

## **Determining the legal nature of the limited liability company in Algerian legislation**

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### **Abstract:**

This study examines the legal nature of the limited liability company (SARL) in Algerian legislation, focusing on the characteristics derived from capital companies, such as the limited liability of the partner, and from partnership companies, such as the freedom to determine capital and the number of shareholders, which has evolved from 20 to 50 partners. This model makes it closer to partnership companies than to capital companies. However, legal scholars almost unanimously consider it to be one of the capital companies.

**Keywords:** Number of partners – capital – limited liability – medium-sized enterprises.

### **Introduction:**

Commercial companies are among the most important legal instruments for organising economic activity, as they enable the pooling of capital and its direction towards investment and production. Among these companies, the limited liability company (SARL) stands out as the most widespread form in Algerian legislation, due to the flexibility it offers compared to other companies.

The Algerian legislator has regulated this type of company within the provisions of the Commercial Code, drawing inspiration from the French model while introducing amendments suited to the national economic environment.

### **Importance of the subject:**

Studying the legal nature of the limited liability company in Algerian legislation is of great importance, as it is a distinctive legal form of commercial company. This study aims to shed light on a legal category of companies that has proven its effectiveness in giving new impetus to small and medium-sized enterprises in many countries around the world.

The importance of this study becomes particularly evident in the event of a legal dispute, where lawyers and judges play a crucial role in ensuring that cases are adjudicated properly and in accordance with the law. It should be noted that this type of company is almost exclusively reserved for small and medium-sized enterprises.

**Main research problem:**

Accordingly, we can pose the following problem: What is the legal nature of the limited liability company in Algerian legislation?

**Methodology used:**

To achieve the desired objective and resolve the aforementioned problem, we have employed the descriptive method, suitable for collecting information and definitions relevant to this study, and the analytical method, appropriate for analysing the distinctive characteristics of the limited liability company and deriving those features borrowed from partnership companies as well as those belonging to capital companies.

**General structure of the study:**

In an attempt to answer this problem, we will address this research paper in two sections. In the first section, we will discuss the legal construction of the limited liability company, and then highlight the determinants of this company in the second section.

**Section One: The legal construction of the limited liability company:**

This section addresses several important aspects. In the first subsection, we present the nature of the limited liability company. In the second subsection, we dedicate attention to the importance of the limited liability company. In the third subsection, we discuss the reasons that necessitate the limited liability company model in Algerian legislation.

**Subsection One: The concept of the limited liability company:**

This subsection aims to clarify the concept of the limited liability company and focus on its economic importance in practice.

**Branch One: Definition of the limited liability company:**

The limited liability company can be defined legally, as defined by the Algerian legislator in Article 564 of the Commercial Code<sup>1</sup>, which states: “The limited liability company is founded by one person or several persons who are only liable for losses up to the amount of their shares.” If the limited liability company founded in accordance with the preceding paragraph includes only one person as a sole partner, this company is called a “single-person limited liability company.” The sole partner exercises the powers vested in the general meeting of partners.

**Branch Two: Definition according to legal scholars:**

Professor Mohamed Sami Fawzi defined it as: a company composed of a number of partners, often fixed, who are subject to limited liability for the company’s debts and obligations up to the amount of their shares in its capital. They do not acquire the status of merchant. The company enjoys legal personality, its capital cannot be raised through a public subscription, and the transfer of partners’ shares is only permitted under the provisions of this law.<sup>2</sup>

Accordingly, the limited liability company can be defined as a commercial company consisting of two or more partners who are only liable for losses up to the amount of their contributions and who do not acquire the status of merchant.

**Subsection Two: The importance of the limited liability company:**

The limited liability company is the most common type in many countries, as it plays an important role in the economic and commercial field. This type of enterprise suits small and medium-sized entrepreneurs because the partner's liability is limited.

Given the great importance of this company, we have dedicated Branch One to its economic importance, and Branch Two to the reduction of fictitious companies.

**Branch One: The economic importance of the limited liability company:**

One of the economic advantages of the limited liability company is that it provides opportunities for partners without them acquiring the status of merchant. This status entails consequences, particularly regarding their liability for the company's obligations and their exposure to bankruptcy, as a partner is only held liable for the company's obligations to the extent of their shareholding.<sup>3</sup>

Economically, it is suitable for establishing small and medium-sized projects that meet the requirements of medium and small investors, and it spares the partner absolute liability for the company's debts; rather, the partner is only liable up to the amount of the shares they have contributed.

