

UNIFORM PARTNERSHIP ACT (1997)
(Last Amended 2013)

Drafted by the

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS

and by it

APPROVED AND RECOMMENDED FOR ENACTMENT
IN ALL THE STATES

at its

ANNUAL CONFERENCE
MEETING IN ITS ONE-HUNDRED-AND-TWENTY-SECOND YEAR
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NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS

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UNIFORM PARTNERSHIP ACT—QUICK CHRONOLOGY

1914—Original Uniform Partnership Act.

1992—Promulgation of Uniform Partnership Act (1992) by Uniform Law Commissioners.

1993—Amendments to Uniform Partnership Act (1992). Becomes Uniform Partnership Act (1993).

1994—Amendments to Uniform Partnership Act (1993). Becomes Uniform Partnership Act (1994).

1996—Amendments to Uniform Partnership Act (1994). Adds Limited Liability Partnership. Becomes Uniform Partnership Act (1996).

1997—Amendment to Uniform Partnership Act (1996), Section 801. Becomes Uniform Partnership Act (1997)

2011—Amendments adopted as part of the Harmonization Project. Becomes Uniform Partnership Act (1997) (Last Amended 2013).

PREFATORY NOTE TO UNIFORM PARTNERSHIP ACT (1997)

The National Conference of Commissioners on Uniform State Laws first considered a uniform law of partnership in 1902. Although early drafts had proceeded along the mercantile or "entity" theory of partnerships, later drafts were based on the common-law "aggregate" theory. The resulting Uniform Partnership Act ("UPA"), which embodied certain aspects of each theory, was finally approved by the Conference in 1914. The UPA governs general partnerships, and also governs limited partnerships except where the limited partnership statute is inconsistent. The UPA has been adopted in every State other than Louisiana and has been the subject of remarkably few amendments in those States over the past 80 years.

In January of 1986, an American Bar Association subcommittee issued a detailed report that recommended extensive revisions to the UPA. See UPA Revision Subcommittee of the Committee on Partnerships and Unincorporated Business Organizations, Section of Business Law, American Bar Association, *Should the Uniform Partnership Act be Revised?*, 43 Bus. Law. 121 (1987) ("ABA Report"). The ABA Report recommended that the entity theory "should be incorporated into any revision of the UPA whenever possible." *Id.* at 124.

In 1987, the Conference appointed a Drafting Committee to Revise the Uniform Partnership Act and named a Reporter. The Committee held its initial meeting in January of 1988 and a first reading of the Committee's draft was begun at the Conference's 1989 Annual Meeting in Kauai, Hawaii. The first reading was completed at the 1990 Annual Meeting in Milwaukee. The second reading was begun at Naples, Florida, in 1991 and completed at San Francisco in 1992. The Revised Uniform Partnership Act (1992) was adopted unanimously by a vote of the States on August 6, 1992. The following year, in response to suggestions from various groups, including an American Bar Association subcommittee and several state bar associations, the Drafting Committee recommended numerous revisions to the Act. Those were adopted at the Charleston, South Carolina, Annual Meeting in 1993, and the Act was restyled as the Uniform Partnership Act (1993). Subsequently, a final round of changes was incorporated, and the Conference unanimously adopted the Uniform Partnership Act (1994) at its 1994 Annual Meeting in Chicago. The Revised Act was approved by the American Bar Association House of Delegates in August, 1994.

The Uniform Partnership Act (1994) ("Revised Act" or "RUPA") gives supremacy to the partnership agreement in almost all situations. The Revised Act is, therefore, largely a series of "default rules" that govern the relations among partners in situations they have not addressed in a partnership agreement. The primary focus of RUPA is the small, often informal, partnership. Larger partnerships generally have a partnership agreement addressing, and often modifying, many of the provisions of the partnership act.

The Revised Act enhances the entity treatment of partnerships to achieve simplicity for state law purposes, particularly in matters concerning title to partnership property. RUPA does not, however, relentlessly apply the entity approach. The aggregate approach is retained for some purposes, such as partners' joint and several liability.

The Drafting Committee spent significant effort on the rules governing partnership

breakups. RUPA's basic thrust is to provide stability for partnerships that have continuation agreements. Under the UPA, a partnership is dissolved every time a partner leaves. The Revised Act provides that there are many departures or "dissociations" that do not result in a dissolution.

Under the Revised Act, the withdrawal of a partner is a "dissociation" that results in a dissolution of the partnership only in certain limited circumstances. Many dissociations result merely in a buyout of the withdrawing partner's interest rather than a winding up of the partnership's business. RUPA defines both the substance and procedure of the buyout right.

Article 6 of the Revised Act covers partner dissociations; Article 7 covers buyouts; and Article 8 covers dissolution and the winding up of the partnership business. See generally Donald J. Weidner & John W. Larson, *The Revised Uniform Partnership Act: The Reporters' Overview*, 49 Bus. Law. 1 (1993).

The Revised Act also includes a more extensive treatment of the fiduciary duties of partners. Although RUPA continues the traditional rule that a partner is a fiduciary, it also makes clear that a partner is not required to be a disinterested trustee. Provision is made for the legitimate pursuit of self-interest, with a counterbalancing irreducible core of fiduciary duties.

Another significant change introduced by RUPA is provision for the public filing of statements containing basic information about a partnership, such as the agency authority of its partners. Because of the informality of many partnerships, and the inadvertence of some, mandatory filings were eschewed in favor of a voluntary regime. It was the Drafting Committee's belief, however, that filings would become routine for sophisticated partnerships and would be required by lenders and others for major transactions.

Another innovation is found in Article 9. For the first time, the merger of two or more partnerships and the conversion of partnerships to limited partnerships (and the reverse) is expressly authorized, and a "safe harbor" procedure for effecting such transactions is provided.

One final change deserves mention. Partnership law no longer governs limited partnerships pursuant to the provisions of RUPA itself. First, limited partnerships are not "partnerships" within the RUPA definition. Second, UPA Section 6(2), which provides that the UPA governs limited partnerships in cases not provided for in the Uniform Limited Partnership Act (1976) (1985) ("RULPA") has been deleted. No substantive change in result is intended, however. Section 1105 of RULPA already provides that the UPA governs in any case not provided for in RULPA, and thus the express linkage in RUPA is unnecessary. Structurally, it is more appropriately left to RULPA to determine the applicability of RUPA to limited partnerships. It is contemplated that the Conference will review the linkage question carefully, although no changes in RULPA may be necessary despite the many changes in RUPA.

Finally, the Drafting Committee wishes to express its deep appreciation for the extraordinary time and effort that has been devoted to this project by its Reporter, Donald J. Weidner, Dean of the Florida State University College of Law; by its Assistant Reporter, Professor John W. Larson of the Florida State University College of Law; by its American Bar Association Advisors Allan G. Donn, of Norfolk, Virginia (ABA Section of Taxation and later the

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The Drafting Committee also would like to express its appreciation to the members of the ABA Committee on Partnerships and Unincorporated Business Organizations, and its chairs, Thurston R. Moore of Richmond, Virginia, and John H. Small of Wilmington, Delaware, for all the time and effort they devoted to this project, and to that Committee's special Subcommittee on the Revised Uniform Partnership Act, the chairs of that subcommittee, Lauris G.L. Rall of New York, New York, and Gerald V. Niesar of San Francisco, California, and its members, in particular, Robert R. Keatinge of Denver, Colorado, Professor Larry E. Ribstein of the George Mason University School of Law, and Anthony van Westrum of Denver, Colorado. Each of these individuals added immeasurably to the Drafting Committee's discussion and consideration of both the major policy issues and the technical drafting issues raised by the Act.

Addendum Pertaining to 1997 Amendments

In 1995, the Conference appointed a Drafting Committee to add provisions to RUPA authorizing the creation of a new form of general partnership called a limited liability partnership (LLP). At the time RUPA was first approved in 1992, only two states had adopted limited liability partnership legislation. By the time the LLP amendments to RUPA were approved by the Conference at the 1996 Annual Meeting, over forty states had adopted limited liability partnership provisions to their general partnership statutes.

The LLP amendments to RUPA deal with four major issues: (1) scope of a partner's liability shield; (2) the voting requirement to become an LLP; (3) the effect of becoming an LLP on the partnership agreement; and (4) the annual filing requirement.

1. Scope of a Partner's Liability Shield

The amendments to add LLP provisions to RUPA include a new Section 306(c) providing for a corporate-styled liability shield which protects partners from vicarious personal liability for all partnership obligations incurred while a partnership is a limited liability partnership. The complete liability shield comports with the modern trend among the states. Most states, however, have adopted a partial liability shield protecting the partners only from vicarious

personal liability for all partnership obligations arising from negligence, wrongful acts or misconduct, whether characterized as tort, contract or otherwise, committed while the partnership is an LLP. The Act does not alter a partner's liability for personal misconduct and does not alter the normal partnership rules regarding a partner's right to indemnification from the partnership (Section 401(c)). Therefore, the primary effect of the new liability shield is to sever a partner's personal liability to make contributions to the partnership when partnership assets are insufficient to cover its indemnification obligation to a partner who incurs a partnership obligation in the ordinary course of the partnership's business.

2. Voting Requirement to Become an LLP

The Act includes a new Section 1001(b) which provides that the decision to become an LLP is a major partnership event equivalent to an amendment of the partnership agreement. Therefore, the required vote equals the vote required to amend the partnership agreement. When the agreement is silent on these matters, the required vote would be unanimous. Where the agreement includes several amendment votes depending on the nature of the amendment, the required vote is that which considers contribution obligations since those obligations are the most affected by the amendments. Most states currently consider the required vote to become a limited liability partnership to be an ordinary partnership decision requiring only a majority consent.

In becoming an LLP, each partner should consider a personal liability calculus. Where partnership assets are insufficient to indemnify a partner for an LLP obligation, each partner forfeits a right to receive contributions from other partners in exchange for being relieved of the obligation to contribute to the personal liability of other partners. This calculus will be different for each partner and will vary, for example, depending on the size and business of the partnership, the number of partners, the amount of insurance, and the relative risk of each partner's business practice compared to fellow partners. To adequately consider these varying interests, the Act adopts the vote required to amend the partnership agreement in special and general cases.

3. Effect of Becoming an LLP on the Partnership Agreement

The last sentence in new Section 306(c) provides that when a partnership becomes an LLP, the resulting liability shield applies notwithstanding inconsistent provisions of the partnership agreement existing immediately before the vote to become an LLP was taken. When the partners vote to become an LLP, they obviously intend to sever their personal responsibility to make contributions to the partnership when partnership assets are insufficient to cover partnership indemnification obligations to a partner. A partner's contribution obligation may be enforced not only by a partner (Sections 401 and 405) but also by a partner's creditors (Section 807(f)). In essence, the new Section 306(c) automatically "amends" the partnership agreement to remove personal liability for contribution obligations that may exist under the terms of the partnership agreement as it exists immediately before the vote. However, the partners are not prohibited from thereafter amending the partnership agreement again to reestablish contribution obligations (see Section 103(b)).

4. Annual Filing Requirement

The Act includes new Section 1001(d) which provides that a partnership's status as an LLP remains effective until it is revoked by a vote of the partners or is canceled by the Secretary of State under new Section 1003(c) for the failure to file an annual report or pay the required annual fees. Most states provide that unless an LLP timely files an annual registration statement, its LLP status is "automatically" terminated but may be resurrected prospectively only with a subsequent corrective filing. Under this view, an operating partnership may have significant "gaps" in its shield which is further complicated by sourcing rules necessary to determine when a partnership obligation belongs to the shielded LLP or the unshielded partnership. As with corporations and limited liability companies, the Act preserves the LLP status and the partners' liability shield unless the LLP status is revoked by the partners or canceled by the Secretary of State. In the latter case, potential gaps in the liability shield are cured with a retroactive resurrection of the LLP status if a corrective filing is made within two years (Section 1003(e)).

The LLP Drafting Committee wishes to express its gratitude to the Reporter for this project, Professor Carter G. Bishop of Suffolk University Law School. Professor Bishop's comprehensive knowledge of partnership law and tax and his drafting expertise were instrumental in enabling the Drafting Committee to complete this project in one year. The Drafting Committee also wishes to thank the following advisors and observers, whose expertise and advice were very important to the success of this project: Elizabeth G. Hester of Richmond, Virginia (ABA Advisor); Lou Conti of Orlando, Florida (ABA Section of Business Law Advisor); Steven G. Frost of Chicago, Illinois (ABA Section of Taxation Advisor); Professor Thomas E. Geu of the University of South Dakota School of Law (ABA Section of Real Property, Probate and Trust Advisor); Sanford J. Liebschutz of Rochester, New York (ABA Section of Real Property, Probate and Trust Advisor and American College of Real Estate Lawyers Advisor); Robert A. Creamer of Chicago, Illinois (Attorneys' Liability Assurance Society, Inc.); R. Michael Duffy of Washington, D.C. (The Accountant's Coalition); Professor Philip Hablutzel of Chicago, Illinois (Illinois Secretary of State's Corporation Law Advisory Committee); Robert R. Keatinge of Denver, Colorado (ABA Business Law Section); Mark Lubin of San Francisco, California (California Bar Association); Professor Sandra Miller of Chester, Pennsylvania; and William R. Stein of Washington, D.C. (The Accountant's Coalition); and Ronald H. Wilcomes of Paramus, New Jersey (American College of Real Estate Lawyers).

PREFATORY NOTE TO 2011 AND 2013 HARMONIZATION AMENDMENTS

From 2009 to 2013, the Uniform Law Conference undertook an intensive effort to harmonize, to the extent possible, all uniform acts pertaining to unincorporated organizations. As part of that effort, the Uniform Partnership Act (1997) underwent four types of changes: substantive; major improvements in language; minor revisions in language for the sake of harmonization; and relocation within this particular "spoke" of provisions that are part of the "HUB" in the new Uniform Business Organizations Code ("UBOC").

Substantive Changes

The most significant substantive changes are:

- simplifying the section on “knowledge” and “notice,” Section 103;
- centralizing constructive notice provisions, Section 103(d);
- revising and expanding provisions pertaining to the partnership agreement, Sections 105–107;
- updating various filing provisions pertaining to limited liability partnerships, Sections 108–118;
- providing that, in the context of a claim to “pierce the veil” of a limited liability partnership, “[t]he failure of [the] limited liability partnership to observe formalities relating to the exercise of its powers or management of its business is not a ground for imposing liability on a partner for a debt, obligation, or other liability of the partnership,” Section 306(d);
- providing rules on unlawful distributions, Sections 406–407;
- “uncabining” (*i.e.*, making non-exhaustive) the codification of fiduciary duties, Section 409 (a)–(b);
- making clear that the act’s obligation of good faith and fair dealing is the common law obligation of contract law, Section 409(d);
- adding as an event causing dissolution “the passage of 90 consecutive days during which the partnership does not have at least two partners,” Section 801(6); and
- adding the comprehensive provisions of the Model Entity Transactions Act, Article 11.

Substantial Improvements to Language

The most significant improvements in language appear in Section 105 (formerly Section 103), the first of three sections addressing the partnership agreement. The structure of Section 105 is far less complicated than the structure of former Section 103.

Harmonization-Based Language Changes

Minor changes in language for the sake of harmonization appear throughout the act.

Relocation and Renumbering of HUB-Based Provisions

The Harmonization Project included both the harmonization of various stand-alone acts and the compilation of UBOC, which comprises a “HUB” (somewhat analogous to Article 1 of the Uniform Commercial Code) and various spokes. Each spoke pertains to a different type of organization (*e.g.*, general partnership, limited partnership, limited liability company, statutory trust entity). Naturally, spokes in the Code do not repeat the provisions from the HUB. In

contrast, each stand-alone act includes provisions that appear in the HUB in the Code.

So that the section numbers of this “spoke” correspond with the spoke provisions in the Code, HUB-based provisions of this Act have been renumbered to appear at the end of articles. *See, e.g.*, Sections 112–121.

The Drafting Committee on Harmonization of Business Entity Acts was greatly assisted in its work by the very substantial and knowledgeable contributions of the following Observers, who diligently attended and actively participated in its meetings:

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EXPLANATORY NOTE ON THE REVISED COMMENTS

As part of the Harmonization Project, the Conference substantially revised the comments to the Uniform Partnership Act. Professor Daniel S. Kleinberger was the principal drafter of the revised comments.

To distinguish among the current and prior versions of uniform business organization acts, the Harmonization Comments use the following references.

The phrase “this act” refers to the Harmonized act (*i.e.*, the Uniform Partnership Act (1997) (Last Amended 2013)).

“UPA (1997)” refers to the version of the Uniform Partnership Act originally promulgated in 1994, with all amendments through 1997.

“UPA (1914)” refers to the original Uniform Partnership Act as promulgated in 1914.

“ULLCA (2006) (Last Amended 2013)” refers to the Revised Uniform Limited Liability Company Act as harmonized.

“ULLCA (2006)” refers to the Revised Uniform Limited Liability Act as promulgated in 2006.

“ULLCA (1996)” refers to the original Uniform Limited Liability Company Act as

promulgated in 1996.

“ULPA (2001) (Last Amended 2013)” refers to the Uniform Limited Partnership Act (2001) as harmonized.

“ULPA (2001)” refers to the Uniform Limited Partnership Act as promulgated in 2001.

“ULPA (1976/1985)” refers to the Revised Uniform Limited Partnership Act as promulgated in 1976 and substantially revised in 1985.

“ULPA (1976)” refers to the Revised Uniform Limited Partnership Act, as promulgated in 1976.

“ULPA (1916)” refers to the Uniform Limited Partnership Act as promulgated in 1916.

“MBCA” refers to the Model Business Corporation Act.

UNIFORM PARTNERSHIP ACT (1997)
(Last Amended 2013)

[ARTICLE] 1

GENERAL PROVISIONS

SECTION 101. SHORT TITLE. This [act] may be cited as the Uniform Partnership Act.

Comment

This act is drafted to replace a state's current general partnership statute, whether or not that statute is based on UPA (1914) or UPA (1997). Section 110 contains transition provisions.

SECTION 102. DEFINITIONS. In this [act]:

(1) "Business" includes every trade, occupation, and profession.

(2) "Contribution", except in the phrase "right of contribution", means property or a benefit described in Section 403 which is provided by a person to a partnership to become a partner or in the person's capacity as a partner.

(3) "Debtor in bankruptcy" means a person that is the subject of:

(A) an order for relief under Title 11 of the United States Code or a comparable order under a successor statute of general application; or

(B) a comparable order under federal, state, or foreign law governing insolvency.

(4) "Distribution" means a transfer of money or other property from a partnership to a person on account of a transferable interest or in a person's capacity as a partner. The term:

(A) includes:

(i) a redemption or other purchase by a partnership of a transferable interest; and

(ii) a transfer to a partner in return for the partner's relinquishment of any right to participate as a partner in the management or conduct of the partnership's business or

have access to records or other information concerning the partnership's business; and

(B) does not include amounts constituting reasonable compensation for present or past service or payments made in the ordinary course of business under a bona fide retirement plan or other bona fide benefits program.

(5) "Foreign limited liability partnership" means a foreign partnership whose partners have limited liability for the debts, obligations, or other liabilities of the foreign partnership under a provision similar to Section 306(c).

(6) "Foreign partnership" means an unincorporated entity formed under the law of a jurisdiction other than this state which would be a partnership if formed under the law of this state. The term includes a foreign limited liability partnership.

(7) "Jurisdiction", used to refer to a political entity, means the United States, a state, a foreign country, or a political subdivision of a foreign country.

(8) "Jurisdiction of formation" means the jurisdiction whose law governs the internal affairs of an entity.

(9) "Limited liability partnership", except in the phrase "foreign limited liability partnership" and in [Article] 11, means a partnership that has filed a statement of qualification under Section 901 and does not have a similar statement in effect in any other jurisdiction.

(10) "Partner" means a person that:

(A) has become a partner in a partnership under Section 402 or was a partner in a partnership when the partnership became subject to this [act] under Section 110; and

(B) has not dissociated as a partner under Section 601.

(11) "Partnership", except in [Article] 11, means an association of two or more persons to carry on as co-owners a business for profit formed under this [act] or that becomes subject to this

[act] under [Article] 11 or Section 110. The term includes a limited liability partnership.

(12) “Partnership agreement” means the agreement, whether or not referred to as a partnership agreement and whether oral, implied, in a record, or in any combination thereof, of all the partners of a partnership concerning the matters described in Section 105(a). The term includes the agreement as amended or restated.

(13) “Partnership at will” means a partnership in which the partners have not agreed to remain partners until the expiration of a definite term or the completion of a particular undertaking.

(14) “Person” means an individual, business corporation, nonprofit corporation, partnership, limited partnership, limited liability company, [general cooperative association,] limited cooperative association, unincorporated nonprofit association, statutory trust, business trust, common-law business trust, estate, trust, association, joint venture, public corporation, government or governmental subdivision, agency, or instrumentality, or any other legal or commercial entity.

(15) “Principal office” means the principal executive office of a partnership or a foreign limited liability partnership, whether or not the office is located in this state.

(16) “Property” means all property, whether real, personal, or mixed or tangible or intangible, or any right or interest therein.

(17) “Record”, used as a noun, means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.

(18) “Registered agent” means an agent of a limited liability partnership or foreign limited liability partnership which is authorized to receive service of any process, notice, or demand required or permitted by law to be served on the partnership.

(19) “Registered foreign limited liability partnership” means a foreign limited liability partnership that is registered to do business in this state pursuant to a statement of registration filed by the [Secretary of State].

(20) “Sign” means, with present intent to authenticate or adopt a record:

(A) to execute or adopt a tangible symbol; or

(B) to attach to or logically associate with the record an electronic symbol, sound, or process.

(21) “State” means a state of the United States, the District of Columbia, Puerto Rico, the United States Virgin Islands, or any territory or insular possession subject to the jurisdiction of the United States.

(22) “Transfer” includes:

(A) an assignment;

(B) a conveyance;

(C) a sale;

(D) a lease;

(E) an encumbrance, including a mortgage or security interest;

(F) a gift; and

(G) a transfer by operation of law.

(23) “Transferable interest” means the right, as initially owned by a person in the person’s capacity as a partner, to receive distributions from a partnership, whether or not the person remains a partner or continues to own any part of the right. The term applies to any fraction of the interest, by whomever owned.

(24) “Transferee” means a person to which all or part of a transferable interest has been

transferred, whether or not the transferor is a partner.

Comment

UPA (1997) section 101 defined fourteen terms. This section defines twenty-four terms. The increase is generally due to harmonization and more particularly to changes made to bring the LLP provisions pertaining to limited liability and filings into line with the corresponding provisions of ULPA (2001) (Last Amended 2013) and ULLCA (2006) (Last Amended 2013). *See, e.g.*, Sections 111–117 (provisions pertaining to filings), 407 (liability for improper distributions).

This section contains definitions for terms used throughout the act; it is important to remember that “partnership” means solely a domestic general partnership, except when “partnership” is used as part of a multiword-term (*e.g.*, “foreign partnership”). Section 1101 contains definitions specific to Article 11’s provisions on mergers, conversions, interest exchanges, and domestications.

“Business” [(1)]—This definition originated in UPA (1914) § 2 and is fundamentally important; a general partnership must have a business purpose. *See* Section 202(a) (referring to the association of two or more persons to carry on as co-owners a business for profit). *Compare* Section 102(1), *with* ULPA (2001) (Last Amended 2013) § 110(b) (“A limited partnership may have any lawful purpose, regardless of whether for profit.”), *and* ULLCA (2006) (Last Amended 2013) § 108(a) (same as to a limited liability company).

“Contribution” [(2)]—This definition is based on ULPA (2001) § 102(2) (“Contribution”, except in the phrase “right of contribution”, means any benefit provided by a person to a limited partnership in order to become a partner or in the person’s capacity as a partner.”). UPA (1997) did not define “contribution.” The Harmonization Project added this definition.

This definition serves to distinguish capital contributions from other circumstances under which a partner or would-be partner might provide benefits to a general partnership (*e.g.*, providing services to the partnership as an employee or independent contractor, leasing property to the partnership).

This definition also distinguishes “contributions” from capital raised from transferees who invest; to be a contribution, the property or benefit must be “provided by a person ... to become a partner or in the person’s capacity as a partner. This distinction is ubiquitous in the law of unincorporated business organizations. *See, e.g.*, ULPA (2001) § 102(2) definition (quoted above); N.Y. LTD. LIAB. CO. LAW § 102(f) (McKinney 2013) (“‘Contribution’ means any cash, property, services rendered, or a promissory note or other binding obligation to contribute cash or property or to render services that a member contributes to a limited liability company in his or her capacity as a member.”)

In contrast, partnership agreements sometimes provide for contributions from transferees. In such circumstances, the default rules for liquidating distributions should be altered

accordingly. *See* Section 806(b)(1) (referring to distributions to be made “to each person owning a transferable interest that reflects *contributions* made and not previously returned.”) (emphasis added).

“Distribution” [(4)(A)—redemptions included]—This provision specifically refers to transactions between a general partnership and one of its partners, which in the corporate context would be labeled “redemption.” The paragraph has subparts because ownership interests in a partnership are conceptually bifurcated into economic rights (“transferable interest”), and governance and information rights.

Under Section 405(a), “[a]ny distribution made by a partnership before its dissolution and winding up must be in equal shares among partners, except to the extent necessary to comply with a transfer effective under Section 503 or charging order in effect under Section 504.” Since a redemption is a distribution, absent authorization in the partnership agreement a partnership may not redeem the interest of one partner or transferee without redeeming (or at least offering to redeem) the interests of all other partners and transferees to a comparable extent.

The law of close corporations has flirted with a similar notion. *See, e.g., Donahue v. Rodd Electrottype Co. of New England, Inc.*, 328 N.E.2d 505, 518 (Mass. 1975) (stating, with regard to closely held corporations, “if the stockholder whose shares were purchased was a member of the controlling group, the controlling stockholders must cause the corporation to offer each stockholder an equal opportunity to sell a ratable number of his shares to the corporation at an identical price”); *cf. Wilkes v. Springside Nursing Home, Inc.*, 353 N.E.2d 657, 663 (Mass. 1976) (stating that “untempered application of the strict good faith standard enunciated in *Donahue* . . . will result in the imposition of limitations on legitimate action by the controlling group in a close corporation which will unduly hamper its effectiveness in managing the corporation in the best interests of all concerned”). *See also Toner v. Baltimore Envelope Co.*, 498 A.2d 642, 650 (Md. 1985) (rejecting the “per se breach of duty” approach).

A partnership agreement can override Section 405(a)’s equal treatment requirement without specifically mentioning redemptions.

EXAMPLE: Ryan Company is a general partnership whose partnership agreement: (i) includes a list (the “protected list”) of decisions or actions that may be taken only with the consent of all partners; and (ii) provides that all other decisions and acts may be taken as the Management Committee determines. The protected list does not include redemptions. The partnership agreement overrides the Section 404(a)’s equal treatment requirement.

[(4)(B)—exclusion]—This exclusion affects the reach of: (i) the charging order remedy under Section 504; and (ii) Section 407’s clawback provision applicable to distributions made by a limited liability partnership. The effect on the clawback provision reflects the law in several states, *see, e.g.,* DEL. CODE ANN. tit. 6, § 15-309(a) (2014); VA. CODE ANN. § 13.1-1036 (2014), and makes sense conceptually and as a matter of policy. *See In re Tri-River Trading, L.L.C.*, 329 B.R. 252, 266 (B.A.P. 8th Cir. 2005), *aff’d*, 452 F.3d 756 (8th Cir. 2006) (“We know of no principle of law which suggests that a manager of a company is required to give up agreed upon

salary to pay creditors when business turns bad.”). UPA (1997) provides no clawback provision, an omission that disadvantaged creditors of an LLP compared to creditors of other entities with a liability shield.

“Foreign limited liability partnership” and “Foreign partnership” [(5) and (6)]—These definitions intend a flexible, comparative approach. Under Paragraph 6, if a particular type of foreign entity has key legal characteristics that approximate the essential legal characteristics of a domestic general partnership, that particular type of foreign entity is a foreign partnership under this act. Likewise, under Paragraph 5, if a foreign partnership has a liability shield similar to the shield provided under this act for a domestic LLP, the foreign partnership is a foreign limited liability partnership.

As further explained in the comment to Section 306(c), this act provides a full liability shield (*i.e.*, the shield applies regardless of the law giving rise to a claim against an LLP). A few jurisdictions provide only a partial shield. *See, e.g.*, 15 PA. CONS. STAT. ANN. § 8204 (West 2013) (providing the partners of an LLP a shield for claims against the partnership “whether sounding in contract or tort or otherwise,” but only the claims that “arise from any negligent or wrongful acts or misconduct committed by another partner or other representative of the partnership”). The resulting partial shield does not protect partners against liability for the partnership’s ordinary commercial debts, such as liability for lease payments. Nonetheless, a partial-shield foreign LLP would be a “foreign limited liability partnership” under Paragraph 6.

“Jurisdiction of formation” [(8)]—This definition” is not limited to United States jurisdictions.

“Limited liability partnership” [(9)]—Under this act (and most, if not all, LLP statutes), a general partnership obtains its LLP status from only one jurisdiction. The resulting LLP is “domestic” with regard to that jurisdiction and “foreign” with regard to all others.

Sections 901(f) (cancellation of statement of qualification) and 903 (administrative revocation of statement of qualification) limit this paragraph’s open-ended definition of a “limited liability partnership” as “a partnership that has filed a statement of qualification under Section 901.” Under this act, LLP status depends on a statement of qualification being in effect. *See* Section 903(d) and its comment.

“Partner” [(10)]—Under Section 202(a), any “person” can be a partner. Paragraph 14 of this section defines “person” very broadly to include individuals and “any . . . legal or commercial entity.” At common law, “[t]he general rule . . . [was] that every person of sound mind, *sui juris*, and not otherwise restrained by law, may enter into a contract of partnership.” JOSEPH STORY, COMMENTARIES ON THE LAW ON PARTNERSHIP § 7, at 10 (2d ed. 1850). The phrase “sound mind” and the term “*sui juris*” suggest that at common law a partner was necessarily an individual. *See* BLACK’S LAW DICTIONARY (9th ed. 2009) (defining *sui juris* as one “[o]f full age and capacity”). UPA (1914) § 2 defined “person” to include “partnerships, corporations, and other associations.” *See, e.g., Williams v. Mammoth of Alaska, Inc.*, 890 P.2d 581, 584 n.8 (Alaska 1995) (stating that under UPA (1914) “[a] partner need not be a natural person”).

