed or manager-managed. A single member UNLLO will be member-managed unless otherwise agreed.

Recommendation 12: The law should provide that, unless otherwise agreed in the members' agreement:

(a) The members of the UNLLO have voting rights in proportion to their respective percentage of ownership of the UNLLO, as stated in the members' agreement. When the percentage of ownership of the UNLLO is not so stated, the members of the UNLLO have equal voting rights;

(b) Any difference arising between members as to matters in the ordinary course of business shall be decided by a majority; and

(c) Any difference arising between members as to matters outside of the ordinary course of business shall be decided by a qualified majority.

IV. Management by managers or members

Recommendation 13: The law should provide that:

(a) A manager of the UNLLO owes: (i) a duty of care; (ii) a duty of loyalty; (iii) a duty to disclose information to all members of the UNLLO; and (iv) a duty of good faith and fair dealing; and

(b) Unless otherwise stated in the member's agreement, fiduciary duties also apply to members of the UNLLO.

Recommendation 14: The law should provide that each manager individually has the authority to bind the UNLLO unless otherwise agreed. Restrictions upon this authority will not be effective against third parties dealing with the UNLLO in the ordinary course of business without proper notice.

Recommendation 15: The law should provide that, unless otherwise agreed by the members, a manager or managers may be elected and removed by a majority decision of the members.

V. Percentage of the ownership of the UNLLO and contribution by members

Recommendation 16: The law should provide that members of the UNLLO:

(a) Should state in the members' agreement their respective percentage of ownership of the UNLLO; and

(b) Share the ownership of the UNLLO equally when that percentage is not so stated.

Recommendation 17: The law should provide that, when deciding the members' respective percentage of ownership of the UNLLO, the members of the UNLLO are permitted to agree upon contributions, if any, made to the UNLLO, including the amount, type and value of such contributions. In the absence of such agreement, contributions that are made to the UNLLO should be equivalent for all members.

VI. Distributions

Recommendation 18: The law should provide that distributions be made to members in proportion to their respective percentage of ownership of the UNLLO as stated in the members' agreement. When the percentage of ownership of the UNLLO is not so stated, any distribution by the UNLLO shall be made equally among its members.

Recommendation 19: The law should prohibit distributions from being made to any member if upon giving effect to such distribution:

- (a) The UNLLO would not be able to pay its debts as they become due in the ordinary course of business; or
- (b) The UNLLO's total assets would be less than the sum of its total liabilities.

Recommendation 20: The law should provide that each member who received a distribution, or any portion of a distribution, is liable to reimburse the UNLLO for the entire amount of the distribution received if that distribution violates recommendation 19.

VII. Transfer of rights

Recommendation 21: The law should provide that members may transfer their financial rights in the UNLLO, but not their voting rights. Members of the UNLLO may vary this rule in the members' agreement.

VIII. Restructuring or conversion

Recommendation 22: The law should provide that the members of an UNLLO may agree to restructure it or convert it into another business form by qualified majority.

IX. Dissolution and winding-up

Recommendation 23: The law should provide that the UNLLO shall be dissolved and wound up in the following circumstances:

- (a) On the occurrence of any event that is specified in the members' agreement as causing the dissolution of the UNLLO;
- (b) On a vote by qualified majority of the members; or
- (c) Upon the rendering of a judicial or administrative decision that the UNLLO is dissolved.

X. Dissociation or withdrawal

Recommendation 24: The law should provide that, unless otherwise agreed, members may withdraw from the UNLLO and be paid over a reasonable period of time the fair value of their interest in the UNLLO.

XI. Record-keeping, inspection and disclosure

Recommendation 25: The law should provide that the UNLLO must keep reasonable records in respect of:

- (a) Its formation document;
- (b) Any record of the members' agreement;
- (c) A current list of managers and members, as well as their contact details;
- (d) Financial statements (if any);
- (e) Tax returns or reports; and

(f) The activities and operations of the UNLLO, as well as its financial information.

Recommendation 26: The law should provide that each member has the right to inspect and copy any of the records required to be kept by the UNLLO under recommendation 25, and to obtain from the UNLLO information concerning its activities, operations and financial information, as well as any other reasonable information in respect of the UNLLO.

XII. Conflict resolution

Recommendation 27: The law should provide that any conflict that arises among members of the UNLLO or any third party may be submitted to any alternative dispute resolution mechanism, unless there are restrictions upon such actions within the State's domestic legal framework.