**Branch Two: Reduction of fictitious companies:**

The Algerian legislator's adoption of the single-person limited liability company has helped reduce recourse to fictitious companies. Reality shows that the multi-partner limited liability company has often been used as a means to create a fictitious company that in reality belongs to a single person who gathered the company's shares in their hands to benefit from limited liability. Thus, the legislator's adoption of the single-person limited liability company spares a natural or legal person wishing to establish a company from having to use borrowed persons, which has indeed reduced fictitious companies on the ground.<sup>4</sup>

**Section Two: Characteristics of the limited liability company:**

This section includes several points. In Subsection One, we clarify the personal characteristics of the limited liability company. In Subsection Two, we focus on the financial characteristics of the limited liability company.

**Subsection One: The personal nature of the limited liability company:**

In this subsection, we seek to examine the personal nature of the limited liability company and focus on its distinctive features that set it apart from traditional forms of commercial companies.

These features are mainly reflected in the number of partners and the freedom to determine capital, stemming from the personal element of the limited liability company. In Branch One, we address the determination of the number of partners; in Branch Two, the partners' freedom to determine the company's capital; and in Branch Three, the permissibility of making a contribution in the form of labour.

### **Branch One: Determination of the number of partners:**

In most legislations that have adopted its provisions, the limited liability company is composed of a small number of partners who know one another. These partners establish the company based on mutual trust between them, which gives it a personal character, even if this is somewhat weaker than in a general partnership.<sup>5</sup>

The Algerian legislator set the maximum number of partners under Article 590 of the Commercial Code before its amendment, which stated: “The number of partners in a limited liability company may not exceed twenty partners. If the company comes to include more than twenty partners, it must be converted into a joint stock company within one year; failing that, the company shall be dissolved unless the number of partners becomes equal to twenty or fewer within that period.” Article 590 of the Commercial Code was amended by Order 15-20 amending and supplementing the Commercial Code.<sup>6</sup>

After the amendment, the number of partners became fifty, i.e. an addition of thirty partners. Accordingly, the amended Article 590 of the Commercial Code states: “The number of partners in a limited liability company may not exceed fifty (50) partners.” This company is unique in having a maximum number of partners, for fear of losing the personal element, and in pursuit of the legislator’s aim to preserve the family character of this company as the ideal model for small and medium-sized enterprises.<sup>7</sup>

Based on the foregoing, we conclude that the limited liability company resembles partnership companies in that the number of partners is large, fixed by the legislator at fifty partners after it had been twenty before the amendment of the Algerian Commercial Code. Accordingly, this increase in the number of partners strengthens the personal aspect of the limited liability company.

### **Branch Two: The partners’ freedom to determine the company’s capital:**

By virtue of the amendment under Law No. 15-20 amending and supplementing the Commercial Code, the Algerian legislator amended the provisions of Article 566 of the Commercial Code, which after amendment reads: “The capital of the limited liability company is freely determined by the partners in the company’s articles of association and is divided into shares of equal nominal value. The capital must be mentioned in all company documents.”<sup>8</sup>

The legislator required that the capital of the limited liability company be divided into nominal shares of equal value, just like partnership companies, whose capital is divided into shares (parts) rather than stocks. It should be noted that the shares in the capital of a limited liability company are not negotiable by commercial methods, and they may not be transferred to third parties except under restrictions and specific conditions.<sup>9</sup> The absence of a minimum capital requirement, together with the possibility of making a contribution in the form of labour, makes the limited liability company lean more towards partnership companies than towards capital companies.<sup>10</sup>

### **Branch Three: Permissibility of making a contribution in the form of labour:**

By virtue of the amendment to the Algerian Commercial Code under Law No. 15-20 amending and supplementing it, the Algerian legislator allowed a partner to contribute a labour share, in addition to cash and in-kind contributions. Article 567 bis, introduced by the aforementioned

Law No. 15-20, states: “A contribution of labour may be made to a limited liability company.”<sup>11</sup> From the text of the aforementioned article, it is clear that the legislator moved from a complete prohibition of labour contributions to permitting them in limited liability companies. In this respect, he follows the example of the French legislator, influenced by him in adopting the possibility of labour contributions pursuant to Article 223-7 of the French Commercial Code.<sup>12</sup> All of this has been considered by legal scholars as justification for saying that the limited liability company has abandoned the financial element and retained only the personal element after the amendment of the provisions governing it.<sup>13</sup>

The main objective of allowing labour contributions in a limited liability company is to keep pace with global developments in the scientific and technological field and their positive effects on intellectual creativity and mental innovation, which cannot be dispensed with in the field of companies to develop their service activities, and to contribute technical knowledge, skills and expertise.<sup>14</sup>

From our evaluation of the element of the possibility of participating with a labour share in a limited liability company, it may be that the removal of this prohibition is intended to encourage investors to establish such companies because they suit small and medium-sized enterprises. Accordingly, this feature brings limited liability companies closer to partnership companies.