After a person has been dissociated as a partner under Section 602, the term “partner” continues to apply to the person’s conduct while a partner. *See* Section 603(b).

“Partnership” [(11)]—This definition, combined with Section 202(a), makes clear that a general partnership is a *business* organization. This definition makes no reference to a partnership having partners upon formation, but Section 202(a) does.

“Partnership agreement” [(12)]—This definition must be read in conjunction with Sections 105 through 107, which further describe the partnership agreement. In particular, although this definition refers to “the agreement . . . of all the partners,” the partnership itself is bound by and may enforce the agreement. Section 106(a).

A partnership agreement is a contract, and therefore all statutory language pertaining to the partnership agreement must be understood in the context of the law of contracts.

The definition in Paragraph 12 is very broad and recognizes a wide scope of authority for the partnership agreement: “the matters described in Section 105(a).” Those matters include not only all relations *inter se* the partners and the partnership but also “the business of the partnership and the conduct of that business.” Section 105(a)(2). Moreover, the definition puts no limits on the form of the partnership agreement. To the contrary, the definition contains the phrase “whether oral, implied, in a record, or in any combination thereof.”

Unless the partnership agreement itself provides otherwise:

- A partnership agreement may comprise a number of separate documents (or records), however denominated; and
- Subject to Section 106(b) (deeming new partners to assent to the then-existing partnership agreement), a document, record, understanding, etc. can be part of the partnership agreement only with the assent of all persons then partners.

An agreement among less than all partners might well be enforceable among those partners as parties, but would not be part of the partnership agreement. However, under Section 105(a)(3), an amendment to a partnership agreement can be made with less than unanimous consent if the partnership agreement itself so provides.

An agreement to form a partnership is not itself a partnership agreement. The term “partnership agreement” presupposes “partners,” and a person cannot be a partner in a partnership before the partnership exists. However, as soon as a partnership comes into existence, it perforce has a partnership agreement. For example, suppose: (i) two persons orally and informally agree to join their activities in a manner that satisfies Section 202 (formation of partnership); (ii) the partnership is thus formed; and (iii) without further ado or agreement, the persons become the partnership’s initial partners. A partnership agreement exists. In the words of Paragraph 12 “all the partners” have agreed who the partners are and that, as “all the partners,” they will conduct a business. That agreement—no matter how informal or rudimentary—is an agreement “concerning the matters described in Section 105(a).” To the extent the agreement does not provide the *inter se* “rules of the game,” the “default rules” of this

act “fill in the gaps.” Section 105(b).

This act states no rule as to whether the statute of frauds applies to partnership agreements. Case law suggests that the answer is yes:

Partnership agreements, like other contracts, are subject to the Statute of Frauds. A contract of partnership for a term exceeding one year is within the Statute of Frauds and is void unless it is in writing [and signed by the party to be bound]; however, a contract establishing a partnership terminable at the will of any partner is generally held to be capable of performance by its terms within one year of its making and, therefore, to be outside the Statute of Frauds.

Abbott v. Hurst, 643 So. 2d 589, 592 (Ala. 1994) (citations omitted).

Likewise, the land provision of the statute of frauds:

applies to an oral contract to transfer or convey partnership real property, and the interest of the other partners therein, to one partner as an individual, as well as to a parol contract by one of the parties to convey certain land owned by him individually to the partnership, or to another partner, or to put it into the partnership stock.

Froiseth v. Nowlin, 287 P. 55, 56 (Wash. 1930) (quoting 27 C.J.S. § 220); *see also E. Piedmont 120 Associates, L.P. v. Sheppard*, 434 S.E.2d 101, 102 (Ga. Ct. App. 1993) (same, stating that “the fact that promises covered by the Statute of Frauds are made in the context of a partnership or joint venture agreement does not render the statute inapplicable”); *Filippi v. Filippi*, 818 A.2d 608, 618 (R.I. 2003) (applying the statute of frauds to an alleged oral agreement to transfer land owned by a limited partnership to one of its partners).

In contrast, the land provision does not apply to a partner’s interest in a partnership, no matter how much the partnership owns or deals in real property. Interests in a partnership are personal property and reflect no direct interest in the entity’s assets. *See* Sections 102(23), 501. Thus, the real property issues pertaining to a partnership ownership of land do not “flow through” to the partners and partnership interests. *See, e.g., Wooten v. Marshall*, 153 F. Supp. 759, 763–64 (S.D.N.Y. 1957) (involving an “oral agreement for a joint venture concerning the purchase, exploitation and eventual disposition of this 160 acre tract” and stating “[t]he real property acquired and dealt with by the venturers takes on the character of personal property as between the partners in the enterprise, and hence is not covered by [the Statute of Frauds]”); *see also Wade v. DeHart*, 1926 WL 2944 (Ohio Misc. 1926), *aff’d sub nom., Wade v. De Hart*, 159 N.E. 838 (Ohio Ct. App. 1927) (same).

On the question of how far a written (or “in a record”) partnership agreement can go to prevent oral or implied-in-fact terms, *see* Section 105(a)(3), comment. For the effect of a pre-formation agreement, *see* Section 106(c). For the partnership’s status viz-a-viz the partnership agreement, *see* Section 106(a).

“Partnership at will” [(13)]—This paragraph defines “partnership at will” in the

negative (*i.e.*, by stating what the defined term is not). A partnership is “at will” if the partners’ agreement does not obligate them to remain in the partnership until the passage of a specified time (a term) or the completion of a specified task, job, project, etc. (an undertaking).

“Partnership at will” is thus the default mode under this act; that is, a partnership is “at will” unless the partners have agreed otherwise. Absent such agreement, a partner may rightfully leave the partnership at any time (dissociate), Sections 601(1), 602(b)(2), and rightfully cause or seek the winding up of the partnership and its business (dissolution), Section 801(1); *see Fleming v. Hagen Estate*, 702 N.W.2d 786, 789 (Minn. Ct. App. 2005) (rejecting “the [appellant] estate’s assertion that the district court erred by not concluding that [a partner’s] counterclaim unilaterally dissolved the agreement pursuant to [Minnesota Statutes section 323A.0801]”); noting that “section 323A.0801(1) is applicable only to an at-will partnership”).

This act does not directly define “partnership for a term” and “partnership for an undertaking,” but their respective meanings are clear from this paragraph’s wording and the case law. *E.g.*, *Girard Bank v. Haley*, 332 A.2d 443, 447 (Pa. 1975) (“A ‘particular undertaking’ under the statute must be capable of accomplishment at some time, although the exact time may be unknown and unascertainable at the date of the agreement.”). This paragraph thus suggests that a partnership under this act will fit into one of three conveniently labeled categories: at-will, for a term, for an undertaking. However, hybrid structures are possible.

EXAMPLE: The partnership agreement of a general partnership:

- states a minimum term of ten years;
- permits one particular partner to leave the partnership at any time upon thirty days advance written notice; and
- provides that that person’s dissociation as a partner will neither cause the partnership to dissolve nor entitle any other person to dissociate.

Hybrid structures cause no trouble, if the partnership agreement: (i) clearly and completely details the partners’ understanding as to dissociation and dissolution; and (ii) does not confuse matters by inaccurately labeling the partnership as if it were a pure form of one of the three categories.

“Principal office” [(15)]—This term appears mostly in provisions pertaining to court proceedings, *e.g.*, Section 809(a), or delivery or service of information; *e.g.*, Sections 117(f)(3), 912(b). The term also helps determine the governing law for a partnership that is not a limited liability partnership. Section 104(2).

UPA (1997) referred to a partnership’s “chief executive office,” *e.g.*, UPA (1997) § 106(a), but did not define the term. *Id.*, cmt. The Harmonization Project substituted “principal office,” as a more traditional and better-understood term in business entity statutes. In most cases, a partnership’s principal office will be the same as the partnership’s chief executive office (however defined). With regard to LLPs and foreign LLPs registered to do business in this state, the annual/biennial report will record the LLP’s view on where the LLP’s principal office is located. *See* Sections 913(a)(3) (domestic LLP), 1003(4) (foreign LLP).

“Property” [(16)]—This definition encompasses every form of property. For rules determining when property belongs to the partnership, see Section 204.

“Transfer” [(22)]—The term “transfer” is broadly defined to include all types of conveyances of interests in property. The reference to “transfer by operation of law” is significant in connection with Section 502 (Transfer of Transferable Interest). That section severely restricts a transferee’s rights (absent the consent of the partners), and this definition makes those restrictions applicable; for example, to transfers ordered by a family court as part of a divorce proceeding and transfers resulting from the death of a partner. The restrictions also apply to transfers in the context of a partner’s bankruptcy, except to the extent that bankruptcy law supersedes this act.

“Transferable interest” [(23)]—Absent a contrary provision in the partnership agreement or the consent of the partners, a “transferable interest” is the only interest in a partnership which can be transferred to a non-partner. *See* the comment to Section 502. This act does not define any term to encompass the entirety of a partner’s rights in a partnership (*i.e.*, governance and information rights as well as economic rights).

UPA (1997) took a different approach, defining the entirety of a partner’s rights directly and identifying the economic aspect through a limit on transferability. *See* UPA (1997) §§ 101(9) (defining “[p]artnership interest” or “partner’s interest in the partnership” as “all of a partner’s interests in the partnership, including the partner’s transferable interest and all management and other rights”), 502 (stating that “the only transferable interest of a partner in the partnership is the partner’s share of the profits and losses of the partnership and the partner’s right to receive distributions”).

This act defines “[t]ransferable interest” as an interest “initially owned by a person in the person’s capacity as a partner,” because this act does not contemplate a partnership directly creating interests that comprise only economic rights. *See* Sections 402 (addressing how a person becomes a partner), 503 (addressing how a person becomes a transferee).

SECTION 103. KNOWLEDGE; NOTICE.

(a) A person knows a fact if the person:

- (1) has actual knowledge of it; or
- (2) is deemed to know it under subsection (d)(1) or law other than this [act].

(b) A person has notice of a fact if the person:

(1) has reason to know the fact from all the facts known to the person at the time in question; or

- (2) is deemed to have notice of the fact under subsection (d)(2).

(c) Subject to Section 117(f), a person notifies another person of a fact by taking steps reasonably required to inform the other person in ordinary course, whether or not those steps cause the other person to know the fact.

(d) A person not a partner is deemed:

(1) to know of a limitation on authority to transfer real property as provided in Section 303(g); and

(2) to have notice of:

(A) a person's dissociation as a partner 90 days after a statement of dissociation under Section 704 becomes effective; and

(B) a partnership's:

(i) dissolution 90 days after a statement of dissolution under Section 802 becomes effective;

(ii) termination 90 days after a statement of termination under Section 802 becomes effective; and

(iii) participation in a merger, interest exchange, conversion, or domestication, 90 days after articles of merger, interest exchange, conversion, or domestication under [Article] 11 become effective.

(e) A partner's knowledge or notice of a fact relating to the partnership is effective immediately as knowledge of or notice to the partnership, except in the case of a fraud on the partnership committed by or with the consent of that partner.

Comment

The Harmonization Project made two important changes to this section. First, unlike UPA (1997), this act contains no generally applicable provisions determining when an organization other than a partnership is charged with knowledge or notice, because those imputation rules: (i) comprise core topics within the law of agency; (ii) are very complicated; (iii) should not have

any different content under this act than in other circumstances; and (iv) are the subject of considerable attention in the Restatement (Third) of Agency (2006). However, Subsection (e) does provide a rule for attributing to a partnership knowledge or notice possessed by a partner.

Second, this act does not define “notice” to include “knowledge.” Although conceptualizing the latter as giving the former makes logical sense and has a long pedigree, that conceptualization is counter-intuitive for the uninitiated. In ordinary usage, notice has a meaning separate from knowledge. This act follows ordinary usage and therefore contains some references to “knowledge or notice.”

Subsection (a)(2)—In this context, the most important source of “law other than this [act]” is the common law of agency.

Subsection (b)(1)—The “facts known to the person at the time in question” include facts the person is deemed to know under Subsection (a)(2).

Subsection (c)—If a person “notifies” another person of a fact, the other person has “reason to know” the fact and therefore has notice under Subsection (b)(1). However, a person can have “notice” of a fact without having been “notified” of the fact.

Section 117(f) pertains to delivery of records *by* the filing office.

Subsection (d)—Following the pioneering approach of UPA (1997), this subsection provides constructive notice of facts stated in specified filed public records. The subsection works in conjunction with other sections of this act to curtail the power to bind and personal liability of partners and persons dissociated as partners. *See* Sections 702, 703, 804, 805. The constructive notice begins ninety days after the effective date of the filed record. For this act’s rules on delayed effective dates, see Section 114.

UPA (1997) used an oblique and decentralized approach to constructive notice. *See, e.g.,* UPA (1997) § 704(c) (stating that “for the purposes of Sections 702(a)(3) [pertaining to the lingering power to bind the partnership of a person dissociated as a partner] and 703(b)(3) [pertaining to a the lingering liability for partnership obligations of a person dissociated as a partner], a person not a partner is deemed to have notice of the dissociation 90 days after [a] statement of dissociation is filed”). As revised by the Harmonization Project, this subsection provides directly for constructive notice and centralizes all of this act’s constructive notice provisions except for those pertaining to statements of authority under Section 303.

Subsection (e)—This subsection states the rule for imputing a partner’s knowledge or notice to the partnership. The rule was part of the common law. *Peoples' Bank of Baltimore v. Keech*, 26 Md. 521, 533 (Md. 1867) (holding that “the firm is bound by notice to one of the co-partners; because each represents the firm and is general agent of all”). UPA (1914) § 12 codified the rule, and UPA (1997) § 102(f) carried forward the codified rule with some modification. The Harmonization Project did not change UPA (1997) § 102(f), except to delete “receipt of a notification”; the phrase “receipt of a notification” is no longer a term of art in the LLC and partnership acts.

SECTION 104. GOVERNING LAW. The internal affairs of a partnership and the liability of a partner as a partner for a debt, obligation, or other liability of the partnership are governed by:

- (1) in the case of a limited liability partnership, the law of this state; and
- (2) in the case of a partnership that is not a limited liability partnership, the law of the jurisdiction in which the partnership has its principal office.

Comment

This section states two choice-of-law rules: an invariable rule for limited liability partnerships, Paragraph 1, and a default rule for non-LLPs, Paragraph 2. Both rules address “internal affairs” and “the liability of a partner as a partner for the debts, obligations, or other liabilities of the partnership.”

Like any other legal concept, “internal affairs” may be indeterminate at its edges. However, the concept certainly includes interpretation and enforcement of the partnership agreement, relations among the partners as partners, and relations between the partnership and a partner as a partner. *Compare* Section 104, with RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 302, cmt. a (1971) (defining “internal affairs” with reference to a corporation as “the relations inter se of the corporation, its shareholders, directors, officers or agents”).

“Internal affairs” do not encompass the power *vel non* of a person to bind a partnership. RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 292(2) (1971) (“The principal will be held bound by the agent’s action if he would so be bound under the local law of the state where the agent dealt with the third person, provided at least that the principal had authorized the agent to act on his behalf in that state or had led the third person reasonably to believe that the agent had such authority.”), 295(1) (“Whether a partnership is bound by action taken on its behalf by an agent in dealing with a third person is determined by the local law of the state selected by application of the rule of § 292.”); RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 345, cmt. c (1934) (Law Governing Effect of Act of Agent or Partner) (“If . . . the principal or partner sends the agent or other partner into a state to act on his behalf, he assumes the risk of liability not only for authorized but for unauthorized conduct of the agent or partner in accordance with the law of that state.”); *see also Farm & Ranch Services, Ltd. v. LT Farm & Ranch, L.L.C.*, 779 F. Supp. 2d 949, 960 (S.D. Iowa 2011).

“Internal affairs” and the “liability of a partner as a partner” are mentioned separately, because it can be argued that the liability of partners to third parties is not an internal affair. *See, e.g.*, RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 307 (1971) (treating shareholders’ liability separately from the internal affairs doctrine). A few cases subsume owner/manager liability into internal affairs. *See, e.g., Kalb, Voorhis & Co. v. American Fin. Corp.*, 8 F.3d 130, 132 (2d Cir. 1993) (holding that the corporation’s “primary purpose is to insulate shareholders from legal

liability” and therefore “the state of incorporation has the greater interest in determining when and if that insulation is to be stripped away” (quoting *Soviet Pan Am Travel Effort v. Travel Comm., Inc.*, 756 F. Supp. 126, 131 (S.D.N.Y. 1991) (internal quotation marks omitted)).

In any event, neither “internal affairs” nor the “liability of a partner as a partner” encompass a claim that a partner is liable to a third party for: (i) having purported inaccurately to have the actual authority to bind a partnership to the third party; or (ii) having committed a tort against the third party while acting on the partnership’s behalf or in the course of the partnership’s business. That liability is not by status (*i.e.*, not “as a partner”) but rather results from function or conduct.

Treating “liability of a partner as a partner” as a matter of domestic law comports generally with the law of business entities. For example, some (if not all) limited liability partnership statutes so provide. *E.g.*, DEL. CODE ANN. tit. 6, § 15-1101(a) (2013) (stating that “[t]he law under which a foreign limited liability partnership is formed governs . . . the liability of partners for obligations of the partnership”); N.Y. P’SHP LAW § 121-1502(l) (2014) (stating that “[t]he laws of the jurisdiction that govern a foreign limited liability partnership shall determine . . . the liability of partners for debts, obligations and liabilities of, or chargeable to, the foreign limited liability partnership”).

Moreover, “[t]he general rule [from the case law] is that a plaintiff’s alter ego theory is governed by the law of the state in which the business at issue is organized.” *Rual Trade Ltd. v. Viva Trade L.L.C.*, 549 F. Supp. 2d 1067, 1077 (E.D. Wis. 2008); *see also In re Gulf Fleet Holdings, Inc.*, 491 B.R. 747, 787 (Bankr. W.D. La. 2013) (stating both conceptual and policy rationales for choosing the law of the state of formation); *In re Saba Enters., Inc.*, 421 B.R. 626, 648–51 (Bankr. S.D.N.Y. 2009) (examining the issue in detail and applying the state of formation rule).

Paragraph 1—The partnership agreement cannot alter this paragraph. *See* Section 105(c)(1). In essence, when a partnership chooses where to deliver for filing a statement of qualification, the partnership chooses its governing law. This approach comports with the law of other businesses entities whose formation or legal status depends at least in part on a publicly filed record. *See, e.g.*, ULPA (2001) (Last Amended 2013) § 104 (stating that the law of the state of formation is the domestic entity’s governing law); ULLCA (2006) (Last Amended 2013) § 104 (same).

However, a partnership agreement may lawfully incorporate by reference the provisions of another state’s partnership act. If done correctly, this incorporation makes the foreign statutory language part of the partnership agreement, and the incorporated terms (together with the rest of the partnership agreement) then govern the partners (and those claiming through the partners) to the extent not prohibited by this act. *See* Section 105. This approach: (i) does not switch the limited liability partnership’s governing law to that of another state; (ii) instead takes the provisions of another state’s law and incorporates them by reference into the contract among the partners; (iii) raises complex drafting issues – *e.g.*, how to address subsequent changes to the incorporated law (whether occurring by statutory amendment or court decision); and (iv) thus is rarely, if ever, a good idea.

Paragraph 2—Section 102(15) defines “principal office.”

The partnership agreement may change the rule stated in this paragraph, although other law may limit a partnership’s options. *See* RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 294 (1971) (Relationship of Partners Inter Se), 187(2) (stating the limited bases for disregarding a contractual choice of law).

When a statement of qualification becomes effective under Section 901: (i) this paragraph no longer applies; and (ii) neither the partnership’s principal office nor the partnership agreement is relevant to determining the law governing the partnership’s internal affairs. Section 105(c)(1) (stating that the partnership agreement may not “vary the law applicable under Section 104(1)”).

SECTION 105. PARTNERSHIP AGREEMENT; SCOPE, FUNCTION, AND LIMITATIONS.

(a) Except as otherwise provided in subsections (c) and (d), the partnership agreement governs:

(1) relations among the partners as partners and between the partners and the partnership;

(2) the business of the partnership and the conduct of that business; and

(3) the means and conditions for amending the partnership agreement.

(b) To the extent the partnership agreement does not provide for a matter described in subsection (a), this [act] governs the matter.

(c) A partnership agreement may not:

(1) vary the law applicable under Section 104(1);

(2) vary the provisions of Section 110;

(3) vary the provisions of Section 307;

(4) unreasonably restrict the duties and rights under Section 408, but the partnership agreement may impose reasonable restrictions on the availability and use of information obtained under that section and may define appropriate remedies, including

liquidated damages, for a breach of any reasonable restriction on use;

(5) alter or eliminate the duty of loyalty or the duty of care, except as otherwise provided in subsection (d);

(6) eliminate the contractual obligation of good faith and fair dealing under Section 409(d), but the partnership agreement may prescribe the standards, if not manifestly unreasonable, by which the performance of the obligation is to be measured;

(7) unreasonably restrict the right of a person to maintain an action under Section 410(b);

(8) relieve or exonerate a person from liability for conduct involving bad faith, willful or intentional misconduct, or knowing violation of law;

(9) vary the power of a person to dissociate as a partner under Section 602(a), except to require that the notice under Section 601(1) to be in a record;

(10) vary the grounds for expulsion specified in Section 601(5);

(11) vary the causes of dissolution specified in Section 801(4) or (5);

(12) vary the requirement to wind up the partnership's business as specified in Section 802(a), (b)(1), and (d);

(13) vary the right of a partner under Section 901(f) to vote on or consent to a cancellation of a statement of qualification;

(14) vary the right of a partner to approve a merger, interest exchange, conversion, or domestication under Section 1123(a)(2), 1133(a)(2), 1143(a)(2), or 1153(a)(2);

(15) vary the required contents of a plan of merger under Section 1122(a), plan of interest exchange under Section 1132(a), plan of conversion under Section 1142(a), or plan of domestication under Section 1152(a);

(16) vary any requirement, procedure, or other provision of this [act] pertaining to:

(A) registered agents; or

(B) the [Secretary of State], including provisions pertaining to records authorized or required to be delivered to the [Secretary of State] for filing under this [act]; or

(17) except as otherwise provided in Sections 106 and 107(b), restrict the rights under this [act] of a person other than a partner.

(d) Subject to subsection (c)(8), without limiting other terms that may be included in a partnership agreement, the following rules apply:

(1) The partnership agreement may:

(A) specify the method by which a specific act or transaction that would otherwise violate the duty of loyalty may be authorized or ratified by one or more disinterested and independent persons after full disclosure of all material facts; and

(B) alter the prohibition in Section 406(a)(2) so that the prohibition requires only that the partnership's total assets not be less than the sum of its total liabilities.

(2) To the extent the partnership agreement expressly relieves a partner of a responsibility that the partner would otherwise have under this [act] and imposes the responsibility on one or more other partners, the agreement also may eliminate or limit any fiduciary duty of the partner relieved of the responsibility which would have pertained to the responsibility.

(3) If not manifestly unreasonable, the partnership agreement may:

(A) alter or eliminate the aspects of the duty of loyalty stated in Section 409(b);

(B) identify specific types or categories of activities that do not violate the duty of loyalty;

(C) alter the duty of care, but may not authorize conduct involving bad faith, willful or intentional misconduct, or knowing violation of law; and

(D) alter or eliminate any other fiduciary duty.

(e) The court shall decide as a matter of law whether a term of a partnership agreement is manifestly unreasonable under subsection (c)(6) or (d)(3). The court:

(1) shall make its determination as of the time the challenged term became part of the partnership agreement and by considering only circumstances existing at that time; and

(2) may invalidate the term only if, in light of the purposes and business of the partnership, it is readily apparent that:

(A) the objective of the term is unreasonable; or

(B) the term is an unreasonable means to achieve the term's objective.

Comment

The Harmonization Project re-wrote this section, for the most part conforming this section to the corresponding section of ULLCA (2006).

Principal Provisions of the Act Concerning the Partnership Agreement

The partnership agreement is pivotal to a partnership, and Sections 105 through 107 are pivotal to this act. They must be read together, along with Section 102(12) (defining the partnership agreement).

This section performs five essential functions. Subsection (a) establishes the primacy of the partnership agreement in establishing *inter se* relations among the partners and partnership. Subsection (b) recognizes this act as comprising mostly default rules (*i.e.*, gap fillers for issues as to which the partnership agreement provides no rule). Subsection (c) lists the few mandatory provisions of the act. Subsection (d) lists some provisions frequently found in partnership agreements, authorizing some unconditionally and others so long as “not manifestly unreasonable.” Subsection (e) delineates in detail both the meaning of “not manifestly unreasonable” and the information relevant to determining a claim that a provision of a partnership agreement is manifestly unreasonable.

Section 106 details the effect of a partnership agreement on the partnership and on persons becoming partners. Section 107 concerns the effect of a partnership agreement on third parties.

Role and Inevitability of Partnership Agreement

Section 102(12) delineates a very broad scope for “partnership agreement.” As a result, once a partnership comes into existence, a partnership agreement necessarily exists. *See* the comment to Section 102(12). Accordingly, this act refers to “the partnership agreement” rather than “a partnership agreement.” This phrasing should not, however, be read to require a partnership or its partners to take any formal action to adopt a partnership agreement.

The partnership agreement is the exclusive consensual process for modifying this act’s various default rules pertaining to relationships *inter se* the partners and between the partners and the partnership. Section 105(a). The partnership agreement also has power over “the obligations of a partnership and its partners to a person in the person’s capacity as a transferee or person dissociated as a partner.” Section 107(b). For the relationship between the partnership agreement and public records in the filing office, see Section 107(d).

The Partnership Agreement and the Fiduciary and Other Duties of Those Who Manage

One of the most complex questions in the law of unincorporated business organizations is the extent to which an agreement among the organization’s owners can affect the fiduciary and other duties of those who have ultimate power to manage the organization—in a general partnership, the partners themselves. As explained in detail in the comment to Subsection (d)(3), this act rejects the notion that a contract can completely transform an inherently fiduciary relationship into a merely arm’s length association. Within that limitation, however, this section provides substantial power to the partnership agreement to reshape, limit, and eliminate fiduciary and other managerial duties.

Subsection (a) recognizes that the partnership agreement is the map to the parties’ deal and that any claim by a partner of managerial misconduct must be assessed first under the relevant terms of the partnership agreement. Subsection (d) specifically validates arrangements commonly used to reshape managerial duties and limit the consequences of breaching those duties. Subsection (c) contains relevant limitations, but those limitations: (i) must be read together with Subsection (d); and (ii) do not preclude the partnership agreement fundamentally redesigning the duties applicable to the partners. For the act’s design of those duties, see Sections 408 and 409.

Subsection (a)—This section describes the very broad scope of a partnership’s partnership agreement, which includes all matters constituting “internal affairs.” *Compare* Section 105(a), *with* Section 104 (using the phrase “internal affairs” in stating a choice of law rule). This broad grant of authority is subject to the restrictions stated in Subsection (c), including the broad restriction stated in Subsection (c)(17) (concerning the rights of third parties under this act).

Subsection (a)(1)—This paragraph encompasses all the rights and duties of each partner, including rights and duties pertaining to transactions under Article 11.

Subsection (a)(3)—Under this provision, the partnership agreement can control both the quantum of consent required (*e.g.*, majority of partners) and the means by which the consent is manifested (*e.g.*, prohibiting modifications except when consented to in writing). *See* the comment to Section 107(a).

If the partnership agreement does not address the issue, Section 401(k) applies and requires the affirmative vote or consent of all the partners. Under Section 119 (supplemental principles of law), the parol evidence rule will apply to a written partnership agreement when appropriate under contract law.

Subsection (b)—To the extent the partnership agreement does not determine an *inter se* matter, this act determines the matter. The partnership agreement may vary any provision of this act pertaining to *inter se* matters, except as provided in Subsections (c) and (d).

Sometimes—but not always—the comments to this act refer to a variable provision as a “default rule” and a non-waivable provision as “mandatory.” These references are merely to draw attention to the default/mandatory distinction in particular contexts and have neither the intent nor the power to affect the default/mandatory status of provisions of this act whose comments lack a comparable reference.

Subsection (c)—This subsection lists provisions of this act whose respective effects cannot be varied or may be varied subject to a stated limitation. For historical reasons, this subsection uses the words “vary” and “alter” interchangeably. No difference in meaning is intended.

If a person claims that a term of the partnership agreement violates this subsection, as a matter of ordinary procedural law the burden of proof is on the person making the claim.

Subsection (c)(1)—“[T]he law applicable under Section 104(1)” establishes the governing law for the internal affairs of a partnership. The organizers of a partnership make this choice of law by choosing to form a partnership under this act. Domestication to another jurisdiction will re-set the choice of law, *see* Sections 1151–56, but the partnership agreement cannot. *See* the comment to Section 104(1).

Subsection (c) contains no parallel prohibition on varying Section 901 (stating the governing law for foreign limited liability partnerships), because a prohibition is unnecessary. As a matter of fundamental contract law, an agreement among partners of one partnership is powerless to govern the affairs of another partnership.

Subsection (c)(3)—Under this act, a partnership is emphatically an entity, and the partners lack the power to alter that characteristic.

The cited section pertains to “actions by and against partnership and partners,” arguably

comes within Subsection (c)(17) (prohibiting the partnership agreement from “restrict[ing] the rights under this [act] of a person other than a partner”), but is specifically noted for the avoidance of doubt.

Subsection (c)(4)—Although phrased as a restriction, this provision grants substantial power to the partnership agreement.

EXAMPLE: A law firm operates as a partnership, and the partnership agreement provides that a “Compensation Committee” periodically decides each partner’s compensation. The agreement also states that only partners who are on the Compensation Committee may have access to the Committee’s compensation decisions pertaining to other partners. This restriction is reasonable.

The act also empowers the partnership “as a matter within the ordinary course of its business [to] impose reasonable restrictions and conditions on access to and use of information” obtained under Section 408. *See* Section 408(j).

In determining whether a restriction is reasonable, a court might consider: (i) the danger or other problem the restriction seeks to avoid; (ii) the purpose for which the information is sought; and (iii) whether, in light of both the problem and the purpose, the restriction is reasonably tailored.

Subsection (c)(5)—This limitation is less powerful than might first appear, because Subsection (d) specifically authorizes substantial alterations to the duties of loyalty and care, including restricting and substantially eliminating those duties.

Subsection (c)(6)—Section 409(d) refers to the “contractual obligation of good faith and fair dealing,” which contract law implies in every contract. The partnership agreement cannot eliminate this obligation, neither in whole (*i.e.*, generally) nor in part (*i.e.*, as applicable to specified situations).