#### **Subsection Two: The financial nature of the limited liability company:**

We discuss the financial nature of the limited liability company, which distinguishes it from other legal forms of companies.

This company is considered one of the capital companies, as it relies on dividing capital into non-negotiable shares without imposing a minimum capital requirement. It is also distinguished by the limited liability of partners, without requiring them to hold the status of merchant, which opens the field for many individuals to participate in it.

#### **Branch One: It is considered one of the capital companies:**

The limited liability company is classified as a capital company. Commercial companies are divided into three categories: capital companies, such as joint stock companies; partnership companies, such as general partnerships; and mixed companies, which combine some features of capital companies and partnership companies, such as partnership limited by shares.

#### **Branch Two: Limited liability of partners:**

Referring to the text of Article 564 of the Algerian Commercial Code, which states: “The limited liability company is founded ... [partners] are only liable for losses up to the amount of their shares ...”<sup>15</sup> The limitation of partners’ liability means that they bear the company’s obligations only to the extent of their shares in it, not with their personal assets, and without joint liability among themselves.<sup>16</sup> This feature makes the position of a partner in a limited liability company similar to that of a partner in a joint stock company.<sup>17</sup> The most important characteristic of this type of company is the limited liability of the partner, who is liable only up to the amount of their contribution to the company’s capital. This brings it close to joint stock companies, where a partner is only liable for the value of the shares they subscribed to, unlike the case of a partner in a general partnership, who bears personal and joint liability.<sup>18</sup>

The consequence of the partner's limited liability is that the company's creditors have recourse only to the general security of the company's assets as a legal entity, without extending to the partner's personal assets.<sup>19</sup>

Thus, limited liability in companies means that a partner's liability for the company's debts is confined to their share in its capital, and the partner does not bear with their personal assets any excess of the company's debts over its assets. Consequently, the company's creditors have no right to recourse against the partner's personal assets when the legal entity's assets are insufficient. Furthermore, the bankruptcy of the company does not entail the partner's bankruptcy.<sup>20</sup> However, a partner only benefits from the limitation of liability in the aforementioned manner if their conduct in the company is proper and in accordance with the law. If their conduct involves a violation of the law or fraud against third parties, the partner becomes personally liable for the consequences of their actions, with all their assets, jointly and severally with other partners or managers who committed the errors.<sup>21</sup>

### **Branch Three: Transferability of shares:**

The transfer of shares means any legal act, whether for consideration or by gift, by which a partner transfers ownership of their stake in the company to another person. The foremost of these acts are the sale and exchange of stakes, and all transactions for consideration, whether they involve the full transfer of ownership of the share or part of it, such as bare ownership.<sup>22</sup>

The company is not affected by a change in the legal status of a partner with respect to the company; it continues after the death of a partner, their declaration of bankruptcy, or loss of legal capacity. This feature is derived from capital companies.<sup>23</sup>

Accordingly, a partner in a limited liability company may transfer their share to an outsider outside the company by following the procedures set out in Article 571 of the Algerian Commercial Code.<sup>24</sup> The Algerian legislator also required that the transfer be made in an official document.

Moreover, this company does not dissolve upon the death of a partner, as shares may be transferred by inheritance, and may be assigned freely between spouses, ascendants and descendants. This is provided for in Article 570 of the Algerian Commercial Code, which states: "Shares are transferable by inheritance and may also be assigned freely between spouses, ascendants and descendants."<sup>25</sup>

These procedures differ from those of general partnerships or simple limited partnerships, where a general partner may not transfer their share except with prior agreement or the consent of the remaining partners.

### **Branch Four: The partner does not acquire the status of merchant:**

The law does not impose that a person who becomes a partner in a limited liability company acquires the status of merchant, unlike a shareholder in a joint stock company or a limited partner in a limited partnership. Consequently, the legislator also does not impose the legal obligations arising from acquiring the status of merchant, such as keeping commercial books and registering in the commercial register.<sup>26</sup> This is contrary to a partner in a general partnership, who, because of their full personal and joint liability, acquires commercial status simply by joining the company. If they did not enjoy this status before joining, they acquire it

upon signing the company's articles of association. Therefore, transactions carried out by the company as a legal entity are considered as if they were conducted on behalf of each partner individually, which places the partner in a general partnership in a position no different from that of a person conducting such activities in their own name, thus requiring commercial capacity.<sup>27</sup>