However, a partnership agreement may “prescribe the standards . . . by which the performance of [that] obligation is to be measured.”

EXAMPLE: A partnership agreement designates a managing partner, provides that partner almost total control of the partnership’s operations, and grants the partner the discretion to cause the partnership to enter into contracts with affiliates of the partner (so-called “Conflict Transactions”). The agreement further provides: “When causing the Company to enter into a Conflict Transaction, the Managing Partner complies with Section 409(d) of [this act] if a disinterested person, knowledgeable in the subject matter, states in writing that the terms and conditions of the Conflict Transaction are equivalent to the terms and conditions that would be agreed to by persons at arm’s length in comparable circumstances.” This provision “prescribes[s] the standards by which the performance of the [Section 409(d)] obligation is to be measured.”

EXAMPLE: Same facts as the previous example, except that, during the performance of

a Conflict Transaction, the managing partner causes the partnership to waive material protections under the applicable contract. The standard stated in the previous example is inapposite to this conduct. Section 409(d) therefore applies to the conduct without any direct contractual delineation. (However, other terms of the agreement may be relevant to determining whether the conduct violates Section 409(d). *See* the comment to Section 409(d).)

EXAMPLE: A partnership agreement designates a managing partner and gives that partner “sole discretion” to make various decisions. The agreement further provides: “Whenever this agreement requires or permits the Managing Partner to make a decision that has the potential to benefit one class of partners to the detriment of another class, the Managing Partner complies with Section 409(d) of [this act] if the Managing Partner makes the decision with:

- a. the honest belief that the decision:
 - i. serves the best interests of the Partnership; or
 - ii. at least does not injure or otherwise disserve those interests; and
- b. the reasonable belief that the decision breaches no partner’s rights under this agreement.”

This provision “prescribe[s] the standards by which the performance of the [Section 409(d)] obligation is to be measured.” *Compare* Section 105(c)(6), *with Nemec v. Shrader*, 991 A.2d 1120 (Del. 2010) (considering such a situation in the context of the right to call preferred stock and deciding by a three-two vote that exercising the call did not breach the implied covenant of good faith and fair dealing).

A partnership agreement that seeks to prescribe standards for measuring the contractual obligation of good faith and fair dealing under Section 409(d) should expressly refer to the obligation. *See Gerber v. Enter. Prods. Hldgs., L.L.C.*, 67 A.3d 400, 418 (Del. 2013) (distinguishing between the implied contractual covenant and an express contractual obligation of “good faith” as stated in a limited partnership agreement).

For an explanation of the function and role of the covenant of good faith and fair dealing, see the comment to Section 409(d). For the rules delimiting the “not manifestly unreasonable” requirement, see Subsection (e).

Subsection (c)(7)—Section 410(b) delineates a partner’s rights to “maintain an action against the partnership or another partner.” It would be unreasonable to frustrate these rights but not unreasonable to channel their exercise. For example, the partnership agreement might select a forum, require pre-suit mediation, provide for arbitration, or require a pre-suit demand on a management committee before a partner files suit against the partnership. Similarly, it is not unreasonable to provide for liquidated damages consonant with the law of contracts. In contrast, it would be unreasonable for a partnership agreement to both: (i) require a partner intending to sue the partnership to make demand on a management committee before filing suit against the partnership regardless of futility; and (ii) bar taking the claim to court no matter how long the management committee ponders the demand.

Subsection (c)(8)—These restrictions are ubiquitous in the law of business entities and,

in conjunction with other provisions of this section, control the otherwise very broad power of a partnership agreement to affect fiduciary and other duties. The restrictions are central to the raft of exculpatory provisions that sprung up in corporate statutes in response to *Smith v. Van Gorkum*, 488 A.2d 858 (Del. 1985), *overruled on other grounds by Gantler v. Stephens*, 965 A.2d 695 (Del. 2009). Delaware led the response with Delaware Code Annotated title 8, section 102(b)(7), and a number of LLC statutes have similar provisions. *E.g.*, GA. CODE ANN. § 14-11-305(4)(A) (2011). For an extreme example, see Virginia Code Annotated section 13.1-1025 (B) (2012). In this context, “conduct” includes both acts and omissions. BLACK’S LAW DICTIONARY (9th ed. 2009) (defining conduct as “[p]ersonal behavior, whether by action or inaction”).

The term “bad faith” has multiple meanings, and the context determines which meaning applies. In the context of the duty of loyalty, “bad faith” includes conduct motivated by ill will or other intent purposely to harm another person. The concept also includes conduct from which a person derives an improper personal benefit. *See, e.g., Mroz v. Hoaloha Na Eha, Inc.*, 410 F. Supp. 2d 919, 936–37 (D. Haw. 2005) (denying a motion to dismiss a claim that “the Majority Partners” were personally liable for the partnership’s wrongful termination of the plaintiff; quoting the complaint as alleging that “the Majority Partners, individually and as a group, acted with malice and/or ill will, and/or with an intent to serve their own personal interests and/or without an intent to serve company interests, and/or outside of the scope of their authority and/or without justification”); *BOGNC, LLC v. Cornelius NC Self-Storage L.L.C.*, 10 CVS 19072, 2013 WL 1867065, at *9 (N.C. Super. [Business Court] May 1, 2013) (noting that “no . . . [exculpatory] provision may limit a manager’s liability for acts known to be in conflict with the interests of the limited liability company, or for acts from which the manager derived an improper personal benefit”) (citing N.C. GEN. STAT. § 57C-3-32(b)); *Lasica v. Savers Grp. of Minn., L.L.C.*, A12-0092, 2012 WL 3553246, at *2 (Minn. Ct. App. Aug. 20, 2012) (noting that an “individual seeking indemnification [under statute providing for indemnification] must have acted in good faith and must not have received an improper personal benefit”) (citing MINN. STAT. § 322B.699, subdivs. 2(a)(2), (3) (2010)).

In the context of the duty of care, the concept of bad faith comes primarily from corporate law and means an extreme breach of the duty (*i.e.*, “the failure to exercise “*honest judgment* in the lawful and legitimate furtherance of corporate purposes”). *Deblinger v. Sani-Pine Products Co., Inc.*, 107 A.D.3d 659, 661 (N.Y. 2013) (quoting *Auerbach v. Bennett*, 393 N.E.2d 994 (N.Y. 1979)) (emphasis added) (internal quotation marks omitted).

Thus, when a plaintiff alleges bad faith as pertaining to the duty of care, “[t]he burden . . . is to show irrationality: a plaintiff must demonstrate that no reasonable business person could possibly authorize the action in good faith. Put positively, the decision must go so far beyond the bounds of reasonable business judgment that its only explanation is bad faith.” *In re Tower Air, Inc.*, 416 F.3d 229, 238 (3d Cir. 2005) (discussing then prevailing Delaware law) (citation omitted); *see also KDW Restructuring & Liquidation Servs. L.L.C. v. Greenfield*, 874 F. Supp. 2d 213, 226 (S.D.N.Y. 2012) (referring to a lack of “a rationale corporate purpose” and “a disregard for the duty to examine all available information—*information that was readily at hand*”) (emphasis added).

With regard to both the duty of loyalty and the duty of care, “bad faith” is entirely distinct

from the meaning of “good faith” in the contractual covenant of good faith and fair dealing. *See* the comment to Section 409(d).

Subsection (c)(8) pertains to indirect as well as direct efforts to “relieve or exonerate” and thus limits how far a partnership agreement can go in providing for indemnification. *See* Section 401(c) (stating a default rule for indemnification).

Although this paragraph does not expressly address contracts between a partnership and a partner, the stated constraints must also apply to such contracts. If not, those constraints are effectively meaningless.

EXAMPLE: A general partnership enters into a management contract with its sole managing partner, and the contract provides the partner exoneration for liability to the partnership even for willful and intentional misconduct. Most likely, contract law will treat the provision as against public policy and therefore unenforceable. RESTATEMENT (SECOND) OF CONTRACTS § 195(1) (1981) (“A term exempting a party from tort liability for harm caused intentionally or recklessly is unenforceable on grounds of public policy.”). If not, a court should hold the provision unenforceable to avoid evisceration of Subsection (c)(8). (Or, the court could invoke the policy expressed in Subsection (c)(8) as grounds for holding the provision unenforceable under contract law.)

Subsection (c)(9)—As a result of this restriction, a partner always has the power to dissociate; the partnership agreement can only negate the right. This approach is consistent with the notions that: (i) a partnership is a voluntary association, *see, e.g., Gangl v. Gangl*, 281 N.W.2d 574, 580 (N.D. 1979) (stating that “[t]he term [association] connotes not only a group of two or more persons but also voluntariness”); (ii) the partnership relationship is essentially contractual, *see, e.g., Wallner v. Schmitz*, 239 Minn. 93, 95, 57 N.W.2d 821, 823 (1953) (stating that “[a] partnership is a contractual relationship as between the parties”); and (iii) only in exceptional circumstances does a party to a contract lack the power to breach, and courts will not enjoin a person to remain in an ongoing contractual relationship that involves trust and confidence. E. ALLAN FARNSWORTH, CONTRACTS § 12.7, at 781 (3d ed.1999) (“A court will not grant specific performance of a contract to provide a service that is personal in nature. This refusal . . . is based [in part] of the undesirability of compelling the continuance of personal relations after disputes have arisen and confidence and loyalty have been shaken and the undesirability, in some instances, of imposing what might seem like involuntary servitude.”) (footnote omitted).

Subsection (c)(10)—The partnership agreement may not change the stated grounds for expulsion but may determine the forum in which a claim for expulsion under Section 601(5) is determined.

Subsection (c)(11)—The partnership agreement may not change the stated grounds for dissolution but may determine the forum in which a claim for dissolution under Section 801(4) or (5) is determined. For example, arbitration and forum selection clauses are commonplace in business relationships in general and in partnership agreements in particular.

The approach of this paragraph differs from the law of Delaware. *See Huatuco v. Satellite Healthcare*, CV 8465-VCG, 2013 WL 6460898, at *1, n.2 (Del. Ch. Dec. 9, 2013) (stating that “the right to judicial dissolution is a default right which the parties may eschew by contract” but reserving the question of “[w]hether the parties may, by contract, divest this Court of its authority to order a dissolution in all circumstances, even where it appears manifest that equity so requires—leaving, for instance, irreconcilable members locked away together forever like some alternative entity version of Sartre’s *Huis Clos*”).

Subsection (c)(12)—The cited provisions comprise the non-waivable aspects of winding up a dissolved partnership. The other provisions of Section 802 are default rules and therefore waivable.

Subsection (c)(13)—Section 901(f) requires the “the affirmative vote or consent of all the partners.” The requirement is non-waivable, because canceling a statement of qualification eliminates the LLP liability shield and makes each partner automatically liable for partnership’s obligations subsequently incurred.

Subsection (c)(14)—Sections 1123(a)(1), 1133(a)(1), 1143(a)(1), and 1153(a)(1) each requires the consent or the affirmative vote of all partners. The partnership agreement may modify these requirements. In contrast, under the sections stated in this subsection:

- each partner is protected from being merged, exchanged, converted, or domesticated “into” the status of a partner in a general partnership that is not a limited liability partnership (or a comparable “unshielded” position in some other organization) without the partner having *directly* consented to either:
 - the merger, interest exchange, conversion, or domestication; or
 - a partnership agreement provision that permits such transactions to occur with less than unanimous consent of the partners; and
- merely consenting to a partnership agreement provision that permits amendment of the partnership agreement with less than unanimous consent of the partners does not qualify as the requisite direct consent.

Subsection (c)(15)—Because these plans are the basic “deal documents” for each of the organic transactions contemplated in Article 11, the partnership agreement may not vary the contents of these plans.

Subsection (c)(16)—This prohibition is arguably implicit in Subsection (c)(17) (affecting rights under this act of third parties) but is stated expressly to avoid any doubt.

Subsection (c)(17)—This limitation pertains only to “the rights under this [act] of” third parties” other than partners. Moreover, the limitation is subject to two major exceptions: Section 106 (pertaining to the partnership agreement’s relationship to the partnership itself and to persons becoming partners) and Section 107(b) (pertaining to the partnership agreement’s power over the rights of transferees).

Subsection (d)—The partnership agreement has plenipotentiary power over the matters

described in Subsection (a), except as specifically limited by Subsections (c) and (d)(3). However, for the convenience of practitioners and the courts, Paragraphs 1 and 2 list various terms often found in partnership agreements. No negative inference should be drawn about terms not listed; the listing is provided “without limiting other terms that may be included in a partnership agreement.”

Paragraph 3 lists arrangements subject to the “not manifestly unreasonable” standard. Subsection (e) delineates that standard. The same standard applies to terms of a partnership agreement which seek to “prescribe the standards . . . by which the performance of the [contractual] obligation [of good faith and fair dealing under Section 409(d)] is to be measured.” Subsection (c)(6).

Subsection (d)(1)(A)—An arrangement *not* involving “one or more disinterested and independent persons” acting “after full disclosure of all material facts” would “alter . . . the aspects of the duty of loyalty stated in Section 409(b)” and would therefore be subject to the “not manifestly unreasonable standard” of Subsection (d)(3)(A).

For the meaning of “material” as applied to information, see the comment to Section 409(f).

Subsection (d)(1)(B)—Section 405(a)(2) prohibits distributions by a limited liability partnership:

- *not merely* when, after the distribution, “the partnership’s total assets would be less than the sum of its total liabilities”;
- *but also* when, after the distribution, the assets would be less than the total liabilities “plus the amount that would be needed, if the partnership were to be dissolved and wound up at the time of the distribution, to satisfy the preferential rights upon dissolution and winding up of partners and transferees whose preferential rights are superior to the rights of persons receiving the distribution.”

The second part of the solvency test pertains to preferential rights to distributions, is thus a matter *inter se* the partners and any transferees, and is therefore subject to change in the partnership agreement.

In contrast, the first part of the solvency test protects third parties—creditors of the partnership—and therefore cannot be changed by the partnership agreement. Section 105(c)(17). Likewise, the partnership agreement cannot change the solvency test stated in Section 406(a)(1) (that “the partnership would not be able to pay its debts as they become due in the ordinary course of the partnership’s business”).

Subsection (d)(2)—The “not manifestly unreasonable” standard does not apply to partnership agreement provisions within this paragraph.

EXAMPLE: ABC Company (“ABC”) has three partners. ABC has two entirely separate

lines of business, the Alpha business and the Beta business. Under ABC's partnership agreement:

- Partner 1's responsibilities pertain exclusively to the Alpha business, while responsibility for:
 - the Beta business is allocated exclusively to Partner 2; and
 - ABC's overall operation is allocated exclusively to Partner 3.
- Partner 2's responsibilities pertain exclusively to the Beta business, while responsibility for:
 - the Alpha business is allocated exclusively to Partner 1; and
 - ABC's overall operation is allocated exclusively to Partner 3.
- Partner 1 has no fiduciary duties pertaining to the Beta business.
- Partner 2 has no fiduciary duties pertaining to the Alpha business.

The elimination of Partner 1's fiduciary duties with regard to the Beta business and Partner 2's fiduciary duties with regard to the Alpha business are enforceable, without regard to the "manifestly unreasonable" standard of Subsection (d)(3).

Section (d)(3)—This act rejects the ultra-contractarian notion that fiduciary duty within a business organization is merely a set of default rules and seeks instead to balance the virtues of "freedom of contract" against the dangers that inescapably exist when some persons have power over the interests of others.

Nonetheless, a properly drafted partnership agreement may substantially alter and even eliminate fiduciary duties. Two important limitations exist. First, arrangements subject to this subsection may not be "manifestly unreasonable." *See* Subsection (e) (delineating this standard).

Second, the partnership agreement may not transform the relationship *inter se* partners and the partnership into an entirely arm's length arrangement. For example, displacement of fiduciary duties is effective only to the extent that the displacement is stated clearly and with particularity. This rule is fundamental in the jurisprudence of fiduciary duty. *See, e.g., Paige Capital Mgmt., L.L.C. v. Lerner Master Fund, L.L.C.*, Civ. A. No. 5502-CS, 2011 WL 3505355, at *31 (Del. Ch. Aug. 8, 2011) (stating that, even under a statute that "permits the waiver of fiduciary duties . . . such waivers must be set forth clearly"); *Kelly v. Blum*, Civ. A. No. 4516-VCP, 2010 WL 629850, at *10 n.70 (Del. Ch. Feb. 24, 2010) ("Having been granted great contractual freedom by the LLC Act, drafters of or parties to an LLC agreement should be expected to provide . . . clear and unambiguous provisions when they desire to expand, restrict or eliminate the operation of traditional fiduciary duties"). It would therefore be manifestly unreasonable for a partnership agreement to negate this rule.

Although Subsection (d)(3) does not expressly address contracts between a partnership and a partner, the stated constraints must also apply to such contracts. If not, those constraints are effectively meaningless.

EXAMPLE: A general partnership enters into a management contract with its sole managing partner, and the contract provides that the duties of loyalty stated in Section

409(b) are entirely eliminated. If the partnership agreement were to so provide, the provision would be subject to the “manifestly unreasonable standard.” Section 105(d)(3)(A). Absent the authorization provided by Section 105(d)(3)(A), the management contract’s attempt to waive fiduciary duties may be unenforceable as a matter of public policy and contract law. *See Neubauer v. Goldfarb*, 108 Cal. App. 4th 47, 57, 133 Cal. Rptr. 2d 218 (2003) (stating that “waiver of corporate directors’ and majority shareholders’ fiduciary duties to minority shareholders in private close corporations is against public policy and a contract provision in a buy-sell agreement purporting to effect such a waiver is void”). If not, a court should hold the provision unenforceable nonetheless so as to avoid eviscerating Subsection (d)(3).

Subsection (d)(3)(A)—Subject to the “not manifestly unreasonable” standard, this paragraph empowers the partnership agreement to eliminate *all* aspects of the duty of loyalty listed in Section 409(b). The obligation of good faith and fair dealing, Section 409(d), would remain. *See* Subsection (c)(6). As to any other, uncoded aspects of the duty of loyalty, see Subsection (d)(3)(D) (empowering the partnership agreement to “alter or eliminate any other fiduciary duty”).

EXAMPLE: Joint Venture Partnership (“JV”) is a general partnership, with two partners, Kappa, Inc. (“Kappa”) and Lambda, LLC (“Lambda”). The partnership agreement provides that:

- JV is managed by a “board” consisting of one person appointed by Kappa and one person appointed by Lambda;
- each appointee:
 - owes fiduciary and any other duties exclusively to the partner that made the appointment; and
 - owes no duties to the other partner and the partnership.

The “not manifestly unreasonable” standard applies to these provisions under Subsection (d)(3)(A) and (D), and the provisions are not manifestly unreasonable. Note that the provisions do not affect the duties of Kappa and Lambda to each other.

Subsection (d)(3)(B)—Under this paragraph, a partnership agreement might provide that an affiliate of a partner will provide compensated services to the partnership at a price not exceeding market price, or that the partner may pursue opportunities that otherwise would be partnership opportunities. Such arrangements are commonplace and permissible.

Subsection (d)(3)(C)—In this context, “conduct” includes both acts and omissions. BLACK’S LAW DICTIONARY (9th ed. 2009) (defining conduct as “[p]ersonal behavior, whether by action or inaction”). Subject to the “not manifestly unreasonable” standard and the bedrock requirements stated here and in Subsection (c)(8), the partnership agreement can reduce the duty of care substantially. In particular, the partnership agreement can eliminate the aspects of the duty of care pertaining to gross negligence and recklessness.

This provision replicates in a particular context the general rule stated in Subsection (c)(8). For the meaning of “bad faith” in the context of the duty of care, see Subsection (c)(8), comment.

Subsection (e)—The “not manifestly unreasonable” concept became part of uniform business entity statutes when UPA (1997) imported the concept from the Uniform Commercial Code. (In the current version of the Uniform Commercial Code, the concept appears in Section 1-302(b).)

This subsection provides rules for applying the concept, specifying:

- who decides the issue of “manifestly unreasonable”
 - “the court . . . as a matter of law,” Subsection (e);
- the framework for determining the issue
 - determination to be made “in light of the purposes, activities, and affairs of the partnership,” Subsection (e)(2);
- the temporal setting for determining the issue
 - “[d]etermination [to be made] as of the time the challenged term became part of the partnership agreement,” Subsection (e)(1); and
- what information is admissible for determining the issue
 - “[o]nly circumstances existing” when “the challenged term became part of the partnership agreement,” Subsection (e)(1).

The subsection also provides a very demanding standard for persons claiming that a term of a partnership agreement is “manifestly unreasonable.” “The court . . . may invalidate the term only if, in light of the purposes, and business of the partnership, it is *readily apparent* that: (A) the objective of the term is unreasonable; or (B) the term is an unreasonable means to achieve the term’s objective.” Subsection (e)(2) (emphasis added).

Subsection (e) is fundamental to this act, because: (i) this act generally defers to the agreement among the partners; and (ii) Subsection (e) safeguards the partnership agreement in at least four ways:

- Determining manifest unreasonableness *inter se* owners of an organization is a different task than doing so in a commercial context, where concepts like “usages of trade” are available to inform the analysis. Each business organization must be understood in its own terms and context.
- If loosely applied, the concept of “manifestly unreasonable” would permit a court to rewrite the partners’ agreement, which would destroy the balance this act seeks to establish between freedom of contract and fiduciary duty.
- Case law has not adequately delineated the concept. *See, e.g., In re Brobeck, Phleger & Harrison L.L.P.*, 408 B.R. 318, 335 (Bankr. N.D. Cal. 2009) (“RUPA [UPA (1997)] does not define what is ‘manifestly unreasonable’ and the parties have not cited, nor can the court locate, a decision that defines the term. Absent case law or even a dictionary definition, the court must rely on its common sense to recognize something as manifestly unreasonable.”).
- In the context of statutes permitting stock transfer restrictions unless “manifestly unreasonable,” courts have often ignored the word “manifestly.” *See, e.g., Brandt v. Somerville*, 692 N.W.2d 144, 152 (N.D. 2005) (stating that “in close corporations, a majority of courts have sustained restrictions that are determined to be reasonable in light

of the relevant circumstances”); *Roof Depot, Inc. v. Ohman*, 638 N.W.2d 782, 786 (Minn. Ct. App. 2002) (stating that “the restrictions [on share transfer] are not ‘manifestly unreasonable’ because they are reasonable means to ensure that the management and control of the business remains in the group of investors or with people well known to them”); *Castriota v. Castriota*, 633 A.2d 1024, 1027–28 (N.J. App. Div. 1993) (“We are obliged to apply the statute in a manner consonant with its essential purpose to permit reasonable restrictions upon alienation.”).

Subsection (e)(1)—The significance of the phrase “as of the time the term as challenged became part of the partnership agreement” is best shown by example.

EXAMPLE: When a particular partnership comes into existence, its business plan is quite unusual and its success depends on the willingness of a particular individual to serve as the partnership’s sole managing partner. This individual has a rare combination of skills, experiences, and contacts, which are particularly appropriate for the partnership’s start-up. In order to induce the individual to accept the position of sole managing partner, the other partners are willing to have the partnership agreement significantly limit the managing partner’s fiduciary duties. Several years later, when the partnership’s operations have turned prosaic and the managing partner’s talents and background are not nearly so crucial, a partner challenges the fiduciary duty limitations as manifestly unreasonable. The relevant time under Subsection (e)(1) is when the partnership began. Subsequent developments are not relevant, except as they might inferentially bear on the circumstances in existence at the relevant time.

EXAMPLE: As initially adopted, a partnership agreement identifies a category of decisions ordinarily subject to the duty of loyalty and provides that “the managing partner’s sole, reasonable discretion” satisfies the duty. A year later, the agreement is amended to delete the word “reasonable.” Later, a partner claims that, without the word “reasonable,” the provision is manifestly unreasonable. The relevant time under Subsection (e)(1) is when the agreement was amended, not when the agreement was initially adopted.

Subsection (e)(2)—If a person claims that a term of the partnership agreement is manifestly unreasonable under Subsections (c)(6) or (d)(3), as a matter of ordinary procedural law the person making the claim has the burden of proof.

SECTION 106. PARTNERSHIP AGREEMENT; EFFECT ON PARTNERSHIP AND PERSON BECOMING PARTNER; PREFORMATION AGREEMENT.

(a) A partnership is bound by and may enforce the partnership agreement, whether or not the partnership has itself manifested assent to the agreement.

(b) A person that becomes a partner is deemed to assent to the partnership agreement.

(c) Two or more persons intending to become the initial partners of a partnership may

make an agreement providing that upon the formation of the partnership the agreement will become the partnership agreement.

Comment

Subsection (a)—This subsection resolves twin questions that have troubled some courts – namely, whether an unincorporated entity that has not signed its foundational agreement nonetheless is bound by and may enforce the agreement. The questions have been particularly troubling in the context of agreements to arbitrate. *See, e.g., Elkjer v. Scheef & Stone, L.L.P.*, 3:13-CV-1655-K, 2014 WL 1255844, at *5–6 (N.D. Tex. Mar. 27, 2014) (concluding that a limited liability partnership “is a party to the Partnership Agreement,” even though the partnership itself never signed or otherwise assented to the agreement; enforcing arbitration provision to the benefit of the LLP). *Contra Trover v. 419 OCR, Inc.*, 921 N.E.2d 1249, 1255 (2010) (finding that “neither FODG [an LLC] nor the Golf Club [a related LLC] was a party to the operating agreements and that they are therefore not bound by the arbitration clauses therein”).

Developments pertaining to the Virginia LLC Act further illustrate the difficulties. In *Mission Residential, L.L.C. v. Triple Net Properties, L.L.C.*, 654 S.E.2d 888, 891 (Va. 2008), the Virginia Supreme Court held that an LLC member’s derivative claim was not subject to the arbitration provision in the operating agreement, because: (i) the LLC was “the real party in interest”; (ii) the LLC had not signed the operating agreement; and (iii) requiring the claim to be arbitrated would “ignore[] the separate existence of Holdings [the LLC].” The Virginia legislature promptly disagreed and amended the LLC act to state: “A limited liability company is bound by its operating agreement whether or not the limited liability company executes the operating agreement.” 2009 VA. ACTS 763 (S.B. 1241), codified as VA. CODE ANN. § 13.1-1023.A.1 (2012). The legislature left open the question of a limited liability company’s power to enforce an operating agreement that the company has not executed.

This subsection answers the twin questions, categorically and in the affirmative.

This subsection does not consider whether a partnership is an indispensable party to a suit concerning the partnership agreement. That question is one of procedural law, and the answer can determine whether federal diversity jurisdiction exists.

Subsection (b)—Given the possibility of oral and implied-in-fact terms in the partnership agreement, a person becoming a partner of an existing partnership should take precautions to ascertain fully the contents of the partnership agreement. *See* Section 105(a)(3), cmt.

Subsection (c)—A pre-formation arrangement is not a partnership agreement. A partnership agreement is among “partners,” and, under this act, the earliest a person can become a partner is upon the formation of the partnership. *See* Section 402.

**SECTION 107. PARTNERSHIP AGREEMENT; EFFECT ON THIRD PARTIES
AND RELATIONSHIP TO RECORDS EFFECTIVE ON BEHALF OF PARTNERSHIP.**

(a) A partnership agreement may specify that its amendment requires the approval of a person that is not a party to the agreement or the satisfaction of a condition. An amendment is ineffective if its adoption does not include the required approval or satisfy the specified condition.

(b) The obligations of a partnership and its partners to a person in the person's capacity as a transferee or person dissociated as a partner are governed by the partnership agreement. Subject only to a court order issued under Section 504(b)(2) to effectuate a charging order, an amendment to the partnership agreement made after a person becomes a transferee or is dissociated as a partner:

(1) is effective with regard to any debt, obligation, or other liability of the partnership or its partners to the person in the person's capacity as a transferee or person dissociated as a partner; and

(2) is not effective to the extent the amendment:

(A) imposes a new debt, obligation, or other liability on the transferee or person dissociated as a partner; or

(B) prejudices the rights under Section 701 of a person that dissociated as a partner before the amendment was made.

(c) If a record delivered by a partnership to the [Secretary of State] for filing becomes effective and contains a provision that would be ineffective under Section 105(c) or (d)(3) if contained in the partnership agreement, the provision is ineffective in the record.

(d) Subject to subsection (c), if a record delivered by a partnership to the [Secretary of

State] for filing becomes effective and conflicts with a provision of the partnership agreement:

- (1) the agreement prevails as to partners, persons dissociated as partners, and transferees; and
- (2) the record prevails as to other persons to the extent they reasonably rely on the record.

Comment

Subsection (a)—This subsection, derived from Delaware Code Annotated title 6, § 18-302(e), permits the partnership agreement to: (i) accord a non-partner veto rights over amendments to the agreement; and (ii) establish other preconditions for amendments. An amendment made in derogation of a veto right or precondition is ineffective.

Veto rights are likely to be sought by lenders but may also be attractive to non-partner managers.

EXAMPLE: A non-partner manager enters into a management contract with a partnership, and that agreement provides in part that the partnership may remove the manager without cause only with the consent of partners holding two-thirds of the profits interests. The partnership agreement contains a parallel provision (the “quantum provision”), but the non-partner manager is not a party to the partnership agreement. Later, the partners amend the quantum provision to reduce the quantum to a simple majority of profits interests and thereafter purport to remove the manager without cause. Although the partnership has undoubtedly breached its contract with the manager and subjected itself to a damage claim, the partnership has the *power* under Section 105(a)(2) to effect the removal—unless the partnership agreement provides the manager a veto right over changes in the partnership agreement’s quantum provision.

This subsection does not refer to partner veto rights because, unless otherwise provided in the partnership agreement, the consent of each partner is necessary to effect an amendment. *See* Section 401(k).

Because “[a] partnership agreement may specify that its amendment requires . . . the satisfaction of a condition,” a partnership agreement can require that any amendment be made through a writing or a record signed by each partner. *See* Section 105(a)(3) (empowering the partnership agreement to determine “the means and conditions for amending the partnership agreement”).

Subsection (b)—The law of unincorporated business organizations is only beginning to grapple in a modern way with the tension between the rights of an organization’s owners to carry on their activities as they see fit (or have agreed) and the rights of transferees of the organization’s economic interests. If, as is often the situation, the partnership agreement

overrides Section 701 (Purchase of Interest of Person Dissociated as Partner), such transferees can include the heirs of the partnership's founders as well as former partners who, by agreement, are "locked in" as transferees of their own interests.

If the law categorically favors the owners, there is a serious risk of expropriation and other abuse. On the other hand, if the law grants former owners and other transferees the right to seek judicial protection, that specter can "freeze the deal" as of the moment an owner leaves the enterprise or a third party obtains an economic interest.

There is little case law in this area, and almost all of it pertains to limited rather than general partnerships. The case law clearly favors the remaining owners over former owners and other transferees. *See, e.g., Bauer v. Blomfield Co./Holden Joint Venture*, 849 P.2d 1365, 1367 n.2 (Alaska 1993) (holding that a mere assignee "was not entitled to complain about a decision made with the consent of all the partners" and stating "[w]e are unwilling to hold that partners owe a duty of good faith and fair dealing to assignees of a partner's interest"); *Bynum v. Frisby*, 311 P.2d 972, 975 (Nev. 1957) ("[A]n assignment of a partnership interest from one partner to a stranger does not bring that stranger into fiduciary relationship with the remaining partners nor require them to resort to dissolution in order to prevent such a relationship from arising. The stranger remains a stranger entitled only to share in the partnership's worth and to demand an accounting upon dissolution.") (applying UPA (1914) § 27, which pertains to rights of an assignee). *See generally* Daniel S. Kleinberger, *The Plight of the Bare Naked Assignee*, 42 SUFFOLK L. REV. 587 (2009).

This subsection follows *Bauer* and other cases by expressly subjecting transferees (including a person dissociated as a partner) to partnership agreement amendments made after the transfer or dissociation, except amendments that increase obligations on transferees. For example, an amendment might extend the duration of a partnership but may not institute a new capital call obligation on transferees.

The issue of whether, in extreme and sufficiently harsh circumstances, transferees might be able to claim some type of duty or obligation to protect against expropriation awaits development in the case law. An unreported LLC case suggests the answer might be yes, but the decision rests primarily on the wording of the LLC's operating agreement. In *Kohannim v. Katoli*, 08-11-00155-CV, 2013 WL 3943078, at *10-11 (Tex. App. July 24, 2013), the court: (i) noted that a limited liability company's "[r]egulations provide[] for the distribution of 'available cash' to members quarterly provided that the available cash is not needed for a reasonable working capital reserve"; (ii) also noted that "Jacob [the defendant member] paid himself \$100,000 for management services that were not performed and failed to make any profit distributions to Mike [former member and ex-spouse of the plaintiff Parvaneh] or Parvaneh [ex-spouse of Mike, who became Mike's transferee as part of their divorce proceeding] even though more than \$250,000 in undistributed profit had accumulated in the company's accounts since the mortgage on the property had been paid off in February 2007"; and (iii) concluded that "more than a scintilla of evidence supports the trial court's finding that Jacob failed to make profit distributions to Pavaneh." In essence, the court upheld a finding that Jacob had breached (or caused the partnership to breach) a contractual obligation to make distributions. But the court went further: "We also agree with the trial court's conclusion that the established facts

demonstrated Jacob engaged in wrongful conduct and exhibited a lack of fair dealing in the company's affairs to the prejudice of Parvaneh.” *Id.* at *11.

For the very limited statutory rights of transferees, see Section 503.

Subsection (b)(1)—This provision is inapposite when “a partner or transferee becomes entitled to receive a distribution.” Section 405(d). In that circumstance:

- “the partner or transferee has the status of . . . a creditor of the partnership with respect to the distribution,” *id.*; and
- the relevant obligation is not owed to “a person in the person’s capacity as a transferee or person dissociated as a partner,” Subsection (b), but rather to the person in the person’s capacity as a creditor.

Subsection (c)—This provision precludes using a filed record (*e.g.*, a statement of authority) to make an end run around the strictures of Section 105(c) and (d)(3).

Subsection (d)—It will be possible, albeit improvident, for a partnership agreement to be inconsistent with a public filing pertaining to the partnership. For those circumstances, this subsection provides rules for determining which source of information prevails.

- For partners and transferees, the partnership agreement is paramount.
- Third parties may invoke the public record upon a showing of reasonable reliance, which presupposes actual knowledge – *i.e.*, deemed knowledge under Section 103(d) does not suffice.

The mere fact that a term is present in a publicly filed record and not in the partnership agreement, or *vice versa*, does not automatically establish a conflict. This subsection does not expressly cover a situation in which: (i) one of the specified filed records contains information in addition to, but not inconsistent with, the partnership agreement, and (ii) a person, other than a partner or transferee, reasonably relies on the additional information. However, the policy reflected in this subsection seems equally applicable to that situation. Moreover, to argue that the partnership agreement prevails over the filed record is to argue that the additional term does conflict with the partnership agreement, at least in effect.

Section 105(a)(3) might also be relevant to the subject matter of this subsection. Absent a contrary provision in the partnership agreement, language in a record delivered to the filing office for filing on behalf of the partnership might be evidence of the partners’ agreement and might thereby constitute or at least imply a term of the partnership agreement.

This subsection does not apply to records delivered to the filing office for filing on behalf of persons other than a partnership.

SECTION 108. SIGNING OF RECORDS TO BE DELIVERED FOR FILING TO [SECRETARY OF STATE].

(a) A record delivered to the [Secretary of State] for filing pursuant to this [act] must be signed as follows:

(1) Except as otherwise provided in paragraphs (2) and (3), a record signed by a partnership must be signed by a person authorized by the partnership.

(2) A record filed on behalf of a dissolved partnership that has no partner must be signed by the person winding up the partnership's business under Section 802(c) or a person appointed under Section 802(d) to wind up the business.

(3) A statement of denial by a person under Section 304 must be signed by that person.

(4) Any other record delivered on behalf of a person to the [Secretary of State] for filing must be signed by that person.

(b) A record filed under this [act] may be signed by an agent. Whenever this [act] requires a particular individual to sign a record and the individual is deceased or incompetent, the record may be signed by a legal representative of the individual.

(c) A person that signs a record as an agent or legal representative affirms as a fact that the person is authorized to sign the record.

Comment

Subsection (a)—Section 102(20) defines “sign” broadly, including “an electronic symbol, sound, or process.”

Subsection (a)(1)—From the perspective of the filing office, it is not necessary that a partner sign a record delivered for filing on behalf of a partnership. The partnership agreement can impose such a requirement as an *inter se* matter, but the requirement would not affect this provision. *See* Section 105(c)(16)(B) (stating that the partnership agreement may not “vary any requirement, procedure, or other provision of this [act] pertaining to . . . the [Secretary of State],

including provisions pertaining to records authorized or required to be delivered to the [Secretary of State] for filing under this [act]”).

The filing office will not check whether a person who purports to be authorized to sign a record on behalf of a partnership actually has that authority, even if a statement of authority pertaining to the matter is in effect. Indeed, even if the filing office somehow “knows” of a statement limiting authority, the office lacks the authority to reject a record on that basis. *See* the comment to Section 117(a) (stating the requirements for filing and noting that the filing office’s review is ministerial and limited to information pertaining to the stated requirements), and the comment to Section 117(c) (explaining why such a statement of authority does not affect the filing office).

Subsection (b)—The filing office will not check the bona fides of a person purporting to have signed a record in a representative capacity. This subsection expressly authorizes taking action through an agent to provide context for Subsection (c) and for the avoidance of doubt. No negative inference should be drawn about using agents to take other action under this act.

Subsection (c)—As a matter of agency law, a person who signs in a representative capacity gives a “warranty of authority.” RESTATEMENT (THIRD) OF AGENCY § 6.10 (2006). This subsection has criminal law implications. Under Section 109(c), “[a]n individual who signs a record authorized or required to be filed under this [act] affirms under penalty of perjury that the information stated in the record is accurate.”

SECTION 109. LIABILITY FOR INACCURATE INFORMATION IN FILED RECORD.

(a) If a record delivered to the [Secretary of State] for filing under this [act] and filed by the [Secretary of State] contains inaccurate information, a person that suffers loss by reliance on the information may recover damages for the loss from:

(1) a person that signed the record, or caused another to sign it on the person’s behalf, and knew the information to be inaccurate at the time the record was signed; and

(2) subject to subsection (b), a partner if:

(A) the record was delivered for filing on behalf of the partnership; and

(B) the partner knew or had notice of the inaccuracy for a reasonably sufficient time before the information was relied upon so that, before the reliance, the partner reasonably could have:

(i) effected an amendment under Section 901(f);

(ii) filed a petition under Section 112; or

(iii) delivered to the [Secretary of State] for filing a statement of change under Section 909 or a statement of correction under Section 116.

(b) To the extent the partnership agreement expressly relieves a partner of responsibility for maintaining the accuracy of information contained in records delivered on behalf of the partnership to the [Secretary of State] for filing under this [act] and imposes that responsibility on one or more other partners, the liability stated in subsection (a)(2) applies to those other partners and not to the partner that the partnership agreement relieves of the responsibility.

(c) An individual who signs a record authorized or required to be filed under this [act] affirms under penalty of perjury that the information stated in the record is accurate.

Comment

Subsection (a)—This subsection relates to liability to third parties for inaccurate information in a filed record. Paragraph 1 requires actual knowledge because the paragraph can inculcate a person who is not a partner. Under Paragraph 2(B), notice suffices, because: (i) the provision applies only to partners; (ii) by status partners have overall management authority; and (iii) therefore, it is reasonable to impose liability when a partner either knows or “has reason to know . . . from all the facts known to the person at the time in question.” Section 103(b)(1) (defining notice). For the same reason, Paragraph 1 applies only to “information [known] to be inaccurate at the time the record was signed,” while Paragraph 2 applies whenever a “partner knew or had notice of the inaccuracy for a reasonably sufficient time before the information was relied upon so that, before the reliance, the partner reasonably could have [taken corrective action].” Paragraph (2)(B).

Subsection (a)(2)—Although this act establishes the avoidance of gross negligence as the standard of care for partners viz-a-viz the partnership, this subsection encompasses liability to third parties. Accordingly, the standard here is more demanding. The phrases “reasonably sufficient time” and “reasonably could have” indicate a standard of ordinary care. “[N]otice of the inaccuracy” involves “reason to know.” Section 103(b)(1).

Subsection (b)—Section 105(d)(2) authorizes the partnership agreement to establish an analogous rule *inter se* the partners. This subsection goes where the partnership agreement cannot reach and affects the rights of third parties.

Subsection (c)—This subsection provides criminal liability. The elements of perjury are a matter for the criminal law of the jurisdiction.

SECTION 110. APPLICATION TO EXISTING RELATIONSHIPS.

(a) Before [all-inclusive date], this [act] governs only:

(1) a partnership formed on or after [the effective date of this [act]]; and

(2) except as otherwise provided in subsection (c), a partnership formed before [the effective date of this [act]] which elects, in the manner provided in its partnership agreement or by law for amending the partnership agreement, to be subject to this [act].

(b) Except as otherwise provided in subsection (c), on and after [all-inclusive date] this [act] governs all partnerships.

(c) With respect to a partnership that elects pursuant to subsection (a)(2) to be subject to this [act], after the election takes effect the provisions of this [act] relating to the liability of the partnership's partners to third parties apply:

(1) before [all-inclusive date], to:

(A) a third party that had not done business with the partnership in the year before the election took effect; and

(B) a third party that had done business with the partnership in the year before the election took effect only if the third party knows or has been notified of the election; and

(2) on and after [all-inclusive date], to all third parties, but those provisions remain inapplicable to any obligation incurred while those provisions were inapplicable under paragraph (1)(B).

Legislative Note:

For states that have previously enacted UPA (1997): For these states this section is unnecessary. There is no need for a delayed effective date, even with regard to pre-existing

partnerships. (Presumably, the “linkage” issue [discussed below] was addressed when UPA (1997) was enacted.)

For states that have not previously enacted UPA (1997): Each enacting jurisdiction should consider whether: (i) this act makes material changes to the “default” (or “gap filler”) rules of the predecessor statute; and (ii) if so, whether Subsection (c) should carry forward any of those rules for pre-existing partnerships. In this assessment, the focus is on pre-existing partnerships that have left default rules in place, whether advisedly or not. The central question is whether, for such partnerships, expanding Subsection (c) is necessary to prevent material changes to the partners’ “deal.”

The “all-inclusive” date should be at least one year after the effective date of this act, Section 1206, but no more than two years.

The “linkage” issue—for states that still have ULPA (1976) or ULPA (1976/1985) in effect: These states should enact ULPA (2001) (Last Amended 2013) to take effect in conjunction with this act. If not, a state’s current limited partnership act must be amended to link to this act.

SECTION 111. DELIVERY OF RECORD.

(a) Except as otherwise provided in this [act], permissible means of delivery of a record include delivery by hand, mail, conventional commercial practice, and electronic transmission.

(b) Delivery to the [Secretary of State] is effective only when a record is received by the [Secretary of State].

Comment

Subsection (a)—Permissible means of delivery are not limited to those listed in this subsection, because this subsection by its terms is a non-exclusive list. Conventional commercial practice includes the use of private delivery or courier services. What constitutes conventional commercial practice may change over time.

Subsection (b)—This section lists permissible means of delivery but, except for delivery to the filing office, does not determine when delivery occurs. Delivery to the filing office is effective only upon actual receipt.

SECTION 112. SIGNING AND FILING PURSUANT TO JUDICIAL ORDER.

(a) If a person required by this [act] to sign a record or deliver a record to the [Secretary of State] for filing under this [act] does not do so, any other person that is aggrieved may petition [the appropriate court] to order:

- (1) the person to sign the record;
- (2) the person to deliver the record to the [Secretary of State] for filing; or
- (3) the [Secretary of State] to file the record unsigned.

(b) If a petitioner under subsection (a) is not the partnership or foreign limited liability partnership to which the record pertains, the petitioner shall make the partnership or foreign partnership a party to the action.

(c) A record filed under subsection (a)(3) is effective without being signed.

Comment

This section gives the court the flexibility to order either that a record be signed or that the record be filed by the filing office unsigned. The latter circumstance may arise; for example, in a situation where the person who should sign the record is not subject to the jurisdiction of the court. This section also makes clear that the court may order a person with control over a record that has been signed to deliver the record to the filing office for filing.

SECTION 113. FILING REQUIREMENTS.

(a) To be filed by the [Secretary of State] pursuant to this [act], a record must be received by the [Secretary of State], comply with this [act], and satisfy the following:

- (1) The filing of the record must be required or permitted by this [act].
- (2) The record must be physically delivered in written form unless and to the extent the [Secretary of State] permits electronic delivery of records.
- (3) The words in the record must be in English, and numbers must be in Arabic or Roman numerals, but the name of an entity need not be in English if written in English letters or Arabic or Roman numerals.
- (4) The record must be signed by a person authorized or required under this [act] to sign the record.
- (5) The record must state the name and capacity, if any, of each individual who

signed it, either on behalf of the individual or the person authorized or required to sign the record, but need not contain a seal, attestation, acknowledgment, or verification.

(b) If law other than this [act] prohibits the disclosure by the [Secretary of State] of information contained in a record delivered to the [Secretary of State] for filing, the [Secretary of State] shall file the record if the record otherwise complies with this [act] but may redact the information.

(c) When a record is delivered to the [Secretary of State] for filing, any fee required under this [act] and any fee, tax, interest, or penalty required to be paid under this [act] or law other than this [act] must be paid in a manner permitted by the [Secretary of State] or by that law.

(d) The [Secretary of State] may require that a record delivered in written form be accompanied by an identical or conformed copy.

(e) The [Secretary of State] may provide forms for filings required or permitted to be made by this [act], but, except as otherwise provided in subsection (f), their use is not required.

(f) The [Secretary of State] may require that a cover sheet for a filing be on a form prescribed by the [Secretary of State].

Comment

The filing office's duty under this section is ministerial, Section 117(a), and the office's assessment of a record delivered for filing is limited to conformity with this section. The filing office *must* file a record delivered for filing if the record contains the information required by this act and is accompanied by the required filing fee. The filing office is authorized to provide forms but not require their use, and, as a result, may not reject records delivered for filing on the basis of form (except to the very limited extent permitted by Subsections (d) and (f)).

In view of the very limited discretion granted to the filing office under this section and Section 117(a), “[t]he filing of . . . a record does not create a presumption that . . . the information contained in the record is correct” Section 117(e).

Subsection (a)—The first requisite for having a record filed is to cause the record actually to be received by the filing office. Section 111(b) reiterates this point.

Subsection (a)(2)—A record delivered for filing must be in typewritten or printed form unless the filing office permits delivery by electronic transmission. The types of electronic transmission that may be used will be determined by the filing office and is intended to include the evolving methods of electronic delivery, including facsimile transmissions, electronic transmissions between computers, and filings through delivery of storage media.

Subsection (a)(3)—The text of an entity filing must be in the English language, except to the limited extent permitted by this paragraph.

Subsection (a)(4)—To be filed a record must be signed by the appropriate person. See the definition of “sign” in Section 102(20) for a description of the manner in which a record may be “signed.” Who is an appropriate person is determined under Section 108, but the filing office will not check to determine whether a person purportedly authorized to sign is in fact authorized. *See* the comment to Section 108(a)–(c).

The requirement in some state statutes that records delivered for filing on behalf of an entity must be acknowledged or verified as a condition for filing has been rejected. These requirements serve little purpose in connection with entity filings. On the other hand, many organizations, like lenders or title companies, may desire that specific records include acknowledgements, verifications, or seals; Subsection (a)(4) does not prohibit the addition of these forms of execution and their use does not affect the eligibility of the record for filing.

Subsection (b)—Under this subsection, a confidentiality obligation does not affect the filing office’s duty to file, and the filing office is authorized but not required to redact. This act does not affect any confidentiality-related obligations the filing office may have under other law.

SECTION 114. EFFECTIVE DATE AND TIME. Except as otherwise provided in Section 115 and subject to Section 116(c), a record filed under this [act] is effective:

(1) on the date and at the time of its filing by the [Secretary of State], as provided in Section 117(b);

(2) on the date of filing and at the time specified in the record as its effective time, if later than the time under paragraph (1);

(3) at a specified delayed effective date and time, which may not be more than 90 days after the date of filing; or

(4) if a delayed effective date is specified, but no time is specified, at 12:01 a.m. on the date specified, which may not be more than 90 days after the date of filing.

Comment

Records accepted for filing become effective at the date and time of filing as recorded by the filing office, or at another specified time on that date, unless a permissible delayed effective date is stated in the record.

Section 117(b) requires the filing office to maintain some means of recording the date and time of delivery of a record and requires that office to record that date and time as the date and time of filing. That provision gives express statutory authority to the common practice of most filing offices of ignoring processing time and treating a record as filed as of the date and time it is delivered for filing even though it may not be reviewed and accepted for filing until several days after delivery. That section contemplates that time of delivery, as well as the date, will be routinely recorded.

Paragraph (1)—In the absence of provision for a delayed effective date, a record delivered for filing becomes effective on the date and time of filing by the filing office. Since under Section 117(b) the date and time of filing is the recorded date and time of delivery of the record to the filing office (which under Section 117(b) is the date and time of actual receipt), together these provisions eliminate any doubt about situations involving same-day transactions in which a record, for example, a statement of merger, is delivered for filing on the morning of the day the merger is to become effective.

Paragraph (3)—This paragraph does not authorize or contemplate the retroactive establishment of an effective date before the date of filing.

Paragraphs (3) and (4)—A record that states an effective date beyond the ninety-day limit is not a record that “satisfies this [act],” Section 117(a), and will properly be rejected by the filing office.

SECTION 115. WITHDRAWAL OF FILED RECORD BEFORE EFFECTIVENESS.

(a) Except as otherwise provided in Sections 1124, 1134, 1144, and 1154, a record delivered to the [Secretary of State] for filing may be withdrawn before it takes effect by delivering to the [Secretary of State] for filing a statement of withdrawal.

(b) A statement of withdrawal must:

(1) be signed by each person that signed the record being withdrawn, except as otherwise agreed by those persons;

(2) identify the record to be withdrawn; and

(3) if signed by fewer than all the persons that signed the record being withdrawn, state that the record is withdrawn in accordance with the agreement of all the persons that signed the record.

(c) On filing by the [Secretary of State] of a statement of withdrawal, the action or transaction evidenced by the original record does not take effect.

Comment

Only records that have not yet taken effect may be withdrawn under this section. If a record has taken effect, it may be corrected under Section 116 if the requirements of that section are satisfied. Otherwise, the record must be amended in accordance with this act.

Subsection (b)(1)—This provision is subject to Section 108(b) (“Whenever this [act] requires a particular individual to sign a record and the individual is deceased or incompetent, the record may be signed by a legal representative of the individual.”).

SECTION 116. CORRECTING FILED RECORD.

(a) A person on whose behalf a filed record was delivered to the [Secretary of State] for filing may correct the record if:

- (1) the record at the time of filing was inaccurate;
- (2) the record was defectively signed; or
- (3) the electronic transmission of the record to the [Secretary of State] was

defective.

(b) To correct a filed record, a person on whose behalf the record was delivered to the [Secretary of State] must deliver to the [Secretary of State] for filing a statement of correction.

(c) A statement of correction:

- (1) may not state a delayed effective date;
- (2) must be signed by the person correcting the filed record;
- (3) must identify the filed record to be corrected;
- (4) must specify the inaccuracy or defect to be corrected; and

(5) must correct the inaccuracy or defect.

(d) A statement of correction is effective as of the effective date of the filed record that it corrects except for purposes of Section 103(d) and as to persons relying on the uncorrected filed record and adversely affected by the correction. For those purposes and as to those persons, the statement of correction is effective when filed.

Comment

This section permits making corrections in filed records without re-submitting the entire record.

Subsection (a)(1) and (2)—A filed record may be corrected because it contains an inaccuracy or because it was defectively signed (including defects in optional forms of execution that do not affect the eligibility of the original record for filing).

Subsection (a)(3)—In addition, a filed record may be corrected if its electronic transmission was defective (*i.e.*, where an electronic delivery is made but, due to a defect in transmission, the filed record is later discovered to be inconsistent with the record intended to be filed). If no delivery is made because of a defect in transmission, a statement of correction may not be used to make a retroactive filing effective. Therefore, a partnership making an electronic delivery should take steps to confirm that the filing office receives the transmission.

Subsection (c)—A provision in a filed record setting an effective date may be corrected under this section, but the corrected effective date must comply with Section 114, which limits delayed effective dates to within ninety days after filing. A corrected effective date is thus measured from the date of the original filing of the record being corrected (*i.e.*, it cannot be before the date of filing of the record or more than ninety days thereafter).

Subsection (d)—The correction relates back to the original effective date of the record being corrected, except as to persons relying on the original entity filing and adversely affected by the correction. As to these persons, the effective date of the statement of correction is the date the statement is filed.

SECTION 117. DUTY OF [SECRETARY OF STATE] TO FILE; REVIEW OF REFUSAL TO FILE; DELIVERY OF RECORD BY [SECRETARY OF STATE].

(a) The [Secretary of State] shall file a record delivered to the [Secretary of State] for filing which satisfies this [act]. The duty of the [Secretary of State] under this section is ministerial.

(b) When the [Secretary of State] files a record, the [Secretary of State] shall record it as filed on the date and at the time of its delivery. After filing a record, the [Secretary of State] shall deliver to the person that submitted the record a copy of the record with an acknowledgment of the date and time of filing and, in the case of a statement of denial, also to the partnership to which the statement pertains.

(c) If the [Secretary of State] refuses to file a record, the [Secretary of State] shall, not later than [15] business days after the record is delivered:

(1) return the record or notify the person that submitted the record of the refusal;
and

(2) provide a brief explanation in a record of the reason for the refusal.

(d) If the [Secretary of State] refuses to file a record, the person that submitted the record may petition [the appropriate court] to compel filing of the record. The record and the explanation of the [Secretary of State] of the refusal to file must be attached to the petition. The court may decide the matter in a summary proceeding.

(e) The filing of or refusal to file a record does not:

(1) affect the validity or invalidity of the record in whole or in part; or
(2) create a presumption that the information contained in the record is correct or incorrect.

(f) Except as otherwise provided by Section 909 or by law other than this [act], the [Secretary of State] may deliver any record to a person by delivering it:

(1) in person to the person that submitted it;
(2) to the address of the person's registered agent;
(3) to the principal office of the person; or

(4) to another address the person provides to the [Secretary of State] for delivery.

Comment

Subsection (a)—Under this subsection the filing office is required to file a record if it “satisfies this [act].” The purpose of this language is to limit the discretion of the filing office to a ministerial role in reviewing the contents of records. If the record submitted is in the form prescribed, contains the information required by this act, and the appropriate filing fee is tendered, the filing office must file the record. Consistent with this approach, this subsection states explicitly that the filing duty of the filing office is ministerial. *See* Subsection (e) (pertaining to presumptions not created).

Subsection (b)—This subsection provides that when the filing office files a record, the filing office records it as filed on the date and time of delivery to the filing office, retains the original record for the office’s records, and delivers a copy of the record to the person who delivered the record for filing with an acknowledgement of the date and time of filing. In the case of a statement of denial, Section 304, the filing office will also send a copy of the record and acknowledgment to the partnership.

In the case of a record transmitted electronically to the filing office that office may deliver by electronic transmission. The copy returned will be the exact or conformed copy if the filing office has required one, or will be a copy made by the filing office if an exact or conformed copy was not required.

Under this subsection the acceptance of a filing is evidenced merely by the filing office’s delivery of a copy of the record with an acknowledgment of the date and time of filing. The act does not provide for the filing office to issue a formal certificate of filing. A copy of the filed record together with an acknowledgment of the date and time of filing should sufficiently indicate that the filing has been accepted for filing and been filed.

Subsection (c)—Because of the simplification of formal filing requirements and the limited discretion granted to the filing office by this act, it is probable that rejection of records delivered to the filing office for filing will occur only rarely. This subsection provides that if the filing office does reject a record delivered for filing, the filing office must return the record to the person that submitted the filing within fifteen days together with a brief written explanation of the reason for rejection. In the case of a record delivered by electronic transmission, rejection of the record may be made electronically by the filing office or by a mailing to the person that submitted the record.

Subsection (e)—This subsection provides that the filing of a record by the filing office does not affect the validity or invalidity of any provision contained in the record and does not create any presumption with respect to any information in the record. Likewise, the refusal of the filing office to file a record creates no presumption that any of the information in the record is incorrect. Persons adversely affected by a statement in a filed record may contest the statement in a proceeding appropriate for that purpose, including a damage action under Section 109.

SECTION 118. RESERVATION OF POWER TO AMEND OR REPEAL. The

[legislature of this state] has power to amend or repeal all or part of this [act] at any time, and all limited liability partnerships and foreign limited liability partnerships subject to this [act] are governed by the amendment or repeal.

Comment

Provisions similar to this section have their genesis in *Trustees of Dartmouth College v. Woodward*, 17 U.S. (4 Wheat) 518 (1819), which held that the United States Constitution prohibited the application of newly enacted statutes to existing corporations while suggesting the efficacy of a reservation of power similar to this section. This section is a generalized form of the type of provision found in many entity organic laws, the purpose of which is to avoid any possible argument that an entity has contractual or vested rights in any specific statutory provision of its organic law and to ensure that the state may in the future modify its entity statutes as it deems appropriate and require existing entities to comply with the statutes as modified.

This section applies to changes in mandatory provisions of this act; the section does not pertain to changes in default rules.

EXAMPLE: Having enacted this act, State A later amends Section 402(b)(3) (affirmative vote or consent of all partners required for a person to become a partner) to reduce, as a default rule, the necessary quantum of consent to consent from partners owning in the aggregate at least two-third of the interests in current profits owned by partners at the time of the consent. XYZ is a partnership formed under State A's act before the amendment. XYZ's partnership agreement is silent on this issue, leaving in place the act's default rule. Whether the act's amended default rule applies depends on whether the partners initially: (i) agreed (whether expressly or implicitly) to accept the then-applicable default rule requiring unanimous consent; (ii) agreed (whether expressly or implicitly) to adopt whatever rule the act provided; or (iii) never considered the issue. In short, the change in a default rule occasions an inquiry into the partners' express or implied agreement as to the role of the default rule in their mutual understanding. In the first instance, the old rule would continue in effect. In the second and third instances, the new rule would apply.

SECTION 119. SUPPLEMENTAL PRINCIPLES OF LAW. Unless displaced by particular provisions of this [act], the principles of law and equity supplement this [act].

Comment

For this act, the common law rules of contract and agency are among the most important supplemental "principles of law." With regard to transactions under Article 11, noteworthy

principles include the rights of creditors following leveraged buyouts, spinoffs, asset purchases, or other similar transactions; and creditors' rights under other laws.

[ARTICLE] 2

NATURE OF PARTNERSHIP

SECTION 201. PARTNERSHIP AS ENTITY.

(a) A partnership is an entity distinct from its partners.

(b) A partnership is the same entity regardless of whether the partnership has a statement of qualification in effect under Section 901.

Comment

Subsection (a)—The law of general partnerships long struggled with the question of whether a partnership is merely an aggregate of its partners or an entity distinct from its partners.

The common law took the aggregate approach. *X-L Liquors v. Taylor*, 111 A.2d 753, 759 (1955) (stating that “the common law did not recognize the separate existence of partnerships”); *Watson v. G.C. Associates Ltd. P'ship*, 691 P.2d 417, 418 (1984) (referring to the “common law or aggregate theory of partnership”); *McKinney v. Truck Ins. Exch.*, 324 S.W.2d 773, 776 (Mo. Ct. App. 1959) (referring to “the aggregate or common-law theory as to partnerships”).

Under UPA (1914), a general partnership had both entity and aggregate characteristics, in part because that act's first reporter, who died during the lengthy drafting process, strongly favored the entity approach, while his replacement just as strongly favored the aggregate construct. *New England Herald Dev. Grp. v. Town of Falmouth*, 521 A.2d 693, 697 (Me. 1987) (“The draftsmen of the uniform act were divided over what effect it should have on the common law [aggregate] rule The result is the Act contains language that supports application of either [the entity or aggregate] theory.”).

According to the comment to this section, UPA (1997) “embrace[d] the entity theory of the partnership,” characterized “the entity theory as the dominant model” for the act, and highlighted a key problem arising from the aggregate aspect of UPA (1914)—namely, “the necessity of a deed to convey title from the ‘old’ partnership to the ‘new’ partnership every time there is a change of cast among the partners.” Under UPA (1997), “there [was] no ‘new’ partnership just because of membership changes,” thereby “avoid[ing] the result in cases such as *Fairway Development Co. v. Title Insurance Co.*, 621 F. Supp. 120 (N.D. Ohio 1985), which held that the ‘new’ partnership resulting from a partner’s death did not have standing to enforce a title insurance policy issued to the ‘old’ partnership.”