In contrast, a partner in a limited liability company is not required to have commercial capacity because they do not acquire the status of merchant. Since the partner's liability is limited, they do not acquire the status of merchant upon entering the company unless they already enjoyed that status beforehand. In the event of the company's bankruptcy, this does not lead to their own bankruptcy. Moreover, they are not required to have full legal capacity; therefore, a person with limited capacity may be a partner in a limited liability company.<sup>28</sup>

It should also be noted that a partner's failure to acquire the status of merchant simply by joining a limited liability company does not mean that merchants are prohibited from becoming partners in it. Rather, the above means that merely becoming a partner in the company does not confer merchant status unless it had already been established for them beforehand.<sup>29</sup>

### **Conclusion:**

At the conclusion of the study on the legal nature of the limited liability company in Algerian legislation, the limited liability company is a commercial company consisting of two or more partners. This company is the most widespread in many countries because it suits small and medium-sized enterprise owners, due to its economic and commercial importance.

The limited liability company derives a set of features from partnership companies, such as the number of partners, freedom to determine capital, and the labour contribution, while at the same time deriving some elements from capital companies, namely the limited liability of the partner and the partner not acquiring the status of merchant.

Accordingly, we can say that this company reflects a manifestation of harmony between the personal and the financial elements, which affects its legal nature, as it approaches partnership companies in some aspects and capital companies in others. The limited liability company combines the characteristics of partnership companies and the elements of capital companies at the same time.

It also appears to us from the Algerian legislator's amendment of the Commercial Code in 2015 under Law No. 15-20 that one of the manifestations of the personal element in this company is the fixed number of partners (50 partners), as well as the legislator's recognition of the permissibility of making a labour contribution under the same amending and supplementing law.

Finally, the study reached a number of results, as follows:

1. The limited liability company occupies an intermediate position between partnership companies and capital companies.
2. The limited liability company has contributed to the creation of small and medium-sized enterprises due to its economic and commercial importance, which has made it the most popular company in many countries.

3. The limited liability company has led to a reduction in the emergence of fictitious companies.
4. The legislator's increase of the number of partners from twenty to fifty enhances the personal character of the limited liability company.
5. Recognition of the labour contribution brings the limited liability company closer to partnership companies.
6. The removal of the minimum capital requirement and leaving the partners free to determine it is a manifestation of the personal element in the limited liability company.
7. The feature of limited liability of the partner is one of the most important characteristics that the limited liability company borrows from capital companies.
8. A partner's entry into a limited liability company does not confer merchant status, which brings this company closer to capital companies.
9. A partner in a limited liability company is not required to have commercial capacity, which also brings this company closer to capital companies.

Finally, we propose some recommendations that we consider important:

- The legislator should preserve the minimum capital requirement for the company, as it represents the sole guarantee for the company's creditors.
- Work should be done to encourage the establishment of this type of company and facilitate its formation, as it is the ideal model for owners of small and medium-sized enterprises and plays a role in the development of the national economy.
- The legislator should intervene to clarify the legal nature explicitly.
- Procedures for transferring shares should be simplified to enhance investment.

#### **Referencing numbers:**

- <sup>1</sup> Article 564 of the Commercial Code.
- <sup>2</sup> Professor Mohamed Sami Fawzi, op. cit.
- <sup>3</sup> Within the limit of their shareholding.
- <sup>4</sup> Reference to reduction of fictitious companies.
- <sup>5</sup> Compared to a general partnership.
- <sup>6</sup> Order 15-20 amending and supplementing the Commercial Code.
- <sup>7</sup> Reference to small and medium-sized enterprises.
- <sup>8</sup> Article 566 of the Commercial Code (amended).
- <sup>9</sup> Transfer restrictions and conditions.
- <sup>10</sup> Absence of minimum capital and labour contribution.
- <sup>11</sup> Article 567 bis of the Commercial Code (as amended by Law No. 15-20).
- <sup>12</sup> Article 223-7 of the French Commercial Code.
- <sup>13</sup> Post-amendment justifications.
- <sup>14</sup> Technical knowledge, skills and expertise.
- <sup>15</sup> Article 564 of the Commercial Code.
- <sup>16</sup> No joint liability among partners.
- <sup>17</sup> Similar to joint stock company partner.

- 18 Personal and joint liability.
- 19 Does not extend to partner's personal assets.
- 20 Bankruptcy of company does not entail partner's bankruptcy.
- 21 Partners or managers who committed errors.
- 22 Transfer of ownership of share.
- 23 Derived from capital companies.
- 24 Article 571 of the Commercial Code.
- 25 Article 570 of the Commercial Code.
- 26 Keeping commercial books and registering in commercial register.
- 27 Requirement of commercial capacity.
- 28 Person with limited capacity as partner.
- 29 Merchant status not acquired unless previously established.

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