The Harmonization process made no changes to this aspect of UPA (1997). Note, however, that UPA (1997) retained several aspects of the aggregate construct: (i) joint and

several liability of the partners for the obligations of a partnership that is not an LLP, Section 306(a); (ii) the concept of a partnership at-will, under which dissociation of any partner by “express will” dissolves the partnership, Section 801(1); and (iii) the susceptibility to dissolution of a partnership for a term or undertaking following the dissociation of a person as a partner. Section 801(2). Those vestiges continue under the Harmonization amendments adopted in 2011 and 2013.

Subsection (b)—Neither becoming nor ceasing to be a limited liability partnership affects a partnership’s entity status. These changes merely add or subtract a characteristic. *Compare* Section 201(b), *with* Section 1146(a)(1) (stating that “[w]hen a conversion becomes effective [] (1) the converted entity is: (A) organized under and subject to the organic law of the converted entity [and therefore a different type of entity]; and (B) the same entity without interruption as the converting entity”).

SECTION 202. FORMATION OF PARTNERSHIP.

(a) Except as otherwise provided in subsection (b), the association of two or more persons to carry on as co-owners a business for profit forms a partnership, whether or not the persons intend to form a partnership.

(b) An association formed under a statute other than this [act], a predecessor statute, or a comparable statute of another jurisdiction is not a partnership under this [act].

(c) In determining whether a partnership is formed, the following rules apply:

(1) Joint tenancy, tenancy in common, tenancy by the entireties, joint property, common property, or part ownership does not by itself establish a partnership, even if the co-owners share profits made by the use of the property.

(2) The sharing of gross returns does not by itself establish a partnership, even if the persons sharing them have a joint or common right or interest in property from which the returns are derived.

(3) A person who receives a share of the profits of a business is presumed to be a partner in the business, unless the profits were received in payment:

(A) of a debt by installments or otherwise;

(B) for services as an independent contractor or of wages or other compensation to an employee;

(C) of rent;

(D) of an annuity or other retirement or health benefit to a deceased or retired partner or a beneficiary, representative, or designee of a deceased or retired partner;

(E) of interest or other charge on a loan, even if the amount of payment varies with the profits of the business, including a direct or indirect present or future ownership of the collateral, or rights to income, proceeds, or increase in value derived from the collateral; or

(F) for the sale of the goodwill of a business or other property by installments or otherwise.

Comment

UPA (1997) § 202 combined UPA (1914) §§ 6 and 7, recasting the “definition” of a partnership in UPA (1914) § 6(1) “as an operative rule of law – *i.e.*, “[a] partnership is an association of two or more persons . . .” became “the association of two or more persons . . . forms.” The change was stylistic and made no substantive change in the law. The Harmonization Project made no substantive change to this section, except to clarify that this act is not linked to the uniform limited partnership act. *See* Subsection (b), cmt.

The addition of the phrase, “whether or not the persons intend to form a partnership,” merely codifies the universal judicial construction of UPA (1914) § 6(1) that a partnership is created by the association of persons whose intent is to carry on as co-owners a business for profit, regardless of their subjective intention to be “partners.” Indeed, they may inadvertently create a partnership despite their expressed subjective intention not to do so. The language of Section 202 alerts readers to this possibility.

Subsection (a)—Consistent with the common law and UPA (1914), under this act “co-ownership” is a key concept. Ownership involves the power of ultimate control (albeit a power that can be substantially diminished by agreement) and a right to share in the profits of the co-owned business. To state that partners are co-owners of a business is to state that: (i) they share in the profits (if any) of the enterprise; and (ii) *ab initio* at least, they collectively have the power of ultimate control. Consequently:

- mere passive co-ownership of property, as distinguished from using the property to carry on a business, does not establish a partnership, Subsection (c)(1); and

- merely sharing gross revenues is likewise insufficient, Subsection (c)(2).

UPA (1997) added, “whether or not the persons intend to form a partnership” to the UPA (1914) formulation, thereby codifying a rule uniformly applied by courts: Subjective intent to create the legal relationship of “partnership” is irrelevant. What matters is the intent *vel non* to establish the business relationship that the law labels a “partnership.” Thus, a disclaimer of partnership status is ineffective to the extent the parties’ intended arrangements meet the criteria stated in this subsection.

Subsection (b)—This subsection continues the UPA (1914) concept that the general partnership is the residual form of business association. Accordingly, partnership-like organizations formed under specially applicable statutes are not within this act. *E.g.*, MONT. CODE ANN. §§ 35-13-101 to 102 (pertaining to mining partnerships).

An arrangement labeled a “joint venture” is a partnership if the arrangement meets the criteria stated in Subsection (a). In fact, in many jurisdictions, the law of general partnerships applies almost without analysis to joint ventures in which the co-venturers share profits. *See Jonathan Woodner Co. v. Laufer*, 531 A.2d 280, 285 n.7 (D.C. 1987) (stating that: (i) “[s]trictly speaking, a joint venture is not the same as a partnership, but there is ‘very little law . . . applicable to one that does not apply to the other’”; (ii) “the rights and liabilities of joint venturers among themselves are generally governed by the laws of partnership”; and (iii) “[p]rinciples of partnership law, in particular the Uniform Partnership act, apply in most instances to joint ventures”) (quoting 46 AM. JUR. 2D JOINT VENTURES § 4, at 25 (1969) and collecting cases).

A limited partnership is not a partnership under this act; a limited partnership is “formed under a statute other than this [act]” (*i.e.*, ULPA (2001) (Last Amended 2013) § 201). Moreover, ULPA (2001) delinked the uniform limited partnership act from the uniform general partnership act. *See* ULPA (2001) (Last Amended 2013) Prefatory Note, *The Decision to “De-Link” and Create a Stand Alone Act*.

An unincorporated nonprofit organization is not a partnership under this act, because the organization is limited to “nonprofit purposes” and therefore cannot “carry on a business” in the traditional sense of that concept. *See* UUNA (2008) (Last Amended 2013) § 102(11) (defining “unincorporated nonprofit association”).

Subsection (c)—UPA (1997) derived this subsection from UPA (1914) § 7 and with one exception, made no substantive change to the law. The substantive change pertains to the sharing of profits, which UPA (1997) recast as creating a rebuttable presumption of partnership rather than merely constituting *prima facie* evidence. “*Prima facie*” means that the party with the burden of proof has adduced sufficient evidence to carry that burden, subject to the finder of fact’s view of any contrary evidence. The burden of persuasion is unchanged. In contrast, “rebuttable presumption” switches the burden of persuasion.

Subsection (c)(3)—The protected categories listed in this paragraph apply regardless of whether the profit share is a single, unvarying percentage or a ratio that varies; for example, after

reaching a dollar floor or different levels of profits. Like UPA (1914), this act makes no attempt to answer in every case whether a partnership is formed. Whether a relationship is more properly characterized as that of borrower and lender, employer and employee, or landlord and tenant is left to the trier of fact. As under UPA (1914), a person may function in both partner and non-partner capacities.

Subsection (c)(3)(E)—UPA (1997) added this protected category, excepting from the rebuttable presumption a share of the profits received in payment of interest or other charges on a loan, “including a direct or indirect present or future ownership in the collateral, or rights to income, proceeds, or increase in value derived from the collateral.” The quoted language was taken from Section 211 of the Uniform Land Security Interest Act and is intended to protect shared-appreciation mortgages, contingent or other variable or performance-related mortgages, and other equity participation arrangements by clarifying that contingent payments do not presumptively convert lending arrangements into partnerships.

SECTION 203. PARTNERSHIP PROPERTY. Property acquired by a partnership is property of the partnership and not of the partners individually.

Comment

Although phrased differently, this section, which originated in UPA (1997), produces the same result as do UPA (1914) §§ 8(1) and 25. All property acquired by a partnership, by whatever manner acquired, becomes partnership property and belongs to the partnership as an entity, rather than to the individual partners.

Section 204 provides guidance concerning when property is “acquired by” the partnership.

UPA (1914) § 25(2)(c) and (e) also provides that partnership property is not subject to exemptions, allowances, or rights of a partner’s spouse, heirs, or next of kin. UPA (1997) omitted those provisions as unnecessary, because the exemptions and rights inure to the property of the partners, and not to partnership property.

SECTION 204. WHEN PROPERTY IS PARTNERSHIP PROPERTY.

(a) Property is partnership property if acquired in the name of:

(1) the partnership; or

(2) one or more partners with an indication in the instrument transferring title to

the property of the person’s capacity as a partner or of the existence of a partnership but without an indication of the name of the partnership.

(b) Property is acquired in the name of the partnership by a transfer to:

(1) the partnership in its name; or

(2) one or more partners in their capacity as partners in the partnership, if the name of the partnership is indicated in the instrument transferring title to the property.

(c) Property is presumed to be partnership property if purchased with partnership assets, even if not acquired in the name of the partnership or of one or more partners with an indication in the instrument transferring title to the property of the person's capacity as a partner or of the existence of a partnership.

(d) Property acquired in the name of one or more of the partners, without an indication in the instrument transferring title to the property of the person's capacity as a partner or of the existence of a partnership and without use of partnership assets, is presumed to be separate property, even if used for partnership purposes.

Comment

Section 204 states the rules *inter se the partners and partnership* for determining when property is acquired by the partnership and so becomes partnership property. These rules apply to "all property, whether real, personal, or mixed or tangible or intangible, or any right or interest therein." Section 102(16) (defining "property").

These rules provide three separate approaches—according to:

- the name or names used in acquiring the property;
- when a partner's name appears as a transferee, the capacity in which the partner is acting; and
- for property acquired by purchase, whether the partnership provided the consideration for the property.

These approaches are complementary, not mutually exclusive.

This section omits any provision corresponding to UPA (1914) § 8(4), which states: "A conveyance to a partnership in the partnership name, even without words of inheritance, passes the entire estate of the grantor unless a contrary intent appears." UPA (1997) omitted the provision as unnecessary because under modern conveyancing law all transfers pass the entire estate or interest of the grantor unless a contrary intent appears.

To what extent this section's *inter se* rules affect third party rights is a matter for other law, but in any event these rules yield automatically to statutes providing record title for particular types of property. For an example, see Subsection (c), comment.

Subsection (a) and (b)—These subsections act in combination to provide the first two of the approaches listed above. Under these subsections, property becomes partnership property if acquired:

- in the name of the partnership; or
- in the name of one or more of the partners with an indication in the instrument transferring title of either:
 - their capacity as partners; or
 - of the existence of a partnership, even if the name of the partnership is not indicated.

Property acquired “in the name of the partnership” includes property acquired in the name of one or more partners in their capacity as partners, but only if the name of the partnership is indicated in the instrument transferring title.

Property transferred to a partner is partnership property, even though the name of the partnership is not indicated, if the instrument transferring title indicates either: (i) the partner's capacity as a partner; or (ii) the existence of a partnership. This approach is consonant with the entity theory of partnership and resolves the troublesome issue of a conveyance to fewer than all the partners but that nevertheless indicates their partner status.

Subsections (c) and (d)—At least *inter se* the partners and partnership, it is the intention of the partners that controls whether property belongs to the partnership or to one or more of the partners in their individual capacities. These subsections each contain a rebuttable presumption as to the partners' intent.

When applicable, the presumptions switch the burden of persuasion but are subject to an important limitation in favor of third parties. *See* Section 302(a)(3) (“Partnership property held in the name of one or more persons other than the partnership, without an indication in the instrument transferring the property to them of their capacity as partners or of the existence of a partnership, may be transferred by an instrument of transfer executed signed by the persons in whose name the property is held.”).

Subsection (c)—Under this subsection, property purchased with partnership property is presumed to be partnership property, notwithstanding the name in which title is held or any other indicia. In this context, a promise made by a partnership in exchange for property triggers the presumption, including a promise to perform services or to guarantee another person's obligation with regard to the purchase of the property.

The presumption is entirely ineffective against third parties with regard to property with record title.

EXAMPLE: Using partnership funds, a partner purchases realty in the partner's own name and records the purchase in the appropriate land records. The partner later transfers title to the realty to a third party that has neither knowledge nor notice of any rights the partnership may have in the property. The relevant real estate statute is the applicable law; this subsection is entirely inapposite.

Subsection (d)—Under this subsection, property acquired in the name of one or more of the partners, without an indication of their capacity as partners and without use of partnership funds or credit, is presumed to be the partners' separate property, even if used for partnership purposes. In effect, this subsection presumes that only the use of the property is contributed to the partnership.

[ARTICLE] 3

RELATIONS OF PARTNERS TO PERSONS DEALING WITH PARTNERSHIP

SECTION 301. PARTNER AGENT OF PARTNERSHIP. Subject to the effect of a statement of partnership authority under Section 303, the following rules apply:

(1) Each partner is an agent of the partnership for the purpose of its business. An act of a partner, including the signing of an instrument in the partnership name, for apparently carrying on in the ordinary course the partnership business or business of the kind carried on by the partnership binds the partnership, unless the partner did not have authority to act for the partnership in the particular matter and the person with which the partner was dealing knew or had notice that the partner lacked authority.

(2) An act of a partner which is not apparently for carrying on in the ordinary course the partnership's business or business of the kind carried on by the partnership binds the partnership only if the act was actually authorized by all the other partners.

Comment

At common law, a general partner was considered a general agent of the partnership. Joseph Story, COMMENTARIES ON THE LAW ON PARTNERSHIP § 101, at 153 (2d ed. 1850); RESTATEMENT (SECOND) OF AGENCY § 14A, cmt. a (1958). The mere status of a general partner "clothes" a person with apparent authority to carry on the partnership business. *Stockwell v. U.S.*, 80 U.S. 531, 567 (1871); *Lincoln Nat'l Bank v. Schoen*, 56 Mo. App. 160, 164 (Mo. Ct. App. 1894); *Kansallis Fin. Ltd. v. Fern*, 659 N.E.2d 731, 733, 740 (Mass. 1996). In 1914, the UPA

codified this principle, UPA (1914) § 9, and “statutory apparent authority” has been part of uniform partnerships acts ever since. *See* UPA (1997) § 301 (1997) (Partnership Agent of Partnership); ULPA (2001) § 402 (General Partner Agent of Limited Partnership).

This section’s principal purpose is to delineate a partner’s statutory apparent authority. The partnership agreement and Section 401 govern the rights of the partners among themselves, including the right to restrict a partner’s actual authority.

Section 301(1)—This paragraph retains the basic principles reflected in UPA (1914) § 9(1) and in effect characterizes a partner as a general managerial agent. Such agents have both actual and apparent authority, and this section delineates the apparent authority. For a discussion of the scope of actual authority, see Section 401(h), comment.

The agency law origins of statutory apparent authority has informed courts’ application of UPA (1914) § 9(1), and that case law is equally applicable under this act. For example, although the statutory language does not appear to require that the appearance of authority be reasonable, the case law does so routinely. *See, e.g., In re Fox Hill Office Invs., Ltd.*, 101 B.R. 1007, 1019 (Bankr. W.D. Mo. 1989) (stating a third-party lender in possession of a copy of a limited partnership’s partnership agreement was on notice of the general partner’s lack of authority and therefore should have inquired as to the partner’s authority), *aff’d*, 926 F.2d 752 (8th Cir. 1991); *Investors Title Ins. Co. v. Herzig*, 360 S.E.2d 786, 789 (N.C. 1987) (stating that “in order to hold the [partnership] liable, [a third party] must show that in the exercise of reasonable care under the circumstances, it was justified in believing that the principal had conferred . . . authority to [act] on behalf of the partnership”); *First Interstate Bank of Oregon, N.A. v. Bergendahl*, 723 P.2d 1005, 1010 (Or. Ct. App. 1986) (stating that bank in possession of management agreement was on notice of general partner’s restricted authority and could not rely on a theory of apparent authority).

Likewise, per the law of apparent authority, a partner can bind a partnership under this section even if the partner intends to take and does take the resulting benefits for the partner’s own benefit. *See Wolfe v. Harms*, 413 S.W.2d 204, 216 (Mo. 1967) (stating that partnership is liable for partner’s acts “even if the predominant motive of the partner was to benefit himself or third persons”); *Rouse v. Pollard*, 18 A.2d 5, 7 (N.J. Eq. 1941) (“All the partners are responsible for the act of one of their number as agent, even though he acts for some secret purpose of his own, and not really for the benefit of the [partnership].”), *aff’d*, 21 A.2d 801 (N.J. Eq. 1941); *Investors Title Ins. Co. v. Herzig*, 360 S.E.2d 786, 788 (N.C. 1987) (stating that the mere fact that the partner’s act was for personal gain was not enough to justify summary judgment for the partnership on the subject of the partnership’s liability for the act).

UPA (1997) § 301(1) effected three changes from UPA (1914) § 9(1). First, Section 301(1) clarified that a partner’s apparent authority includes acts for carrying on in the ordinary course “business of the kind carried on by the partnership,” not just the business of the particular partnership in question. UPA (1914) is ambiguous on this point, but the drafters of UPA (1997) found some authority for an expanded construction in accordance with the so-called English rule. *See, e.g., Burns v. Gonzalez*, 439 S.W.2d 128, 131 (Tex. Civ. App. 1969) (dictum); *Comm’l Hotel v. Weeks*, 254 S.W. 521 (Tex. Civ. App. 1923).

The Harmonization Project preserved this UPA (1997) change, the significance of which depends on how broadly courts construe “business of the kind carried on by the partnership.” For example, does a partnership that acts as a grain broker (never taking a position in grain) do business “of the kind carried on” by a partnership that buys grain for resale?

Second, UPA (1997) used “carrying on in the ordinary course” in lieu of the UPA (1914) phrase “in the usual way.” The 1997 comments stated that: (i) “[t]he UPA and the case law use both terms without apparent distinction”; and (ii) “[n]o substantive change [was] intended by use of the more customary phrase.”

The change in language had the benefit of aligning Section 301(1) with Section 305 (establishing attribution rules for a partner’s wrongful conduct and referring to “ordinary course of business of the partnership” and “the ordinary course of the partnership’s business”). The Harmonization Project also preserved this UPA (1997) change. For a discussion of the relationship between the ordinary course of the partnership’s business and a partner’s ordinary duties, see Section 305(a), comment.

UPA (1997)’s third change to UPA (1914) § 9(1) concerned the allocation of risk of a partner’s lack of authority. Under UPA (1914) § 9(1) and (4), a restriction on a partner’s authority binds only a person with knowledge of the restriction. In contrast, UPA (1997) § 301(1) provides that a person who has received a notification of a restriction is also bound. Thus, UPA (1997) shifted the risk of lack of authority somewhat away from the partnership and somewhat toward third parties dealing with partners.

The Harmonization Project shifted the risk a bit further, binding third parties who know or *have reason to know* of a restriction. Section 301(1). (However, it is arguable that the Harmonization Project merely made explicit a rule implicit in the case law. As noted above, the case law requires a third party to show a *reasonable* belief in the partner’s authority. A third party who has reason to know of a partner’s lack of authority will be hard pressed to make that showing.)

Statements of partnership authority, Section 303, affect the application of this paragraph only in two ways. First, under Section 303(e) all persons (other than partners) are deemed to know of a limitation on the authority of a partner to transfer real property contained in a statement recorded in the appropriate land records. Second, a person (other than a partner) with actual knowledge of a grant or limitation of a partner’s authority may rely on that knowledge.

Section 301(2)—UPA (1997) drew this paragraph directly from UPA (1914) § 9(2), with conforming changes to mirror the new language of Paragraph (1). Consistent with the law of agency, a partnership is bound by a partner’s actual authority, even if the partner lacks apparent authority. Under general agency principles, a partnership can subsequently ratify a partner’s unauthorized act. *See* Section 119.

UPA (1914) § 9(3) and (4)—UPA (1997) omitted UPA (1914) § 9(3), which lists five acts requiring unanimous consent of the partners to bind the partnership. Most of the listed acts probably remain outside the apparent authority of a partner under this act, such as disposing of

the goodwill of the business, but the drafters of UPA (1997) believed that eliminating categorical rules affords useful flexibility. In particular, it seemed “archaic to always require unanimous consent to submit a partnership claim to arbitration.” UPA (1997) § 301, cmt.

UPA (1914) § 9(4) provides that a partnership is not bound by an act of a partner in contravention of a restriction on a partner’s authority known to the other party. UPA (1997) omitted that provision as being entirely redundant of UPA (1997) § 301(1).

The Harmonization Project preserved UPA (1997)’s approach to both UPA (1914) § 9(3) and (4).

SECTION 302. TRANSFER OF PARTNERSHIP PROPERTY.

(a) Partnership property may be transferred as follows:

(1) Subject to the effect of a statement of partnership authority under Section 303, partnership property held in the name of the partnership may be transferred by an instrument of transfer signed by a partner in the partnership name.

(2) Partnership property held in the name of one or more partners with an indication in the instrument transferring the property to them of their capacity as partners or of the existence of a partnership, but without an indication of the name of the partnership, may be transferred by an instrument of transfer signed by the persons in whose name the property is held.

(3) Partnership property held in the name of one or more persons other than the partnership, without an indication in the instrument transferring the property to them of their capacity as partners or of the existence of a partnership, may be transferred by an instrument of transfer signed by the persons in whose name the property is held.

(b) A partnership may recover partnership property from a transferee only if it proves that signing of the instrument of initial transfer did not bind the partnership under Section 301 and:

(1) as to a subsequent transferee who gave value for property transferred under subsection (a)(1) and (2), proves that the subsequent transferee knew or had been notified that

the person who signed the instrument of initial transfer lacked authority to bind the partnership;
or

(2) as to a transferee who gave value for property transferred under subsection (a)(3), proves that the transferee knew or had been notified that the property was partnership property and that the person who signed the instrument of initial transfer lacked authority to bind the partnership.

(c) A partnership may not recover partnership property from a subsequent transferee if the partnership would not have been entitled to recover the property, under subsection (b), from any earlier transferee of the property.

(d) If a person holds all the partners' interests in the partnership, all the partnership property vests in that person. The person may sign a record in the name of the partnership to evidence vesting of the property in that person and may file or record the record.

Comment

UPA (1997) § 302 replaced UPA (1914) §10 and provides rules for the transfer and recovery of partnership property. While UPA (1914) § 10 covers only real property, this section applies also to personal property acquired by instrument and held in the name of the partnership or one or more of the partners.

The language of this section was adapted in part from the Georgia partnership statute in effect during the UPA (1997) drafting process. *See* GA. CODE ANN. § 14-8-10. Rules stated in this section necessarily parallel the rules stated in Section 203.

Subsection (a)—Subsection (a)(1) deals with the transfer of partnership property held in the name of the partnership and Subsection (a)(2) deals with property held in the name of one or more of the partners with an indication either of their capacity as partners or of the existence of a partnership. Subsection (a)(3) deals with partnership property held in the name of one or more of the partners without an indication of their capacity as partners or of the existence of a partnership. Like Section 301, Subsection (a)(1) is subject to statements of partnership authority under Section 303. *See* the comment to Section 301(1).

Subsection (b)—This subsection deals with the right of a partnership to recover partnership property transferred by a partner without actual authority. The subsection's structure corresponds to the structure of Subsection (a).

Subsection (b)(1)—This paragraph deals with the recovery of “property transferred under subsection (a)(1) [or] (2).”

Subsection (b)(2)—This paragraph deals with the recovery of “property transferred under subsection (a)(3).”

Subsection (c)—UPA (1997) added this subsection, which parallels Uniform Fraudulent Transfer Act, section 8(a) (subsequent transferee from bona fide purchaser protected), 8(b)(2) (same).

Subsection (d)—UPA (1997) added this subsection. So that this provision does not destroy transferee rights, “all the partners interests” must be read to mean “each interest that originated as a partner interest—which includes all transferable interests, by whomever owned.”

The UPA (1997) comment to this subsection took a noteworthy position on the consequences of all the partners’ interests in the partnership being held by one person:

Subsection (d) allows for clear record title, even though the partnership no longer exists as a technical matter. When a partnership becomes a sole proprietorship by reason of the dissociation of all but one of the partners, title vests in the remaining “partner,” although there is no “transfer” of the property. The remaining “partner” may execute a deed or other transfer of record in the name of the non-existent partnership to evidence vesting of the property in that person’s individual capacity.

Section 801(6), added during the Harmonization Project, changes the analysis. The paragraph states that dissolution is caused by “the passage of 90 consecutive days during which the partnership does not have at least two partners.” Consequently, for at least eighty-nine consecutive days a partnership remains un-dissolved although having only one partner, and even at ninety days the partnership remains a partnership, albeit dissolved and compelled to wind up its business. Subsection (d) remains quite useful if the sole remaining partner winds up the partnership by becoming a sole proprietor, but it is no longer accurate to state that a partnership with only one partner “no longer exists as a technical matter.”

SECTION 303. STATEMENT OF PARTNERSHIP AUTHORITY.

(a) A partnership may deliver to the [Secretary of State] for filing a statement of partnership authority. The statement:

(1) must include the name of the partnership and:

(A) if the partnership is not a limited liability partnership, the street and mailing addresses of its principal office; or

(B) if the partnership is a limited liability partnership, the name and street and mailing addresses of its registered agent;

(2) with respect to any position that exists in or with respect to the partnership, may state the authority, or limitations on the authority, of all persons holding the position to:

(A) sign an instrument transferring real property held in the name of the partnership; or

(B) enter into other transactions on behalf of, or otherwise act for or bind, the partnership; and

(3) may state the authority, or limitations on the authority, of a specific person to:

(A) sign an instrument transferring real property held in the name of the partnership; or

(B) enter into other transactions on behalf of, or otherwise act for or bind, the partnership.

(b) To amend or cancel a statement of authority filed by the [Secretary of State], a partnership must deliver to the [Secretary of State] for filing an amendment or cancellation stating:

(1) the name of the partnership;

(2) if the partnership is not a limited liability partnership, the street and mailing addresses of the partnership's principal office;

(3) if the partnership is a limited liability partnership, the name and street and mailing addresses of its registered agent;

(4) the date the statement being affected became effective; and

(5) the contents of the amendment or a declaration that the statement is canceled.

(c) A statement of authority affects only the power of a person to bind a partnership to persons that are not partners.

(d) Subject to subsection (c) and Section 103(d)(1), and except as otherwise provided in subsections (f), (g), and (h), a limitation on the authority of a person or a position contained in an effective statement of authority is not by itself evidence of any person's knowledge or notice of the limitation.

(e) Subject to subsection (c), a grant of authority not pertaining to transfers of real property and contained in an effective statement of authority is conclusive in favor of a person that gives value in reliance on the grant, except to the extent that if the person gives value:

(1) the person has knowledge to the contrary;

(2) the statement has been canceled or restrictively amended under subsection (b);

or

(3) a limitation on the grant is contained in another statement of authority that became effective after the statement containing the grant became effective.

(f) Subject to subsection (c), an effective statement of authority that grants authority to transfer real property held in the name of the partnership, a certified copy of which statement is recorded in the office for recording transfers of the real property, is conclusive in favor of a person that gives value in reliance on the grant without knowledge to the contrary, except to the extent that when the person gives value:

(1) the statement has been canceled or restrictively amended under subsection (b), and a certified copy of the cancellation or restrictive amendment has been recorded in the office for recording transfers of the real property; or

(2) a limitation on the grant is contained in another statement of authority that

became effective after the statement containing the grant became effective, and a certified copy of the later-effective statement is recorded in the office for recording transfers of the real property.

(g) Subject to subsection (c), if a certified copy of an effective statement containing a limitation on the authority to transfer real property held in the name of a partnership is recorded in the office for recording transfers of that real property, all persons are deemed to know of the limitation.

(h) Subject to subsection (i), an effective statement of dissolution is a cancellation of any filed statement of authority for the purposes of subsection (f) and is a limitation on authority for purposes of subsection (g).

(i) After a statement of dissolution becomes effective, a partnership may deliver to the [Secretary of State] for filing and, if appropriate, may record a statement of authority that is designated as a post-dissolution statement of authority. The statement operates as provided in subsections (f) and (g).

(j) Unless canceled earlier, an effective statement of authority is canceled by operation of law five years after the date on which the statement, or its most recent amendment, becomes effective. The cancellation is effective without recording under subsection (f) or (g).

(k) An effective statement of denial operates as a restrictive amendment under this section and may be recorded by certified copy for purposes of subsection (f)(1).

Comment

UPA (1997) § 303 pioneered this concept, which was refined in ULLCA (2006) and further refined in the Harmonization Project. This section is conceptually divided into two realms: (i) statements pertaining to the power to transfer interests in the partnership real property; and (ii) statements pertaining to other matters. In the latter realm, statements are filed only in the records of the filing office and operate only to the extent the statements are actually known and relied on by a third party. Section 303(d), (e).

As to interests in real property, in contrast, this section: (i) requires double filing—with the filing office and in the appropriate land records; and (ii) provides for constructive knowledge of statements limiting authority. Thus, a properly filed and recorded statement can protect the partnership, Section 303(g), and, in order for a statement pertaining to real property to be a sword in the hands of a third party, the statement must have been both filed and properly recorded, Section 303(f). Experience suggests that statements of authority will most often be used in connection with transactions in real estate.

By its terms, this section applies only to domestic general partnerships. The section refers throughout to “partnership,” which means a domestic general partnership. *See* Section 102(11) (“‘Partnership’ . . . means an association of two or more persons to carry on as co-owners a business for profit formed under this [act] or that becomes subject to this [act] under [Article] 11 [mergers and other organic transactions] or Section 110 [transition provision that eventually makes pre-existing general partnerships subject to this act].”). *Cf. Fannie Mae v. Heather Apartments Ltd. P’ship*, A13-0562, 2013 WL 6223564, at *6 (Minn. Ct. App. Dec. 2, 2013) (considering the remedies available to a judgment creditor with respect to the judgment debtor’s interest in a Cook Islands LLC; rejecting the debtor’s argument that the creditor’s “only remedy is to obtain a charging order under” [the Minnesota LLC statute]; explaining that “this argument fails because that statute only applies to Minnesota limited liability companies” which that statute “defines . . . as ‘a limited liability company, other than a foreign limited liability company, organized or governed by this chapter’”) (emphasis added) (statutory citations omitted).

Subsection (a)(2)—This paragraph permits a statement to designate authority by position (or office) rather than by specific person, thus avoiding the need to file anew whenever a new person assumes the position or the office. This type of a statement will enable partnerships to provide evidence of ongoing power to enter into transactions without having to disclose to third parties the entirety of the partnership agreement.

Here and elsewhere in the section, the phrase “real property” includes all types of interests in real property, such as mortgages, easements, etc.

Subsection (a)(2)(A) and (a)(3)(A)—The authority to “sign” an instrument includes the authority to commit the partnership to the transfer reflected in the agreement. *See* Subsection (f) (referring not merely to signing but also to “an effective statement of authority that grants authority to transfer real property”).

Subsection (c)—This subsection expresses a very important limitation – *i.e.*, that this section’s rules do not operate *viz-a-viz* partners. For partners, the partnership agreement is controlling. Section 107(d). However, like any other record delivered for filing on behalf of a partnership, a statement of authority might be some evidence of the contents of the partnership agreement. *See* the comment to Section 107(d).

Another important limitation exists. The filing office is not affected by a statement of authority that purports to delineate the authority of persons to sign documents to be delivered for filing on behalf of a partnership. The act does define “[p]erson” to include a “government or governmental subdivision, agency, or instrumentality,” Section 102(14), but “a limitation on the

authority of a person or a position contained in an effective statement of authority is not by itself evidence of knowledge or notice of the limitation by any person,” Subsection (d).

Moreover, even if an employee of the filing office happened to see that a statement of authority purported to delineate the authority of persons to sign records to be delivered on behalf of a partnership, that information would not pertain to a “fact [that] is material to the agent's duties to the principal” and therefore would not be attributed to the filing office. RESTATEMENT (THIRD) OF AGENCY § 5.03 (2006).

Subsection (d)—The phrase “by itself” is important, because the existence of a limitation of authority could be evidence if, for example, the person in question reviewed the public record at a time when the limitation was of record.

Subsection (e)(2)—This paragraph by its terms does not affect a claim of lingering apparent authority. A person could: (i) assert knowledge of a statement of authority as the statement existed before a cancellation or restrictive amendment; and (ii) characterize the original statement as a manifestation of authority traceable to the partnership. RESTATEMENT (THIRD) OF AGENCY § 3.03, cmt. b (2006) (“Apparent authority is present only when a third party's belief is traceable to manifestations of the principal.”).

However, for apparent authority to exist, the purported agent must *reasonably* appear to be authorized. RESTATEMENT (THIRD) OF AGENCY § 2.03 (2006) (stating that apparent authority can only exist when “a third party reasonably believes the actor has authority to act on behalf of the principal”). Given the possibility of cancellation or restrictive amendment, how reasonable can it be for a person to know of a statement of authority, let time pass, and then rely on the statement without re-checking the public record?

Subsections (f)–(h)—These subsections: (i) pertain to transactions in real property; (ii) provide a mechanism by which authority to transfer a partnership’s real property can be made to appear in the real estate records; and (iii) thus address the principal concerns (raised by real estate lawyers) that led the drafters of UPA (1997) to provide for statements of authority.

Subsection (f)—This subsection provides a sword for a vendee of real property. If the vendee has “give[n] value in reliance on the grant without knowledge to the contrary,” the statement of authority protects the vendee against claims that contradict the grant.

Subsection (f)(1) and (2)—As to a claim of lingering apparent authority, see Section (e)(2), comment. The analysis stated there applies even more strongly in the context of customary practices involving land transfers.

Subsection (g)—This subsection provides a shield for the partnership as alleged vendor. If a vendee’s claim contradicts the stated limitation, constructive notice knowledge (“deemed to know”) defeats the claim even if the vendee gave value and lacked actual knowledge.

Subsection (h)—This subsection integrates statements of dissolution, Section 802(b)(2)(A), and termination, Section 802(b)(2)(F), into the operation of this section.

The effect of a statement of dissolution depends on the circumstances.

EXAMPLE: ABC, a general partnership, has in effect a properly filed and recorded statement of authority authorizing ABC's CEO to transfer real estate owned by the partnership. The proper filing and recording by ABC of a statement of dissolution cancels the statement of authority. Subsequently, Buyer gives value in return for a deed signed by the CEO on behalf of ABC. Due to Subsections (h) and (f)(1), Subsection (f) does not protect Buyer. Moreover, under Subsections (g) and (h), Buyer is "deemed to know" of the dissolution. Whether that deemed knowledge functions to deprive the CEO of authority to bind ABC depends on agency law and additional facts. For example, the CEO might have had actual or apparent authority to transfer the real estate despite the dissolution of the partnership.

In contrast, the effect of a statement of termination, Section 802(b)(2)(f), is categorical. If properly filed with the filing office and properly recorded in the office for land records, the statement eliminates the power of any person to transfer real property owned in the name of the partnership. No one can have the authority to act for a non-existent entity. *Cf.* RESTATEMENT (THIRD) OF AGENCY § 4.04(1)(a) (2006) (precluding ratification by a principal that did not exist at the time of the unauthorized act).

Subsection (i)—This provision permits a partnership to use statements of authority during winding up. As an additional protection for third parties, a statement must be "designated as a post-dissolution statement of authority" to be effective under this provision.

Subsection (k)—Presumably, when real property is involved, a person who obtains the filing of a statement of denial under Section 304 will cause a certified copy of the statement to be "recorded by certified copy for purposes of subsection (f)(1)" [undercutting constructive notice as to authority to transfer real property]. However, nothing in this subsection prevents the partnership from causing a certified copy to appear in the land records; due the section's use of the passive voice ("may be recorded"), the act does not delimit who has the authority to act under this subsection.

SECTION 304. STATEMENT OF DENIAL. A person named in a filed statement of authority granting that person authority may deliver to the [Secretary of State] for filing a statement of denial that:

(1) provides the name of the partnership and the caption of the statement of authority to which the statement of denial pertains; and

(2) denies the grant of authority.

Comment

A person whose powers are delineated in the public record by another person should have the right to dissent from that delineation. This section takes an “all or nothing” approach; a person may not deny in part and confirm in part. For the effect of a statement of denial, see Section 303(c), comment, and Section 303(k).

Section 308(c) makes clear that a person does not become a partner solely because he is named as a partner in a statement of partnership authority filed by another person.

SECTION 305. PARTNERSHIP LIABLE FOR PARTNER’S ACTIONABLE CONDUCT.

(a) A partnership is liable for loss or injury caused to a person, or for a penalty incurred, as a result of a wrongful act or omission, or other actionable conduct, of a partner acting in the ordinary course of business of the partnership or with the actual or apparent authority of the partnership.

(b) If, in the course of the partnership’s business or while acting with actual or apparent authority of the partnership, a partner receives or causes the partnership to receive money or property of a person not a partner, and the money or property is misapplied by a partner, the partnership is liable for the loss.

Comment

Subsection (a)—This provision is derived from UPA (1914) § 13 (Partnership Bound by Partner’s Wrongful Act), as modernized by UPA (1997) § 305(a) (Partnership Liable for Partner’s Actionable Conduct) and for the most part parallels the agency law doctrine of *respondeat superior*. See RESTATEMENT (SECOND) OF AGENCY § 14A, cmt. a (1958) (“When one of the partners is in active management of the business or is otherwise regularly employed in the business, he is a servant of the partnership.”). The liability is vicarious and without regard to the fault of those managing the partnership.

UPA (1997) expanded this attribution rule in two ways. First, the 1997 language omitted the 1914 phrase “not being a partner in the partnership,” thereby permitting a partner to sue the partnership under this subsection during the term of the partnership, rather than being limited to the remedies of dissolution and an accounting. This change was consistent with UPA(1997) § 410(b) (stating “[a] partner may maintain an action against the partnership or another partner, with or without an accounting as to partnership business, to enforce the partner’s rights and

protect the partner's interests"). Second, adding "or other actionable conduct" broadens the subsection to cover no-fault torts.

To successfully invoke this provision, a plaintiff must show: (i) "a wrongful act or omission or other actionable conduct" by a partner; (ii) that caused "loss or injury"; and (iii) that at the relevant moment, the partner was acting with actual authority, apparent authority (if relevant), or within "the ordinary course of business of the partnership."

Extrapolating from agency law, apparent authority is relevant only when the appearance of authority augments the impact of the wrongful act. *See* RESTATEMENT (THIRD) OF AGENCY, § 7.08 (2006) ("A principal is subject to vicarious liability for a tort committed by an agent in dealing or communicating with a third party on or purportedly on behalf of the principal when actions taken by the agent with apparent authority constitute the tort or enable the agent to conceal its commission.").

An act or omission may be "in the ordinary course of business of the partnership" even though the act is wrongful. Any other interpretation would vitiate the "ordinary course" element. "The proper question . . . is not whether the specific wrongful act is 'ordinary course' . . . , but rather whether that type of act, if done rightfully, would be." DANIEL S. KLEINBERGER, AGENCY, PARTNERSHIP AND LLCs: EXAMPLES AND EXPLANATIONS § 10.5.1, at 350 (4th ed. 2012) (emphasis omitted)

However, in *Jackson v. Jackson*, 201 S.E.2d 722, 724 (N.C. App. 1974), the North Carolina Court of Appeals stated that, while "[a]dvising the initiation of a criminal prosecution is clearly within the normal range of activities for a typical law partnership, . . . taking such action maliciously and without probable cause is quite a different matter." The court held that "[i]n view of [ethics] rules, which clearly forbid any attempt by a lawyer to prosecute a person without cause, it cannot be held that malicious prosecution is within the ordinary course of business of a law partnership." *Id.* It is difficult to identify a reasonable limit to this approach. Presumably, at least, a partner's "plain vanilla" malpractice is within a law firm's ordinary course of business despite the ethical rules requiring lawyers to act zealously and competently.

In any event, Subsection (a) refers to "the ordinary course of business of the *partnership*" (emphasis added); thus, the proper question is whether the conduct is in the ordinary course for the partnership and not whether the particular partner ordinarily plays a role in that part of the partnership's business. *See Vanacore v. Kennedy*, 86 F. Supp. 2d 42, 51 (D. Conn. 1998), *aff'd sub nom.*, *Vanacore v. Space Realty, Inc.*, 208 F.3d 204 (2d Cir. 2000) (stating that "Kennedy [a partner] committed his misdeeds, which led directly to plaintiff's injuries, within the ordinary course of the business of E & K [the partnership]"); *Sheridan v. Desmond*, 697 A.2d 1162, 1166 (Conn. App. Ct. 1997) (stating that to be considered "in ordinary course of the business," a partner's action must be "the kind of thing a . . . partner would do") (emphasis added); *In Moren ex. rel. Moren v. JAX Rest.*, 679 N.W.2d 165, 167–68 (Minn. Ct. App. 2004) (stating, as part of its analysis under UPA (1997) § 305, that "[i]t is undisputed that one of the cooks scheduled to work that evening [at the partnership's restaurant] did not come in, and that [one] partner asked [another partner] to help in the kitchen . . . [and] that [the other partner] was making pizzas for the partnership when" her negligence injured the plaintiff).

Subsection (b)—This provision is derived from UPA (1914) § 14 (Partnership Bound by Partner’s Breach of Trust) and UPA (1997) § 305(b) (Partnership Liable for Partner’s Actionable Conduct). It is not necessary that the partner “receiv[ing] or caus[ing] the partnership to receive money or property” do so wrongfully. Culpability is necessary at the second phase—*i.e.* when “the money or property is misapplied by a partner.”

SECTION 306. PARTNER’S LIABILITY.

(a) Except as otherwise provided in subsections (b) and (c), all partners are liable jointly and severally for all debts, obligations, and other liabilities of the partnership unless otherwise agreed by the claimant or provided by law.

(b) A person that becomes a partner is not personally liable for a debt, obligation, or other liability of the partnership incurred before the person became a partner.

(c) A debt, obligation, or other liability of a partnership incurred while the partnership is a limited liability partnership is solely the debt, obligation, or other liability of the limited liability partnership. A partner is not personally liable, directly or indirectly, by way of contribution or otherwise, for a debt, obligation, or other liability of the limited liability partnership solely by reason of being or acting as a partner. This subsection applies:

(1) despite anything inconsistent in the partnership agreement that existed immediately before the vote or consent required to become a limited liability partnership under Section 901(b); and

(2) regardless of the dissolution of the limited liability partnership.

(d) The failure of a limited liability partnership to observe formalities relating to the exercise of its powers or management of its business is not a ground for imposing liability on a partner for a debt, obligation, or other liability of the partnership.

(e) The cancellation or administrative revocation of a limited liability partnership’s statement of qualification does not affect the limitation in this section on the liability of a partner

for a debt, obligation, or other liability of the partnership incurred while the statement was in effect.

Comment

Derivation—This section was derived from UPA (1997) § 306, which was also the source for ULPA (2001) § 404 and ULLCA (2006) § 304. The Harmonization Project brought the two partnership acts and the limited liability company act into accord to the extent the three acts overlap.

Subsection (a)—Until the advent of limited liability partnerships and limited liability limited partnerships, one hallmark of general partner status was strict, vicarious liability for the debts, obligations, and other liabilities of the partnership. This subsection states that venerable rule, albeit with two changes:

- Under UPA (1914) § 15, the nature of the general partners' liability depended on the claim, giving rise to the partnership's liability. If the partnership's liability sounded in tort, the general partners' liability was joint and several. If the partnership's liability sounded in contract, the general partners' liability was only several. UPA (1997) § 306(a) dispensed with that distinction.
- UPA (1997) § 307(d) generally requires a judgment creditor to exhaust the partnership's assets before enforcing a judgment against the separate assets of a partner. Prior law was to the contrary.

The Harmonization Project made no substantive changes to this subsection.

Subsection (b)—UPA (1997) continued the approach of UPA (1914) §§17 and 41(7) to the vicarious liability of an incoming partner, but used a simpler and clearer formulation. The Harmonization Project made no substantive changes to this subsection.

With regard to when a partnership incurs a debt, obligation, or other liability, the case law is scant and concerns only contractual and similar obligations. The leading case is *Conklin Farm v. Leibowitz*, 658 A.2d 1257 (N.J. 1995), which holds that: (i) obligations on a loan, whether for interest or principal, are incurred when the loan is made, not when each particular payment is due; and (ii) obligations for lease payments are incurred when each rental payment is due, not when the lease is made.

Conklin concerned a partnership loan obligation that was: (i) entered into before a particular partner joined the partnership; but (ii) for the most part, was payable afterwards. The court held that “interest is part of the contractual debt, and the obligation to pay interest on a loan *arises*, if at all, at the time that the parties execute the note or other debt instrument. *Conklin*, 658 A.2d at 1261. The court indicated that the same analysis applies to the obligation to repay principal. *Id.* at 1263 (stating that “the decisive issue before this court . . . [is that] [p]ayment of interest, like repayment of advances, is an obligation that arises at the time the debt instrument is executed”).

Conklin discussed the lease issue in response to the creditor's argument that “just as a rent obligation arises for current use of property, an interest obligation arises for current use of principal.” *Id.* at 1261. Rejecting that argument, the court: (i) noted “the *common-law* obligation to pay rent based on current tenancy [which] . . . arises with each period of tenancy, and . . . arises even in the absence of a lease”; (ii) described “the common-law obligation to pay rent [as] entirely independent of the contractual obligation under the lease”; and (iii) held that, for purposes of partnership law, the rule for “incurring” a lease obligation rests on the common law duty in tenancy and not on the lease as a contract. *Id.* at 1262 (citing *Ellingson v. Walsh, O'Connor & Barneson*, 104 P.2d 507, 508 (Cal. 1940)).

As to when a partnership incurs a tort liability, the answer might be found by analogy to statute of limitation rules, another area of law concerned with when claims arise. “Although the courts have not been consistent . . . , the interpretation of [when] a . . . statute [of limitations begins to run] as applied to torts has been such that the statute does not usually begin to run until the tort is complete A tort is ordinarily not complete until there has been an invasion of a legally protected interest of the plaintiff.” RESTATEMENT (SECOND) OF TORTS § 899, cmt c (1979); *see also Loehr v. Ventura Cnty. Cmty. Coll. Dist.*, 147 Cal. App. 3d 1071, 1078 (Cal. Ct. App. 1983). By analogy, a partnership would incur liability for a tort when the harm occurs. *See, e.g., Jones v. Cox*, 828 P.2d 218, 224 (Colo. 1992) (“A cause of action has commonly been understood to ‘accrue’ when a suit may be maintained thereon.”) (quoting BLACK’S LAW DICTIONARY 19 (5th ed. 1979)); *Loehr*, 147 Cal. App. 3d at 1078.

However, a policy argument exists to the contrary. Vicarious liability for a partnership's torts should be confined to persons who are partners when the wrongful conduct occurs. It is the conduct, not the consequences, that is wrongful; therefore, the occurrence of the wrongful conduct should determine which set of partners is liable for the conduct's consequences.

For further discussion of the “incurred” issue, see Subsection (c), comment (The Temporal Nexus—When Claim Incurred).

Subsection (c)—This subsection provides a corporate/LLC-like liability shield for partners, protecting them from (and only from) the debts, obligations and liabilities of the partnership – *i.e.*, against a partner’s alleged vicarious liability for the obligations of the entity.

Full Liability Shield

This act provides a full liability shield – *i.e.*, the shield applies regardless of the law giving rise to a claim against an LLP. A few jurisdictions provide only a partial shield. *See, e.g.*, 15 PA. CONS. STAT. ANN. § 8204 (West 2013) (providing the partners of an LLP a shield for claims against the partnership “whether sounding in contract or tort or otherwise,” but only the claims that “arise from any negligent or wrongful acts or misconduct committed by another partner or other representative of the partnership”). The resulting partial shield does not protect partners against liability for the partnership’s ordinary commercial debts, such as liability for lease payments.

Shield Applicable Regardless of the Identity of the Plaintiff

What makes the shield relevant is the nature of the claim. If the complaint seeks to hold a partner vicariously liable for the LLP's obligations, the shield applies. If not, not. Thus, there is no distinction among a claim arising from an LLP's debt to a commercial creditor, a partner's claim that the LLP has failed to return a contribution as required by the partnership agreement, and a claim by a former partner that the LLP has failed to follow through on a buy-out agreement. *See Rappaport v. Gelfand*, 197 Cal. App. 4th 1213, 1230–32 (Cal. Ct. App. 2011) (involving a claim by a former partner). *Accord Ederer v. Gursky*, 881 N.E.2d 204, 212–13 (N.Y. 2007) (Smith, J., dissenting).

Shield Inapposite for Claims Arising from a Partner's Own Conduct

Because the partner liability at issue is solely vicarious, the LLP shield is irrelevant to claims seeking to hold a partner directly liable on account of the partner's own conduct. Case law on this issue comes from the analogous context of limited liability companies, and in that context a few judges have failed to understand this point. *See ULLCA* (2006) (Last Amended 2013) § 304(c), cmt. (Shield Inapposite for Claims Arising from a Member's or Manager's Own Conduct). However, the overwhelming weight of case law is contrary, as are the actual words of shield provisions (immunizing only for obligations of the entity and making no reference to direct obligations of an owner or manager) and public policy (which recoils from the idea of immunizing a person's misconduct solely because the person acts on behalf of an organization).

EXAMPLE: A partner personally guarantees a debt of a limited liability partnership. Subsection (c) is irrelevant to the partner's liability as guarantor.

EXAMPLE: A partner purports to bind a limited liability partnership while lacking any agency law power to do so. The LLP is not bound, but the partner is liable for having breached the "warranty of authority" (an agency law doctrine). Subsection (c) does not apply. The liability is not *for* a debt, obligation, or other liability of the LLP, but is rather the partner's own, direct liability. Indeed, the liability exists because the LLP is *not* indebted, obligated or liable. RESTATEMENT (THIRD) OF AGENCY § 6.10 (2006).

EXAMPLE: A partner of a limited liability partnership defames a third party in circumstances that render an LLP vicariously liable under Section 305(a). Under Subsection (c), the third party cannot hold the partner accountable for the *partnership's* liability, but that protection is immaterial. The partner is the tortfeasor and in that role is directly liable to the third party.

EXAMPLE: A limited liability partnership provides professional services, and one of its partners commits malpractice. The liability shield is irrelevant to the partner's direct liability in tort. However, if the partner's malpractice liability is attributed to the partnership under Section 305(a), the liability shield will protect the other partners against a claim that they must make good on the LLP's liability. The same analysis applies if the plaintiff also successfully claims that another partner was negligent in supervising the first partner.

EXAMPLE: A limited liability partnership with two partners enters into a contract to build a home, and the partners perform substantial amounts of the work. The homeowner sues both the LLP and the partners for allegedly defective work, but the complaint sounds in contract rather than in tort. The LLP may be liable, but the partners are not. *See Ogea v. Merritt*, 130 So. 3d 888, 905 (La. 2013).

Subsection (c) pertains only to claims based on the LLP's liability and is irrelevant to claims by a limited liability partnership or a partner against another partner and *vice versa*. *See* Sections 307 (pertaining to actions by partners), 409 (pertaining to management duties).

Shield Inapposite to Role Liability Claims

Provisions of regulatory law may impose liability on a partner of an LLP due to a role the partner plays in the partnership. *See, e.g., Food Team Intern., Ltd. v. Unilink, L.L.C.*, 872 F. Supp. 2d 405, 424 (E.D. Pa. 2012) (holding several individuals “subject to secondary individual liability under PACA [Perishable Agricultural Commodities Act]” because their roles within a limited liability company enabled them to control the relevant assets) (citing *Bear Mountain Orchards, Inc. v. Mich–Kim, Inc.*, 623 F.3d 163, 172 (3d Cir. 2010)). Subsection (c) does not affect this “role liability.”

The Temporal Nexus—When Claim Incurred

The LLP shield functions only with respect to obligations incurred while the partnership is a limited liability partnership. The shield does not protect partners from vicarious liability for partnership obligations incurred before a partnership becomes an LLP or after the partnership cancels its LLP status. *See* Section 903(d). The same is true initially when LLP status has been administratively revoked, but reinstatement of LLP status resurrects the shield retroactively, except as to persons who relied on the revocation. Section 903(d).

For a preliminary discussion of when a partnership obligation is incurred, see Subsection (b), comment. It could well be argued that “incurred” under Subsection (c) has the same meaning as “incurred” under Subsection (b). *IBP, Inc. v. Alvarez*, 546 U.S. 21, 34 (2005) (referring to “the normal rule of statutory interpretation that identical words used in different parts of the same statute are generally presumed to have the same meaning”); *Timberline Air Serv., Inc. v. Bell Helicopter-Textron, Inc.*, 884 P.2d 920, 925 (1994) (stating that “[w]hen the same words are used in different parts of the same statute, it is presumed that the Legislature intended that the words have the same meaning”).

However, the argument should yield if the subsections’ different contexts raise different issues of policy. 1A SUTHERLAND STATUTES AND STATUTORY CONSTRUCTION § 45:12 (7th ed.) (stating that “departure from the literal construction of a statute is justified when such a construction would produce an absurd and unjust result and would clearly be inconsistent with the purposes and policies of the act in question”); *see, e.g., S.V. v. R.V.*, 933 S.W.2d 1, 4 (Tex. 1996) (“[W]e have held that a cause of action accrues when a wrongful act causes some legal injury, even if the fact of injury is not discovered until later, and even if all resulting damages have not yet occurred. We have not applied this rule without exception, however, and have

sometimes held that an action does not accrue until the plaintiff knew or in the exercise of reasonable diligence should have known of the wrongful act and resulting injury.”) (citations omitted).

The case law concerning contractual obligations (incurred when the contract is made) applies appropriately in the context of the LLP shield. However, the lease case law is problematic. If an obligation is incurred each time rent is due, subsection(c) is a trap for the unwary landlord.

EXAMPLE: Ordinary general partnership enters into a lease with a commercial landlord. Knowing that each partner is automatically liable for the partnership's debt, the landlord does not obtain personal guarantees. Subsequently, the partnership becomes an LLP. If future rent payments are incurred when due, and not as of when the lease was made, the landlord loses a very important part of the bargain.

Thus, for the purposes of Subsection (c), lease obligations should be treated as contractual obligations, incurred when the contract is made.

A similar issue exists with regard to tort liability. Courts must look to when the conduct causing the injury takes place and not to when actual injury occurs. Otherwise, a partnership could: (i) engage in wrongful conduct that does not cause immediate injury; (ii) come to realize that the conduct has occurred; (iii) subsequently file a statement of qualification; (iv) thereby become an LLP; and (v) thereby eliminate the vicarious liability of its partners for all harm subsequently arising from the misconduct. *Cf. Savini v. Univ. of Haw.*, 153 P.3d 1144, 1150 (Haw. 2007) (addressing the question of when a statute of limitations begins to run for bodily injury, when another statute precludes bringing a claim until the amount of damages has reached a specified threshold).

In general, courts should determine the “incurred” question under Subsection (c) so that the LLP shield protects the partners of an LLP to the same extent that the corporate and LLC shields protect corporate shareholders and LLC members. From that perspective, LLP status obtained after a partnership commits a wrongful act should provide no greater protection for the partners than a sole proprietor obtains by forming an LLC after committing a wrongful – *i.e.*, none. *See, e.g., Foxchase, L.L.L.P. v. Cliatt*, 562 S.E.2d 221, 224 (Ga. Ct. App. 2002) (holding that a partnership’s liability shield did not protect partners from claims of property damage caused by the construction of a golf course, where the jury could have found that the “damage . . . occurred when they, not the partnership, owned the course”).

From the same perspective, *Evanston Ins. Co. v. Dillard Dept. Stores, Inc.*, 602 F.3d 610 (5th Cir. 2010) makes no sense. Interpreting the Texas LLP statute, the court held that a partner’s liability for a partnership debit is incurred only when judgment is entered against the partnership. Although the decision itself benefitted creditors, the holding invites the type of gamesmanship shown in the leasing example, above. Moreover, the decision: (i) has been criticized by the Texas Court of Appeals, *Am. Star Energy & Minerals Corp. v. Stowers*, 405 S.W.3d 905, 907 (Tex. App. 2013); (ii) ignores the precedent discussed in Subsection (b), comment and Section 307(c), comment; and (iii) can be distinguished as depending on the particular (non-uniform) language

of the Texas statute. *Evanston Ins. Co v. Dillard Dep't Stores, Inc.*, 602 F.3d 610, 615–16 (5th Cir. 2010) (contrasting “incurred” with “committed”).

Effect of LLP Status on Relations Inter Se the Partners

Although the most noticeable consequence of LLP status is the corporate/LLC-like liability shield, there are two *inter se* consequences as well. One is straightforward; the other is complex.

- When a partnership chooses the jurisdiction in which to deliver for filing a statement of qualification, the partnership chooses its governing law. Section 104(1). The partnership agreement cannot override that choice. Section 105(c)(1).
- When a partnership becomes a limited liability partnership, several related default rules change (going forward):
 - Partners no longer share losses. Capital losses “lay where they fall.”
 - Except for contributions promised but not made, partners no longer have contribution obligations.
 - Due to:
 - the liability shield, partners are no longer required to contribute capital to enable the partnership to meet its obligations to creditors; and
 - the elimination of loss sharing, partners are no longer required to contribute capital to adjust capital losses *inter se*.

In this context, a partnership’s obligations include a duty to indemnify partners (and others). Thus, indemnification provisions (whether as provided by this act, Section 401(c), or the partnership agreement) are no longer “backstopped” by the partners. *See* the comment to Subsection (c)(1).

Subsection (c)(1)—The main part of Subsection (c) overrides contribution obligations under this act. Paragraph 1 overrides contribution obligations created by the partnership agreement.

EXAMPLE: The partnership agreement of a non-LLP partnership requires partners to contribute additional capital as necessary to fund the partnership’s obligations to indemnify partners. When the partnership becomes an LLP, Paragraph 1 overrides that requirement.

Paragraph 1 does not, however, override contribution and indemnification requirements running directly from partner to partner. These obligations are not obligations of the LLP but rather personal to each partner. If such obligations remain in the partnership agreement, they might disable the shield as to partnership liability arising from the misconduct of a partner.

EXAMPLE: The partnership agreement of a non-LLP partnership requires partners to contribute additional capital as necessary to fund the partnership’s obligations to indemnify the Managing Partner and also states:

To the extent the partnership lacks sufficient funds to perform the partnership’s

indemnification obligation, each partner shall indemnify the Managing Partner to the same extent and under the same conditions as the partnership. As among themselves, the indemnifying partners shall share the indemnification obligation proportional to their rights to distributions of then current profits as of the time the Managing Partner's conduct gave rise to the claim for which the Managing Partner is to be indemnified.

The partnership becomes an LLP. Subsequently, the Managing Partner is held liable in tort for conduct within the scope of the Managing Partner's responsibility and the partnership is held liable under Section 305(a). The partnership has no funds to pay the judgment or indemnify the Managing Partner. Paragraph 1 overrides the contribution requirement but does not change each partner's obligation to indemnify the Managing Partner.

The Managing Partner's right to be indemnified is an asset of the Managing Partner, and the judgment creditor can levy on that asset, thereby defeating the liability shield in effect if not in form.

Subsection (c)(2)—*The Shield and Dissolution.* The rule stated here is inherent in the nature of partnership dissolution. “[D]issolution does not end a partnership’s existence but rather changes the purpose of that existence.” Section 801, cmt. “A dissolved partnership shall wind up its business and... continues after dissolution ... for the purpose of winding up.” Section 802(a). Put another way: dissolution and winding up are part of the life cycle of a partnership – sometimes the most complicated part. There is no logical reason to remove the shield during the last part of an LLP’s life cycle.

This subsection makes this point expressly, because it is possible to misinterpret some outlying cases as holding to the contrary. *See, e.g., Carolina Cas. Ins. Co. v. L.M. Ross Law Grp., LLP*, 151 Cal. Rptr. 3d 628, 635 (2012) (affirming the trial court’s decision to hold an LLP’s named partner liable for a judgment against his limited liability partnership; noting that “[c]entral to the decision to amend the judgment to add Ross [the named partner] as a judgment debtor ... is the trial court’s finding that Ross Law Group dissolved”; recognizing, however, that, before the partnership incurred the liability, Ross had signed and filed with the California Secretary of State a form stating that the law firm had “cease[d] to be a registered limited liability partnership and is hereby filing this notice with the California Secretary of State that [it] is no longer a registered limited partnership”) (quotation marks omitted).

The Shield and Termination. This subsection does not expressly provide that, when a limited liability partnership’s existence terminates, the LLP shield remains in place as to any debt, obligation, or other liability of the partnership incurred before the termination. However, the point follows ineluctably from Subsection 306(b). That subsection adopts an “occurrence” rather than a “claims made” basis for determining whether the shield applies. *See* the comment to Subsection (b). (The Temporal Nexus –When Claim Incurred).

Moreover, any other result would: (i) create huge holes in the shield; (ii) put the law of unincorporated businesses at odds with the law of corporations; (iii) render surplus this act’s distribution recapture provision, Section 407; (iv) render meaningless the exception to the notice requirement as stated in Sections 807(b)(5) and 808(b)(4); and (v) render nonsensical the otherwise logical extension of the equitable trust fund theory to limited liability partnerships. *Cf.*

Velasquez v. Franz, 589 A.2d 143, 146 (N.J. 1991) (explaining that “the trust-fund doctrine... renders shareholders who receive distributed assets of the corporation liable as ‘trustees’ for claims of the corporation's creditors”).

Subsection (d)—This subsection was added during the Harmonization Project and pertains to the equitable doctrine of “piercing the veil” – *i.e.*, conflating an entity and its owners to hold one liable for the obligations of the other. The doctrine of “piercing the corporate veil” is well established, and courts should apply the doctrine to limited liability partnerships for the same reasons that courts have regularly (and sometimes almost reflexively) applied the doctrine to limited liability companies. *Cf. Axtmann v. Chillemi*, 740 N.W.2d 838, 847 (N.D. 2007) (stating that “the shield of a limited liability partnership may be pierced under ‘the case law that states the conditions and circumstances under which the corporate veil or limited liability shield of a corporation may be pierced under North Dakota law’”) (quoting N.D.C.C. § 45-22-09(1)).

However, as with LLC piercing, LLP piercing involves one important distinction from the corporate realm. While under corporate law “disregard of corporate formalities” is a key piercing factor, that factor is inapposite in the law of unincorporated organizations. Corporate formalities reflect statutory mandates. LLP formalities derive for the most part from the agreement among the partners. From a policy perspective, disregarding formalities adopted by agreement differs substantially from disregarding formalities imposed by law. *See e.g. In re Packer*, Bankruptcy No. 13–41304, 2014 WL 5100095 (Bankr. E.D. Tex. Oct. 10, 2014) (noting the informality of LLC governance, recognizing that “the disregard of corporate formalities ... [is] one of the key factors in [corporate] veil-piercing determinations”; but holding that “it makes no sense to imperil the shield simply because the members do not undergo meaningless formalities such as formal meetings”) (citing Carter G. Bishop & Daniel S. Kleinberger, LIMITED LIABILITY COMPANIES: TAX AND BUSINESS LAW ¶ 6.03 at *3 (Thomson Reuters Tax and Accounting 2014)).

Moreover, because the terms of a partnership agreement may be “implied,” Section 102(12), an LLP’s ongoing disregard of formalities may well constitute an amendment to the partnership agreement. If so, disregard equals amendment, and the concept of “disregard of formalities” makes no sense.

In contrast, this subsection is inapposite to another key piercing factor – disregard of the separateness between entity and owner. *Cf. Vanderford Co. v. Knudson*, 165 P.3d 261, 271 (Idaho 2007) (noting that managing member and “his accountant testified that the LLC’s checking account was so confusing that the accountant could not be sure whose money was in the account at what times”); *Utzler v. Braca*, 972 A.2d 743 (Conn. App. Ct. 2009) (holding that veil piercing was appropriate under alter-ego theory when owner deposited LLC funds into a commingled bank account from which he made withdrawals for personal needs and unrelated projects).

EXAMPLE: A partner in a limited liability partnership uses a car titled in the partnership’s name for personal purposes and writes checks on the partnership’s account to pay for personal expenses. These facts are relevant to a piercing claim; they pertain to economic separateness, not Subsection (b) formalities.

This subsection addresses claims to “impos[e] liability on a partner for a debt, obligation,

or other liability of the partnership” – *i.e.*, for what is sometimes termed a “direct pierce.” Whether the same approach should apply to claims for a “reverse pierce” is a question for the courts. *See Comm’r of Envtl. Prot. v. State Five Indus. Park, Inc.*, 37 A.3d 724, 732–33 (Conn. 2012) (stating that “[a]lthough some courts have adopted reverse veil piercing with little distinction as a logical corollary of traditional veil piercing, because the two share the same equitable goals, others wisely have recognized important differences between them”).

This subsection is inapposite to a member’s claim that the disregard of agreed-upon formalities is a breach of the partnership agreement.

Subsection (e)—The rule stated here is implicit in Subsection (c) but is stated expressly for the avoidance of doubt.

SECTION 307. ACTIONS BY AND AGAINST PARTNERSHIP AND PARTNERS.

(a) A partnership may sue and be sued in the name of the partnership.

(b) To the extent not inconsistent with Section 306, a partner may be joined in an action against the partnership or named in a separate action.

(c) A judgment against a partnership is not by itself a judgment against a partner. A judgment against a partnership may not be satisfied from a partner’s assets unless there is also a judgment against the partner.

(d) A judgment creditor of a partner may not levy execution against the assets of the partner to satisfy a judgment based on a claim against the partnership unless the partner is personally liable for the claim under Section 306 and:

(1) a judgment based on the same claim has been obtained against the partnership and a writ of execution on the judgment has been returned unsatisfied in whole or in part;

(2) the partnership is a debtor in bankruptcy;

(3) the partner has agreed that the creditor need not exhaust partnership assets;

(4) a court grants permission to the judgment creditor to levy execution against the assets of a partner based on a finding that partnership assets subject to execution are clearly insufficient to satisfy the judgment, that exhaustion of partnership assets is excessively

burdensome, or that the grant of permission is an appropriate exercise of the court's equitable powers; or

(5) liability is imposed on the partner by law or contract independent of the existence of the partnership.

(e) This section applies to any debt, liability, or other obligation of a partnership which results from a representation by a partner or purported partner under Section 308.

Comment

Section 307 reflects the entity construct, Section 201(a), was new in UPA (1997), and cannot be varied by the partnership agreement. *See* Section 105(c)(3). The Harmonization Project made no substantive changes to this section.

Subsection (a)—UPA (1997) § 307 clarified and simplified an “entity versus aggregate” question that had been at best complicated under the common law and UPA (1914) (*i.e.*, whether a general partnership could sue and be sued in its own name and without joining all the partners).

“[A]t common law, . . . a partnership could neither sue or be sued in its name. The individual partners were required to be named as plaintiffs in an action brought by the partnership and as defendants in an action against a partnership.” *Telamarketing Commc'ns, Inc. v. Liberty Partners*, 798 S.W.2d 462, 463 (Ky. 1990) (discussing Kentucky law); *see also* JOSEPH STORY, COMMENTARIES ON THE LAW ON PARTNERSHIP § 241, at 373–74 (2d ed. 1850) (“It is a general rule, that in all such suits at law [between a partnership and a third party] all the partners should join.”).

UPA (1914) was silent on the point, although some courts inferred capacity to sue (and presumably to be sued) from other entity-like characteristics reflected in that act. *E.g.*, *Decker Coal Co. v. Commonwealth Edison Co.*, 714 P.2d 155, 157 (Mont. 1986) (agreeing with a party's contention that “[a]lthough . . . the UPA does not expressly deal with the question of a partnership's capacity to sue, . . . the UPA does show the modern tendency to treat a partnership as a legal entity distinct from and independent of the individuals composing it”; citing as an example, a partnership's ability to “own property in its own name”; and holding that “it is clear that a partnership is indeed a legal entity distinct from its partners [and] [t]herefore, . . . has the capacity to sue in its own name”).

The situation was further complicated by “common name” statutes enacted in many states. *See Silliman v. DuPont*, 302 A.2d 327, 331 (Del. Super. 1972), *aff'd sub nom.*, *F. I. Du Pont, Glore Forgan & Co. v. Silliman*, 310 A.2d 128 (Del. 1973) (“The basic purpose of [common name] statutes was to permit a non-corporate entity to be sued in the name it presented to the public without the necessity of joining the many individuals who composed it.”).

The rule stated here is perhaps implicit in Section 201(a) (“A partnership is an entity distinct from its partners.”). It is a hallmark of a legal entity that it can sue and be sued. In any event, this subsection leaves no room for doubt.

Subsection (b)—The phrase “not inconsistent with Section 306” means:

- If a debt, obligation, or other liability is incurred by a limited liability partnership, this subsection does not permit joinder of a partner.
- Likewise, if a debt, obligation, or other liability is incurred by an ordinary partnership before a person becomes a partner, this subsection does not permit joinder of that person.

As for when a claim is incurred, see Section 307(c) and (d), comments.

The reference to “not inconsistent with Section 306” is the procedural analog to the substantive protections of Section 306(b) (incoming partner not liable for pre-existing partnership obligations) and (c) (partners not liable for partnership obligations incurred by an LLP). When a partner has personally guaranteed a partnership obligation, naming that partner in a suit against the partnership is “not inconsistent with Section 306.” *See* the comment to Section 306(c) (Shield Inapposite for Claims Arising from a Partner’s Conduct); *cf. Bank of Bos. Conn. v. Schlesinger*, 595 A.2d 872, 875 (Conn. 1991) (upholding pre-judgment attachment of a partner’s assets, where the partner had personally guaranteed the partnership’s obligations).

Subsection (c)—Reflecting the entity construct, Section 201(a), this subsection provides that a judgment against the partnership: (i) is not, standing alone, a judgment against the partners; and (ii) cannot be satisfied from a partner’s personal assets absent a judgment against the partner.

As did UPA (1914) and UPA (1997), this act leaves to the law of judgments to determine the collateral effects to be accorded a prior judgment for or against the partnership in a subsequent action against a partner individually. *See* RESTATEMENT (SECOND) OF JUDGMENTS § 60, cmts. (1982); *see also Detrio v. U.S.*, 264 F.2d 658 (5th Cir. 1959); *Brunson v. Seltz*, 414 N.W.2d 547 (Minn. Ct. App. 1987) (Lansing, J.). *Contra Evanston Ins. Co. v. Dillard Dep’t Stores, Inc.*, 602 F.3d 610, 618 (5th Cir. 2010) (disregarding *sub silentio* the separateness of partner and partnership, overlooking therefore the issue of collateral estoppel, discussing with approval a bankruptcy case in which “the trustee sought to enforce the partnership judgment against [partners] simply by virtue of their status as partner”; and quoting with approval that case’s holding that “[o]nce the liability of the partnership became fixed, the only issue remaining was whether the Defendants are partners of [the partnership]” (quoting *In re Jones*, 161 B.R. 180, 183–84 (Bankr. N.D. Tex. 1993))).

This subsection and Subsection (d) combine to create a trap for the unwary. For statute of limitations purposes, a creditor’s claim against the partners accrues simultaneously with the claim against the partnership. If a creditor chooses not to sue the partners in its suit against the partnership, the statute of limitations may run before the creditor commences suit against the partners. *Am. Star Energy & Minerals Corp. v. Stowers*, 405 S.W.3d 905, 907 (Tex. App. 2013)

(holding that the partnership creditor “was obligated to sue the partners of S & J . . . within the same limitations period it had to sue S & J, the partnership” and that “[b]ecause, [the creditor] did not, the trial court correctly held that limitations ran”); *Sunseri v. Proctor*, 487 F. Supp. 2d 905, 908 (E.D. Mich. 2007), *aff’d*, 286 F. App’x 930 (6th Cir. 2008) (“While the plaintiff may use collateral estoppel to prevent the partner from relitigating the issue of liability, the plaintiff must still bring suit within the applicable limitations period for the underlying wrong.”)

Subsection (d)—Subject to the five listed exceptions, this subsection prevents a partner’s assets from being the first recourse for a judgment creditor of the partnership, even if the partner is liable for the judgment debt under Section 306.

Although this subsection is silent with respect to pre-judgment remedies, as a matter of policy the subsection should guide courts as they apply the law of pre-judgment remedies. *Compare Sec. Pac. Nat’l Bank v. Matek*, 175 Cal. App. 3d 1071, 1077 (Cal. Ct. App. 1985) (granting a pre-judgment remedy against a partner because there is “no distinction between those sued individually as partners and those sued as sole proprietors”), *with Bank of Bos. Conn. v. Schlesinger*, 595 A.2d 872, 875 (Conn. 1991) (upholding pre-judgment attachment of a partner’s assets, because the partner had personally guaranteed the partnership’s obligations).

Subsection (e)—The effect of this subsection depends on whether Section 308 applies to produce a partnership obligation or a joint and several obligation. *See* Section 308(a) (“If partnership liability results [under the subsection], the purported partner is liable with respect to that liability as if the purported partner were a partner. If no partnership liability results, the purported partner is liable with respect to that liability jointly and severally with any other person consenting to the representation.”), (b) (“If all the partners of the existing partnership consent to the representation, a partnership act or obligation results. If fewer than all the partners of the existing partnership consent to the representation, the person acting and the partners consenting to the representation are jointly and severally liable.”).

SECTION 308. LIABILITY OF PURPORTED PARTNER.

(a) If a person, by words or conduct, purports to be a partner, or consents to being represented by another as a partner, in a partnership or with one or more persons not partners, the purported partner is liable to a person to whom the representation is made, if that person, relying on the representation, enters into a transaction with the actual or purported partnership. If the representation, either by the purported partner or by a person with the purported partner’s consent, is made in a public manner, the purported partner is liable to a person who relies upon the purported partnership even if the purported partner is not aware of being held out as a partner to the claimant. If partnership liability results, the purported partner is liable with respect to that

liability as if the purported partner were a partner. If no partnership liability results, the purported partner is liable with respect to that liability jointly and severally with any other person consenting to the representation.

(b) If a person is thus represented to be a partner in an existing partnership, or with one or more persons not partners, the purported partner is an agent of persons consenting to the representation to bind them to the same extent and in the same manner as if the purported partner were a partner with respect to persons who enter into transactions in reliance upon the representation. If all the partners of the existing partnership consent to the representation, a partnership act or obligation results. If fewer than all the partners of the existing partnership consent to the representation, the person acting and the partners consenting to the representation are jointly and severally liable.

(c) A person is not liable as a partner merely because the person is named by another as a partner in a statement of partnership authority.

(d) A person does not continue to be liable as a partner merely because of a failure to file a statement of dissociation or to amend a statement of partnership authority to indicate the person's dissociation as a partner.

(e) Except as otherwise provided in subsections (a) and (b), persons who are not partners as to each other are not liable as partners to other persons.

Comment

UPA (1997) § 308 continued the basic principles of partnership by estoppel stated in UPA (1914) § 16. To the extent a partnership liability results under Section 308, Section 307 applies. *See* Section 307(e). The Harmonization Project made no substantive changes to this section.

Subsections (a) and (b)—Even though these subdivisions refer to “reliance” without expressly imposing a reasonableness requirement, the requirement exists in the case law. *See, e.g., In re Cay Clubs*, 319 P.3d 625, 633 (Nev. 2014) (adopting the requirement and stating that, although the requirement is not explicitly stated in [the statute,] [g]enerally, jurisdictions provide

that the partnership-by-estoppel doctrine conditions liability on the plaintiff having reasonably relied on the representation of partnership, which often involves an exercise of due diligence to ascertain the facts”).

Subsection (a)—This subsection continues the distinction between representations made to specific persons and those made in a public manner. In both circumstances, the claimant must show reliance.

Like UPA (1914) § 16, this section imposes no duty of denial; thus, a person held out by another as a partner is not liable without having actually consented to the representation. *See* Subsection (c) (no duty to file statement of denial); Subsection (d) (no duty to file statement of dissociation or to amend statement of partnership authority).

Subsections (c) and (d)—These subsections were new in UPA (1997) and preclude negative inferences from outdated information in filed statements.

Subsection (e)—Derived from UPA (1914) § 7(1), this subsection circumscribes the circumstances in which a person can be liable as a partner to third parties for the obligations of the partnership – *i.e.*, only if (i) the person is a partner in the partnership; or (ii) the person is liable under Section 308(a) or (b).

[ARTICLE] 4

RELATIONS OF PARTNERS TO EACH OTHER

AND TO PARTNERSHIP

SECTION 401. PARTNER’S RIGHTS AND DUTIES.

(a) Each partner is entitled to an equal share of the partnership distributions and, except in the case of a limited liability partnership, is chargeable with a share of the partnership losses in proportion to the partner’s share of the distributions.

(b) A partnership shall reimburse a partner for any payment made by the partner in the course of the partner’s activities on behalf of the partnership, if the partner complied with this section and Section 409 in making the payment.

(c) A partnership shall indemnify and hold harmless a person with respect to any claim or demand against the person and any debt, obligation, or other liability incurred by the person by reason of the person’s former or present capacity as a partner, if the claim, demand, debt,

obligation, or other liability does not arise from the person's breach of this section or Section 407 or 409.

(d) In the ordinary course of its business, a partnership may advance reasonable expenses, including attorney's fees and costs, incurred by a person in connection with a claim or demand against the person by reason of the person's former or present capacity as a partner, if the person promises to repay the partnership if the person ultimately is determined not to be entitled to be indemnified under subsection (c).

(e) A partnership may purchase and maintain insurance on behalf of a partner against liability asserted against or incurred by the partner in that capacity or arising from that status even if, under Section 105(c)(7), the partnership agreement could not eliminate or limit the person's liability to the partnership for the conduct giving rise to the liability.

(f) A partnership shall reimburse a partner for an advance to the partnership beyond the amount of capital the partner agreed to contribute.

(g) A payment or advance made by a partner which gives rise to a partnership obligation under subsection (b) or (f) constitutes a loan to the partnership which accrues interest from the date of the payment or advance.

(h) Each partner has equal rights in the management and conduct of the partnership's business.

(i) A partner may use or possess partnership property only on behalf of the partnership.

(j) A partner is not entitled to remuneration for services performed for the partnership, except for reasonable compensation for services rendered in winding up the business of the partnership.

(k) A difference arising as to a matter in the ordinary course of business of a partnership

may be decided by a majority of the partners. An act outside the ordinary course of business of a partnership and an amendment to the partnership agreement may be undertaken only with the affirmative vote or consent of all the partners.

Comment

For the most part, Section 401 merely restates the rules of UPA (1914) § 18, thereby establishing many of the default rules that govern the relations among partners. All of these rules are, however, subject to contrary agreement of the partners as provided in Sections 105 through 107.

UPA (1997) § 401(a) experimented with providing a default configuration for capital accounts. For the reasons stated in Section 405, comment, the Harmonization Project ended the experiment and eliminated the configuration.

Subsection (a)—This subsection continues the approach of UPA (1914) § 18(a), although for the reasons stated in Section 405, comment, the Harmonization Project substituted “distribution” for “profits.” Distributions are shared equally and losses are shared in proportion to each partner’s share of distributions. Thus, under this default rule, partners share distributions per capita and not in proportion to capital contribution (per capital).

If partners agree to share distributions other than equally, losses will be shared in the same proportion as distributions, absent agreement to do otherwise. This rule, carried over from UPA (1914) rests on the assumption that partners would likely agree to share losses on the same basis as distributions, but may fail to say so. Of course, by agreement, they may share losses on a different basis from distributions.

Subject to contrary agreement and the effect of Section 806(e), this subsection’s loss sharing rules apply, even where one or more of the partners contribute no capital. The rule was the same under UPA (1914) § 18(a), although there is some case law to the contrary. *See, e.g., Kovacik v. Reed*, 315 P.2d 314 (Cal. 1957); *Becker v. Killarney*, 523 N.E.2d 467 (Ill. App. Ct. 1988). It may seem unfair that the contributor of services, who contributes little or no capital, should be obligated to contribute toward the capital loss of the large contributor who contributed no services. In entering a partnership with such a capital structure, the partners should foresee that application of the default rule might bring about unusual results and take advantage of their power to vary by agreement the allocation of capital losses.

Subsections (b) and (c)—A partnership’s obligation, if any, to reimburse or indemnify others (*e.g.*, employees, other agents, and independent contractors) is a question for other law, including the law of agency, contract, and restitution. The fact a person has dissociated as a partner does not affect any obligations incurred by the partnership under these subsections for conduct occurring before the dissociation.

To the extent a partnership agreement modifies or displaces the default rules stated in

Sections 401 and 409, the agreement should also address these sections. For example, if the partnership agreement establishes a duty of ordinary care (modifying Section 409(c)), the agreement should specify which level of care is necessary to satisfy Subsections (b) and (c). It is not necessary that the levels of care be the same, only that the partnership agreement make the situation clear and thereby avoid difficult issues of interpretation.

Subsection (b)—UPA (1997) derived this subsection from UPA (1914) § 18(b). The Harmonization Project made two changes: (i) deleting “for the preservation of its business or property” as a separate category for reimbursement, because that category is a subset of the category of “payments made . . . in the course of the partner’s activities on behalf of the partnership”; and (ii) conditioning reimbursement on the partner’s having complied with the duties stated in Section 409.

The reimbursement obligation stated here is a default rule and roughly parallels a rule of agency law. Restatement (Third) of Agency § 8.14(2) (2006) (stating that “[a] principal has a duty to indemnify an agent . . . when the agent makes a payment (i) within the scope of the agent’s actual authority, or (ii) that is beneficial to the principal, unless the agent acts officiously in making the payment”).

Subsection (c)—This subsection provides for indemnification, but the provision is a default rule.

The rule’s eligibility requirements correspond to the default rules on management duties, which is appropriate because otherwise the statutory default rule on indemnification could undercut or even vitiate the statutory default rules on duty. However, subject only to Section 105(c)(8), the partnership agreement can substantially relax the eligibility requirements. The agreement can also impose stricter preconditions.

Although referring broadly to any “person,” this subsection is actually limited to present and former partners. The indemnification obligation applies to only a “debt, obligation, or other liability incurred by the person by reason of the person’s former or present capacity as a partner.” Thus, by its terms this subsection does not apply to a person in the capacity of an officer, manager, etc.

Of course, the partnership agreement may mandate indemnification to persons in such positions, as well as to other persons providing services to or acting for the partnership. Within the limitations stated in Section 105(c)(8), a partnership agreement may obligate a partnership to indemnify a person even though the person has breached a duty to the partnership.

A separate agreement between a partnership and another person may also provide for indemnification. For example, a management contract between a partnership and its managing partner may contain an indemnification provision. The limitations stated in Section 105(c)(8) apply to such separate agreements, for the reasons stated in the comment to that paragraph.

Subsection (d)—This subsection authorizes but does not require a partnership to provide advances to cover expenses. *Cf. Majkowski v. Am. Imaging Mgmt. Servs., L.L.C.*, 913 A.2d 572, 589 (Del. Ch. 2006) (“Because rights to indemnification and advancement differ in important

ways, our courts have refused to recognize claims for advancement not granted in specific language clearly suggesting such rights.”). The phrase “hold harmless” likewise does not encompass advances. *Id.* The authorization applies only to those persons eligible for indemnification under Subsection (c), but the partnership agreement certainly can authorize a broader scope and can also make advances obligatory.

The reference to “ordinary course” pertains to Subsection (k) (stating that any “difference arising in the ordinary course of the business of the partnership may be decided by a majority of the partners”).

Subsection (e)—This subsection’s language is very broad and authorizes a partnership to purchase insurance to cover (*e.g.*, a partner’s intentional misconduct). It is unlikely that such insurance would be available. This authorization comes from the act, not the partnership agreement, and therefore is not subject to Section 105(c)(8) (precluding the partnership agreement from “reliev[ing] or exonerate[ing] a person from liability for conduct involving bad faith, willful or intentional misconduct, or knowing violation of law”).

Subsection (f)—This subsection was UPA (1997) § 401(d) and is based on UPA (1914) § 18(c).

Subsection (g)—This subsection was UPA (1997) § 401(c) and is based on UPA (1914) § 18(c).

Subsection (h)—This subsection was UPA (1997) § 401(f) and is based on UPA (1914) § 18(e). UPA (1997) § 401, comment 7, suggests that UPA (1914) § 18(e) case law continues to be relevant and notes that Section 18(e) “has been interpreted broadly to mean that, absent contrary agreement, each partner has a continuing right to participate in the management of the partnership and to be informed about the partnership business, even if, per the partnership agreement, the partner’s assent to partnership business decisions is not required.”

Note also that for some decisions this act requires the affirmative vote or consent of all partners. *See, e.g.*, Subsection (k) (“an act outside the ordinary course of business of a partnership and an amendment to the partnership agreement”); Section 402(b)(3) (becoming a partner after formation of the partnership).

The subsection has important implications for a partner’s actual authority to act on behalf of the partnership. The actual authority of a partner is a question of agency law and depends fundamentally on the contents of the partnership agreement. If, however, the partnership agreement is silent on the issue, this subsection helps delineate that actual authority. Acting individually, a partner:

- has no actual authority to commit the partnership to any matter for which this act requires the affirmative vote or consent of all partners;
- has the actual authority to commit the partnership to usual and customary matters, unless the partner has reason to know that: (i) other partners might disagree; or (ii) for some other reason consultation with fellow partners is appropriate; and

- has no actual authority to take unusual or non-customary actions that will have a substantial effect on the partnership.

The first point follows self-evidently from the language of this act. Where this act requires unanimity, no partner could reasonably believe to the contrary (unless the partnership agreement provided otherwise).

The second point follows because:

- Subsection (h) serves as the gap-filler manifestation from the partnership to its partners and does *not* require partners to act *only* in concert or after consultation. To the contrary, subject to the partnership agreement, this subsection expressly provides that “each partner has equal rights in the management and conduct of the partnership’s business.”
- It would be impractical to require collective action on even the smallest of decisions.
- However, to the extent a partner has reason to know of a possible difference of opinion among the partner, Subsection (k) requires a decision by at least “a majority of the partners” and by unanimous consent if the matter is “outside the ordinary course of the business.”

The third point is a matter of common sense. The more serious the matter, the less likely it is that a partner has actual authority to act unilaterally. *Cf.* RESTATEMENT (THIRD) OF AGENCY § 3.03, cmt. c (2006) (noting the unreasonableness of believing, without more facts, that an individual has “an unusual degree of unilateral authority over a matter fraught with enduring consequences for the institution” and stating that “[t]he gravity of the matter from the standpoint of the organization is relevant to whether a third party could reasonably believe that the manager has authority to proceed unilaterally”).

Finally, the authority granted by this subsection includes the authority to delegate. Delegation does not relieve the delegating partner or partners of their duties under Section 409. However, the fact of delegation is a fact relevant to any breach of duty analysis.

EXAMPLE: A partner personally handles all important paperwork for a partnership. The partner neglects to renew the fire insurance coverage on a building owned by the partnership, despite having received and read a warning notice from the insurance company. The building subsequently burns to the ground and is a total loss. The partner might be liable for breach of the duty of care under Section 409(c) (gross negligence).

EXAMPLE: A partner delegates responsibility for insurance renewals to the partnership’s office manager, and that manager neglects to renew the fire insurance coverage on the building. Even assuming that the office manager has been grossly negligent, the partner is not necessarily liable under Section 409(c). The office manager’s gross negligence is not automatically attributed to the partner. Under Section 409(c), the question is whether the partner was grossly negligent (or worse) in selecting the office manager, delegating insurance renewal matters to the office manager, and supervising the general manager after the delegation.

The partnership agreement may also provide for delegation and, subject to Section 105(c), may modify a partner's duties under Section 409 accordingly.

Subsection (i)—This subsection states directly what UPA (1914) § 25(2)(a) provides indirectly, through the “tenancy in partnership.” That tenancy reflected the aggregate view of partnership (in the extreme), stated management rights as property rights, and was eliminated by UPA (1997) 401(g). The Harmonization Project relocated the UPA (1997) provision into this subsection.

The substance of UPA (1997) § 401(i), which continued the substance of UPA (1914) § 18(g), now appears in Section 402(b)(3) (providing that no person can become a partner without the affirmative vote or consent of all partners).

Subsection (j)—This subsection (i) follows the default rule of UPA (1914) § 18(f) (providing that a partner is not entitled to remuneration for services performed, except in winding up the partnership); while (ii) expanding the exception to include any partner who undertakes winding up. “[R]easonable compensation” includes reimbursement for reasonable expenses. *Moran v. Willensky*, 339 S.W.3d 651, 663 (Tenn. Ct. App. 2010) (stating that “the winding up partner . . . [is] entitled to recover costs associated with the winding up process); *see also O'Reilly's Adm'r v. Brady*, 28 Ala. 530, 535 (1856) (holding that “the surviving partner is entitled, at least, to an allowance and deduction for ‘tavern bills,’ [sic] and ‘other expenses incurred’ ‘in the adjustment and settling up’ of the affairs of the partnership.”). Reasonable expenses include reasonable attorney's fees, even when the winding up partner has (rightfully) caused the partnership to sue one of the partners. *Moran*, 339 S.W.3d at 663 (“Because Mr. Willensky's capital account had a negative balance, Ms. Moran was well within her rights to sue him to make up that balance.”).

In UPA (1997), this subsection was Subsection (h). The Harmonization Project made no change except to relocate the provision.

Subsection (k)—UPA (1997) continued the allocation of management authority stated by UPA (1914) § 18(h), with one important clarification. UPA (1914) § 18(h) requires majority consent for ordinary matters and unanimous consent for amending the partnership but is silent regarding extraordinary matters. Courts have generally required the consent of all partners for those matters. *See, e.g., Paciaroni v. Crane*, 408 A.2d 946 (Del. Ch. 1989); *Thomas v. Marvin E. Jewell & Co.*, 440 N.W.2d 437 (Neb. 1989); *Duell v. Hancock*, 83 A.D.2d 762 (N.Y. 1981). UPA (1997) codified those cases in § 401(j). The Harmonization Project made no substantive change but relocated the provision to Subsection (k).

Other provisions of this act also contain default rules providing for unanimous consent. *E.g.*, Sections 402(b)(3) (for a person to become a partner), 504(c) (for compromising a person's obligation to make a contribution). In addition, absent a contrary provision in the partnership agreement, the transactions authorized under Article 11 each require unanimous consent.

SECTION 402. BECOMING PARTNER.

(a) Upon formation of a partnership, a person becomes a partner under Section 202(a).

(b) After formation of a partnership, a person becomes a partner:

- (1) as provided in the partnership agreement;
- (2) as a result of a transaction effective under [Article] 11; or
- (3) with the affirmative vote or consent of all the partners.

(c) A person may become a partner without:

- (1) acquiring a transferable interest; or
- (2) making or being obligated to make a contribution to the partnership.

Comment

This section was adopted in the 2011 and 2013 Harmonization amendments and changes UPA (1997) both in style and substance.

Subsection (b)(2)—Article 11 deals with entity transactions (*e.g.*, mergers and conversions). This reference is new, although UPA (1997) Article 9 did contemplate mergers and conversions.

Subsection (b)(3)—A partnership being a creature of contract, consent is determined on an objective basis (*i.e.*, contract law’s “reasonable person” standard). Depending on the terms of the partnership agreement, the partners’ manifestation of consent might involve detailed formalities, entirely informal activities, or anything in between. Moreover, the partnership agreement might reduce the quantum of consent necessary or shift the consent right to the management committee or managing partners.

A partnership being a voluntary association, a person cannot become a partner without manifesting consent to do so. That consent also is judged objectively.

Under Section 106(b), “[a] person that becomes a partner is deemed to assent to the partnership agreement,” and the agreement binds the partner regardless of whether the partner has actually indicated assent in any way.

Subsection (c)(1)—To accommodate business practices, this provision permits so-called “non-economic partners.”

SECTION 403. FORM OF CONTRIBUTION. A contribution may consist of property transferred to, services performed for, or another benefit provided to the partnership or

an agreement to transfer property to, perform services for, or provide another benefit to the partnership.

Comment

This section is derived from ULLCA (2006) § 402, was adopted as part of the 2011 and 2013 Harmonization amendments, is intentionally quite broad, and encompasses past, present, and promised benefits.

Partnership law and practice are in accord. *E.g.*, *Canet v. Gooch Ware Travelstead*, 917 F. Supp. 969, 974 (E.D.N.Y. 1996) (referring to “Travelstead’s acknowledged use of ‘sweat equity’ participations” in two projects); *In re Jones*, 445 B.R. 677, 717 (Bankr. N.D. Tex. 2011) (stating that “Ex-Mrs. Mullen essentially put ‘sweat equity’ (*i.e.*, the provision of modeling services and related consultation) into Simple Beaute and not a significant monetary investment”); *Tumminaro v. Tumminaro*, 556 N.E.2d 293, 299 (Ill. App. Ct. 1990) (“A partner’s contribution to the partnership may consist of ‘services, skill, know-how, or ‘sweat equity.’”) (quoting *Becker v. Killarney*, 532 N.E.2d 931 (Ill. App. Ct. 1988)).

This act does not contain a statute of frauds specifically applicable to promised contributions. Generally applicable statutes of fraud might apply, however. For example, a promise to contribute land to a partnership would be subject to the statute of frauds pertaining to land transfers. Likewise, a promise that by its terms requires performance that extends beyond one year from the making of the contract would be subject to the one-year provision of the statute of frauds. *See* the comment to Section 102(12).

SECTION 404. LIABILITY FOR CONTRIBUTION.

(a) A person’s obligation to make a contribution to a partnership is not excused by the person’s death, disability, termination, or other inability to perform personally.

(b) If a person does not fulfill an obligation to make a contribution other than money, the person is obligated at the option of the partnership to contribute money equal to the value of the part of the contribution which has not been made.

(c) The obligation of a person to make a contribution may be compromised only by the affirmative vote or consent of all the partners. If a creditor of a limited liability partnership extends credit or otherwise acts in reliance on an obligation described in subsection (a) without knowledge or notice of a compromise under this subsection, the creditor may enforce the obligation.

Comment

Subsection (a)—Under common law principles of impracticability, an individual’s death or incapacity will sometimes discharge a duty to render performance. RESTATEMENT (SECOND) OF CONTRACTS §§ 261 (Discharge by Supervening Impracticability), 262 (Death or Incapacity of Person Necessary For Performance) (1981). This subsection overrides those principles. Moreover, the reference to “perform personally” is not limited to individuals but rather may refer to any legal person (including an entity) that has a non-delegable duty.

Subsection (b)—This subsection is a statutory liquidated damage provision, exercisable at the option of the partnership, with the damage amount set according to the value of the promised, non-monetary contribution.

EXAMPLE: In order to become a partner, a person promises to contribute to the partnership various assets “free and clear,” which the partnership agreement values at \$150,000. In return for the person’s promise, and in light of the agreed value, the partnership admits the person as a partnership with a right to receive twenty-five percent of the partnership’s distributions.

However, the promised assets are subject to a security agreement, and, before the partner can contribute the assets, the secured party forecloses on the security interest and sells the assets at a public sale for \$75,000. Even if the \$75,000 reflects the actual fair market value of the assets, under this subsection the partnership has a claim against the partner for “money equal to the value of the part of the contribution which has not been made” – *i.e.*, \$150,000.

EXAMPLE: Same facts as the previous example, except that the public sale brings \$225,000. The limited liability company is neither obliged to invoke this subsection nor limited to the \$150,000. The LLC may instead sue for breach of the promise to make the contribution, asserting the \$225,000 figure as evidence of the actual loss suffered as a result of the breach.

Subsection (c)—The unanimity requirement expressed in the first sentence might indirectly benefit creditors, but the requirement is nonetheless a default rule and therefore may be varied in the partnership agreement. The right of each partner to consent is not a “right[] under this [act] of a person other than a partner.” *See* Section 105(c)(17) (preventing the partnership agreement from affecting such rights). In contrast, the right stated in the second sentence fits squarely within Section 105(c)(17) and therefore may not be varied by the partnership agreement.

SECTION 405. SHARING OF AND RIGHT TO DISTRIBUTIONS BEFORE DISSOLUTION.

(a) Any distribution made by a partnership before its dissolution and winding up must be

in equal shares among partners, except to the extent necessary to comply with a transfer effective under Section 503 or charging order in effect under Section 504.

(b) Subject to Section 701, a person has a right to a distribution before the dissolution and winding up of a partnership only if the partnership decides to make an interim distribution.

(c) A person does not have a right to demand or receive a distribution from a partnership in any form other than money. Except as otherwise provided in Section 806, a partnership may distribute an asset in kind only if each part of the asset is fungible with each other part and each person receives a percentage of the asset equal in value to the person's share of distributions.

(d) If a partner or transferee becomes entitled to receive a distribution, the partner or transferee has the status of, and is entitled to all remedies available to, a creditor of the partnership with respect to the distribution. However, the partnership's obligation to make a distribution is subject to offset for any amount owed to the partnership by the partner or a person dissociated as partner on whose account the distribution is made.

Comment

Past uniform unincorporated entity acts and many current limited liability company acts provide default rules for allocation of profits, and UPA (1997) even provides a default configuration for maintaining capital accounts. For the following reasons, this act, incorporating changes made by the Harmonization Project, provides a default rule only for rights to share in distributions:

- Capital accounts are maintained for one purpose, to determine how distributions will be made to partners. The rules for maintenance of capital accounts can be very complex. Generally, however, profits increase capital account balances (and increase the amounts that will be distributed to the partners) and losses reduce capital account balances (and reduce the amounts that will be distributed to the partners). If the statute has a simple default rule for how distributions are to be made to the partners, providing an additional set of default profit and loss allocation provisions and capital account rules will be, at best, duplicative and, at worse, inconsistent with the distribution rules.
- Some argue that capital account rules and profit and loss allocation provisions are necessary to comply with tax requirements. Tax income or loss is allocated to partners according to the partners' economic interests in the partnership, and these interests are based on distributions that would be made to partners on liquidation of the partnership.

By including default distribution provisions, the act includes the information necessary to make these tax determinations. To the extent the tax law allows partners to make further tax elections or satisfy alternative safe harbors, the partners may look to the tax law for guidance and include necessary provisions in their agreements.

Subsection (a)—The rule stated applies to redemptions as well as operating distributions but is a default rule in both contexts. *See* the comment to Section 102(4)(A).

Subsection (b)—Section 701 provides a default rule for buying out a person dissociated as a partner when the dissociation does not lead to dissolution of the partnership.

Subsection (d)—For the rights of partners and transferees that receive a distribution in the form of indebtedness, see Section 406(d).

SECTION 406. LIMITATIONS ON DISTRIBUTIONS BY LIMITED LIABILITY PARTNERSHIP.

(a) A limited liability partnership may not make a distribution, including a distribution under Section 806, if after the distribution:

(1) the partnership would not be able to pay its debts as they become due in the ordinary course of the partnership's business; or

(2) the partnership's total assets would be less than the sum of its total liabilities plus the amount that would be needed, if the partnership were to be dissolved and wound up at the time of the distribution, to satisfy the preferential rights upon dissolution and winding up of partners and transferees whose preferential rights are superior to the rights of persons receiving the distribution.

(b) A limited liability partnership may base a determination that a distribution is not prohibited under subsection (a) on:

(1) financial statements prepared on the basis of accounting practices and principles that are reasonable in the circumstances; or

(2) a fair valuation or other method that is reasonable under the circumstances.

(c) Except as otherwise provided in subsection (e), the effect of a distribution under subsection (a) is measured:

(1) in the case of a distribution as defined in Section 102(4)(A), as of the earlier of:

(A) the date money or other property is transferred or debt is incurred by the limited liability partnership; or

(B) the date the person entitled to the distribution ceases to own the interest or rights being acquired by the partnership in return for the distribution;

(2) in the case of any other distribution of indebtedness, as of the date the indebtedness is distributed; and

(3) in all other cases, as of the date:

(A) the distribution is authorized, if the payment occurs not later than 120 days after that date; or

(B) the payment is made, if the payment occurs more than 120 days after the distribution is authorized.

(d) A limited liability partnership's indebtedness to a partner or transferee incurred by reason of a distribution made in accordance with this section is at parity with the partnership's indebtedness to its general, unsecured creditors, except to the extent subordinated by agreement.

(e) A limited liability partnership's indebtedness, including indebtedness issued as a distribution, is not a liability for purposes of subsection (a) if the terms of the indebtedness provide that payment of principal and interest is made only if and to the extent that a payment of a distribution could then be made under this section. If the indebtedness is issued as a distribution, each payment of principal or interest is treated as a distribution, the effect of which

is measured on the date the payment is made.

(f) In measuring the effect of a distribution under Section 806, the liabilities of a dissolved limited liability partnership do not include any claim that has been disposed of under Section 807, 808, or 809.

Comment

Both this section and Section 407 were derived essentially from the Model Business Corporation Act section 6.40, and were added during the Harmonization Project. Both sections are necessary and appropriate because a limited liability partnership provides the partners a corporate-like liability shield. With the exception noted in the comment to Subsection (a)(2), the provisions of this section are non-waivable. Section 105(c)(17).

“Distribution” does not include “amounts constituting reasonable compensation for present or past service or payments made in the ordinary course of business under a bona fide retirement plan or other bona fide benefits program.” Section 102(4)(B).

Subsection (a)—Insolvency is a fundamental issue under this section, and this subsection provides two tests of insolvency. The tests are disjunctive; a distribution violates this section if after the distribution the LLP fails either of the tests. The subsection applies both to interim and liquidating distributions.

Solvency is also a fundamental issue under bankruptcy and fraudulent transfer law, which provide their own respective definitions of the concept.

Subsection (a)(2)—The reference to “preferential rights upon dissolution and winding up” is a default rule, because removing this protection for preferred partners or transferees is an *inter se* matter. *See* Section 105(d)(1)(B). The rest of the section is not subject to change in the partnership agreement. Section 105(c)(17).

Subsection (b)—This subsection states a standard of ordinary care, in contrast with the generally applicable standard stated in Section 409(c) (gross negligence).

Subsection (b)(2)—This alternative valuation provision is likely to be both useful and fair when the partnership has appreciated assets but for accounting purposes these assets are valued at book value less depreciation.

Subsection (c)—This subsection provides three alternative rules for determining the point(s) in time of as which to apply the solvency tests stated in Subsection (a). The timing depends on which of three categories encompasses a distribution: (i) a distribution in the nature of a redemption (regardless of whether the distribution includes a distribution of indebtedness); (ii) any distribution of indebtedness other than a distribution in the nature of a redemption; and (iii) any distribution that involves neither a redemption nor a distribution of indebtedness. A

requirement for additional solvency testing pertaining to distributions of indebtedness appears in Subsection (e).

Subsection (c)(1)—Section 102(4)(A) encompasses distributions in the nature of a redemption.

Subsection (c)(1)(A) and (B)—Under Subparagraph (A), any beginning of payment activity triggers the rule and sets the date as of when to apply the solvency tests. Under Subparagraph (B), the partnership's complete acquisition of the rights is necessary to trigger the rule.

Subsection (c)(2)—This provision states the general rule for distributions in the form of debt and which are not connected with a redemption.

Subsection (c)(3)—This provision states alternative rules for all distributions of money or property (*i.e.*, not debt). The measuring date depends on the length of time between the authorization and payment of the distribution.

Subsection (d)—For a related provision, characterizing as a creditor a person who has become entitled to receive a distribution, see Section 405(d).

Subsection (e)—This subsection contains two rules pertaining to indebtedness issued as part of a distribution and the Subsection (a) solvency tests. The first sentence states the sensible rule that indebtedness that is essentially subordinated to the solvency requirement (*i.e.*, not payable if making payment would transgress that requirement) is not counted in determining liabilities for purposes of the solvency tests. The second sentence applies the solvency tests to each payment of principal and interest on any indebtedness issued as a distribution, in addition to any previous testing required by Subsection (c)(1)(A) or (c)(2).

EXAMPLE: A limited liability partnership and one of its partners agree that the LLP will buy out the person's entire ownership interest in the LLP in return for a promissory note from the LLP, payable in installments. Under the redemption agreement: (i) on January 15 the person surrenders all its interests and rights and dissociates as a partner; and (ii) the LLP signs and delivers the note to the person on February 15. Under the note, payment of interest is due monthly beginning March 15, with a balloon payment of the principal due December 30.

Under Subsection (c)(1)(B), the solvency tests are applied as of January 15. Under Subsection (e), the solvency tests are again applied on the March 15, April 15, etc., and again on December 30.

Subsection (f)—The cited sections provide methods for extinguishing or limiting the debts of an LLP that is winding up its affairs and activities and thus any debt affected by any of the cited sections is irrelevant for purposes of solvency testing.

SECTION 407. LIABILITY FOR IMPROPER DISTRIBUTIONS BY LIMITED LIABILITY PARTNERSHIP.

(a) Except as otherwise provided in subsection (b), if a partner of a limited liability partnership consents to a distribution made in violation of Section 406 and in consenting to the distribution fails to comply with Section 409, the partner is personally liable to the partnership for the amount of the distribution which exceeds the amount that could have been distributed without the violation of Section 406.

(b) To the extent the partnership agreement of a limited liability partnership expressly relieves a partner of the authority and responsibility to consent to distributions and imposes that authority and responsibility on one or more other partners, the liability stated in subsection (a) applies to the other partners and not to the partner that the partnership agreement relieves of the authority and responsibility.

(c) A person that receives a distribution knowing that the distribution violated Section 406 is personally liable to the limited liability partnership but only to the extent that the distribution received by the person exceeded the amount that could have been properly paid under Section 406.

(d) A person against which an action is commenced because the person is liable under subsection (a) may:

(1) implead any other person that is liable under subsection (a) and seek to enforce a right of contribution from the person; and

(2) implead any person that received a distribution in violation of subsection (c) and seek to enforce a right of contribution from the person in the amount the person received in violation of subsection (c).

(e) An action under this section is barred unless commenced not later than two years after the distribution.

Comment

This section and Section 406 were derived essentially from Model Business Corporation Act section 6.40. The provisions of this section are non-waivable. Section 105(c)(17).

This section contemplates two categories of liability: liability of those who have authorized improper distributions (Subsection (a) – *i.e.*, the partners) and the liability of those who have received improper distributions (Subsection (c) – *i.e.*, partners and transferees). Neither dissociating as a partner nor ceasing to be a transferee affects liability previously incurred under this section.

The liability is to the LLP, not to the creditors of an insolvent LLP. *Weinstein v. Colborne Foodbotics, L.L.C.*, 302 P.3d 263, 268 (Colo. 2013); *Rev O, Inc. v. Woo*, 725 S.E.2d 45, 52 (N.C. Ct. App. 2012).

This section does not preclude or interfere with claims for fraudulent transfer. *See* the comment to Subsection (e).

Subsection (a)—The liability is not strict liability but rather attaches only to the extent a decision maker has failed to comply with the duties stated in Section 409. To the extent those duties have been permissibly revised by the partnership agreement, the revised standards apply to this subsection. *See* Section 406(b)(1) (permitting reasonable reliance on specified financial information).

Subsection (b)—*Compare* Section 407(b), *with* Section 105(d)(2) (generally permitting provisions of this type).

Subsection (c)—Actual knowledge is necessary to impose liability. Reason to know does not suffice. *Compare* Section 407(c), *with* Section 103(a), (b).

Subsections (c) and (d)(2)—Liability could apply to a person who receives a distribution under a charging order, but only if the person meets the knowledge requirement. That situation is very unlikely unless the person with the charging order is also a partner.

Subsection (e)—When the distribution is in the form of indebtedness, the distribution may occur on several different dates. *See* the comment to Section 406(e).

This statute of limitations applies only to actions “under this section” and does not affect claims under other applicable law, which most often is fraudulent transfer law. For a different approach, see Delaware Code Annotated title 6, section 15-309(c) (West 2013) (applying a three-year statute of limitations to claims “under this chapter or other applicable law”); New York Limited Liability Company section 508(c) (2013) (same). *But see, e.g., In re The Heritage Org.*,

L.L.C., 413 B.R. 438, 461 (Bankr. ND Tex. 2009) (invoking the Texas Uninform Fraudulent Act (TUFTA) to recover distributions made by a Delaware LLC headquartered in Texas; rejecting Delaware Code title 6, section 18-607(c) on choice of law grounds; stating that “the Delaware legislature cannot limit the reach of TUFTA”).

**SECTION 408. RIGHTS TO INFORMATION OF PARTNERS AND PERSONS
DISSOCIATED AS PARTNER.**

(a) A partnership shall keep its books and records, if any, at its principal office.

(b) On reasonable notice, a partner may inspect and copy during regular business hours, at a reasonable location specified by the partnership, any record maintained by the partnership regarding the partnership’s business, financial condition, and other circumstances, to the extent the information is material to the partner’s rights and duties under the partnership agreement or this [act].

(c) The partnership shall furnish to each partner:

(1) without demand, any information concerning the partnership’s business, financial condition, and other circumstances which the partnership knows and is material to the proper exercise of the partner’s rights and duties under the partnership agreement or this [act], except to the extent the partnership can establish that it reasonably believes the partner already knows the information; and

(2) on demand, any other information concerning the partnership’s business, financial condition, and other circumstances, except to the extent the demand or the information demanded is unreasonable or otherwise improper under the circumstances.

(d) The duty to furnish information under subsection (c) also applies to each partner to the extent the partner knows any of the information described in subsection (c).

(e) Subject to subsection (j), on 10 days’ demand made in a record received by a partnership, a person dissociated as a partner may have access to information to which the person

was entitled while a partner if:

- (1) the information pertains to the period during which the person was a partner;
- (2) the person seeks the information in good faith; and
- (3) the person satisfies the requirements imposed on a partner by subsection (b).

(f) Not later than 10 days after receiving a demand under subsection (e), the partnership in a record shall inform the person that made the demand of:

(1) the information that the partnership will provide in response to the demand and when and where the partnership will provide the information; and

(2) the partnership's reasons for declining, if the partnership declines to provide any demanded information.

(g) A partnership may charge a person that makes a demand under this section the reasonable costs of copying, limited to the costs of labor and material.

(h) A partner or person dissociated as a partner may exercise the rights under this section through an agent or, in the case of an individual under legal disability, a legal representative. Any restriction or condition imposed by the partnership agreement or under subsection (j) applies both to the agent or legal representative and to the partner or person dissociated as a partner.

(i) Subject to Section 505, the rights under this section do not extend to a person as transferee.

(j) In addition to any restriction or condition stated in its partnership agreement, a partnership, as a matter within the ordinary course of its business, may impose reasonable restrictions and conditions on access to and use of information to be furnished under this section, including designating information confidential and imposing nondisclosure and safeguarding obligations on the recipient. In a dispute concerning the reasonableness of a restriction under this

subsection, the partnership has the burden of proving reasonableness.

Comment

Subsections (a) and (c) derive from UPA (1997). The other subsections are derived from the ULPA (2001) § 401 (rights to information of general partners and former general partners) and were adopted as part of the 2011 and 2103 Harmonization amendments. The rules stated here might be termed “quasi-default rules”—subject to some change by the partnership agreement. *See* Section 105(c)(4) (prohibiting unreasonable restrictions on the information rights stated in this section).

Although the rights and duties stated in this section are extensive, they are not necessarily all-inclusive. This act’s statement of fiduciary duties is not exhaustive, *see* the comment to Section 409(a), and some cases characterize owners’ information rights as reflecting a fiduciary duty of those with management power. *E.g. Bakerman v. Sidney Frank Importing Co., Inc.*, No. Civ.A. 1844–N, 2006 WL 3927242, at *14 (Del. Ch. Oct. 16, 2006) (holding that an LLC manager owed “certain duties to members of the LLC” and stating that “[w]hen fiduciaries communicate with their beneficiaries in the context of asking the beneficiary to make a discretionary decision—such as whether to consent to a sale of substantially all the assets of an LLC—the fiduciary has a duty to disclose all material facts bearing on the decision at issue”) (citing *Loudon v. Archer-Daniels-Midland Co.*, 700 A.2d 135, 137 (Del. 1997)).

Subsection (a)—A general partnership is often a very informal organization. Accordingly, this subsection states a default-required location for any books and records a partnership may have but does not require that books and records be kept. Other law may so require, however—particularly tax law. This subsection applies to any books and records kept to satisfy other law.

Subsection (b)—This subsection states the rule pertaining to information memorialized in “any record maintained by the partnership.” For the meaning of “material” as applied to information, *see* Section 409(f), comment.

Subsections (c) and (d)—In appropriate circumstances, violation of either or both of these provisions might cause a court to enjoin or even rescind action taken by the partnership, especially when the violation has interfered with an approval or veto mechanism involving partner consent. *E.g., Blue Chip Emerald L.L.C. v. Allied Partners Inc.*, 299 A.D.2d 278, 279–80 (N.Y. App. Div. 2002) (invoking partnership law precedent as reflecting a duty of full disclosure and holding that “[a]bsent such full disclosure, the transaction is voidable”).

Subsection (c)—This subsection imposes a duty on the partnership, not the partners. However, a partner could be liable in damages if the partner were to: (i) breach a duty under Section 409 or the partnership agreement; and (ii) in doing so cause or suffer the partnership to breach the duty stated in this paragraph.

Subsection (c)(1)—This provision imposes an affirmative duty to volunteer information. However, given the assumption that each partner will be active in management, the obligation

ceases “to the extent the partnership can establish that it reasonably believes the partner already knows the information.”

In any event, the obligation is limited to information that is both material and known by the partnership. “Knowledge” is viewed subjectively (*i.e.*, actual knowledge). Section 103(a)(1). Materiality is viewed objectively. Thus, the duty applies to known, material information, even if the partnership does not know that the information is material.

A partnership will “know” what its partners know. Under Section 103(e), “[a] partner’s knowledge . . . of a fact relating to the partnership is effective immediately as knowledge of or notice to the partnership.” As to others acting or reasonably appearing to act on behalf of the partnership, common law agency rules will apply. RESTATEMENT (THIRD) OF AGENCY § 5.03 (2006) (Imputation of Notice of Fact to Principal).

Typically a partner’s duties are continuous, and therefore a partner’s right to information is not just transaction-specific. Ongoing managerial responsibilities require ongoing information—both periodically and *ad hoc* when a situation warrants.

For the meaning of “material” as applied to information, see Section 409(f), comment.

Subsection (c)(2)—Other law determines which party has the burden of proof as to the stated exception.

Subsection (d)—This subsection imposes a duty directly on each partner, “except to the extent the [partner] can establish that it reasonably believes [another] partner already knows the information.”

EXAMPLE: A partnership has two partners: each of which is regularly engaged in conducting the partnership’s activities; both of which are aware of and have regular access to all significant partnership records; and neither of which has special responsibility for or knowledge of any particular aspect of those activities or the relevant partnership records. Most likely, neither partner is obliged to draw the other general partner’s attention to information apparent in the partnership’s records.

EXAMPLE: Although a partnership has three partners, one is the managing partner with day-to-day responsibility for running the partnership’s activities. The other two meet periodically with the managing partner and together with that partner function in a manner analogous to a corporate board of directors. Most likely, the managing partner has a duty to draw the attention of the other partners to important information, even if that information would be apparent from a review of the partnership’s records.

Because this subsection imposes duties directly on partner, the duties are in the nature of a contractual obligation, and breach is a matter of strict liability. For example, it is no defense for a partner under this section to assert that, although the partner failed to furnish required information, the failure did not amount to gross negligence under Section 409(c).

Subsection (e)—Codifying the information rights of former owners began with UPA (1997) § 403(b).

For the additional information rights of the legal representative of a deceased partner, see Section 505.

Subsection (e)(1)—A person dissociated as a partner has information rights in that capacity only as to the period during which the person was a partner. To the extent that further information is accessible under Section 505(2) (providing access to the legal representative of a deceased partner), that access is limited both in purpose (“for purposes of settling the estate”) and in scope (“the rights the deceased partner had under Section 408”).

Subsection (e)(2)—A duty of good faith is needed here, because a person claiming access under this subsection is no longer a partner and is no longer subject to a partner’s obligation of good faith and fair dealing under Section 409(d). *See* Section 603(b)(2) (stating a person’s dissociation as a partner terminates as to subsequent events the person’s duties under Section 409, including the contractual obligation of good faith). *But see id.*, cmt (noting that the common law implied covenant will continue to be relevant if the partnership agreement provides continuing rights and obligations for a person dissociated as a partner).

In the context of Subsection (e)(2), “good faith” is properly understood to mean an honest belief that the request is made for a proper purpose. *Associated Indem. Corp. v. CAT Contracting, Inc.*, 964 S.W.2d 276, 285 (Tex. 1998) (holding that “‘good faith’ in the surety agreement before us refers to conduct which is honest in fact, free of improper motive or wilful ignorance of the facts at hand”); *Andrews v. Bible*, 812 S.W.2d 284, 288 (Tenn. 1991) (describing “subjective good faith” as “[a] pure heart but an empty head”) (quoting *Whittington v. Ohio River Co.*, 115 F.R.D. 201, 209 (E.D.Ky.1987)). Willful ignorance includes being an ostrich. “While ‘honesty’ may require no more than a pure heart, it is questionable that a pure heart can co-exist with closed eyes. It is not honest to close one’s eyes so as to maintain an empty head.” *J.R. Hale Contracting Co. v. United New Mexico Bank at Albuquerque*, 799 P.2d 581, 591 (NM 1990). *See also* UPA (1914) § (3)(1) (“A person has ‘knowledge’ of a fact within the meaning of this act not only when he has actual knowledge thereof, but also when he has knowledge of such other facts as in the circumstances shows bad faith.”).

Subsection (h)—For the avoidance of doubt, this subsection expressly authorizes taking action through an agent. The doubt might arise from old corporate cases in which the parties contested a shareholder’s right to exercise inspection rights through another person. *White v. Coeur D’Alene Big Creek Mining Co.*, 55 P.2d 720, 723 (Idaho 1936) (stating that “[t]he refusal to permit respondent [shareholder] to appoint his own attorney or agent to make the examination [of the corporation’s books] was in effect a denial of his right” of inspection); *State v. Monida & Yellowstone Stage Co.*, 124 N.W. 971, 972 (Minn. 1910) (upholding a trial court’s mandamus order, “which shall provide that [the shareholder complainant], or such attorney or agent as he may select, ... shall be allowed to inspect the books, records, and papers of the defendant [corporation]”).

No negative inference should be drawn about using agents to take other action under this

act.

Subsection (j)—This subsection provides fallback protection for gaps in the partnership agreement. For example, the partners may protect trade secrets from disclosure and prohibit various misuses of confidential information even if the partnership agreement omits to do so.

The reference to “ordinary course” pertains to Section 401(k) (stating that any “matter in the ordinary course of business of a partnership may be decided by a majority of the partners”). This approach is necessary, lest a requesting partner have the power to block imposition of a reasonable restriction or condition needed to prevent the requestor from abusing the partnership.

The burden of persuasion under this subsection contrasts with the burden of persuasion under Section 105(c)(4) (prohibiting unreasonable limitations on the information rights provided by this section). Under that paragraph, as a matter of ordinary procedural law the burden is on the person making the claim.

SECTION 409. STANDARDS OF CONDUCT FOR PARTNERS.

(a) A partner owes to the partnership and the other partners the duties of loyalty and care stated in subsections (b) and (c).

(b) The fiduciary duty of loyalty of a partner includes the duties:

(1) to account to the partnership and hold as trustee for it any property, profit, or benefit derived by the partner:

(A) in the conduct or winding up of the partnership’s business;

(B) from a use by the partner of the partnership’s property; or

(C) from the appropriation of a partnership opportunity;

(2) to refrain from dealing with the partnership in the conduct or winding up of the partnership business as or on behalf of a person having an interest adverse to the partnership; and

(3) to refrain from competing with the partnership in the conduct of the partnership’s business before the dissolution of the partnership.

(c) The duty of care of a partner in the conduct or winding up of the partnership business

is to refrain from engaging in grossly negligent or reckless conduct, willful or intentional misconduct, or a knowing violation of law.

(d) A partner shall discharge the duties and obligations under this [act] or under the partnership agreement and exercise any rights consistently with the contractual obligation of good faith and fair dealing.

(e) A partner does not violate a duty or obligation under this [act] or under the partnership agreement solely because the partner's conduct furthers the partner's own interest.

(f) All the partners may authorize or ratify, after full disclosure of all material facts, a specific act or transaction by a partner that otherwise would violate the duty of loyalty.

(g) It is a defense to a claim under subsection (b)(2) and any comparable claim in equity or at common law that the transaction was fair to the partnership.

(h) If, as permitted by subsection (f) or the partnership agreement, a partner enters into a transaction with the partnership which otherwise would be prohibited by subsection (b)(2), the partner's rights and obligations arising from the transaction are the same as those of a person that is not a partner.

Comment

This section originated as UPA (1997) § 404. The 2011 and 2013 Harmonization amendments made one major substantive change; they “un-cabined” fiduciary duty. UPA (1997) § 404 had deviated substantially from UPA (1914) by purporting to codify all fiduciary duties owed by partners. This approach had a number of problems. Most notably, the exhaustive list of fiduciary duties left no room for the fiduciary duty owed by partners to each other – *i.e.*, “the punctilio of an honor the most sensitive”). *Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928). Although UPA (1997) § 404(b) purported to state “[a] partner’s duty of loyalty to the partnership *and the other partners*” (emphasis added), the three listed duties each protected the partnership and not the partners.

“Un-cabining” harmonized this act to ULLCA (2006), and this section states some of the core aspects of the fiduciary duty of loyalty, provides a duty of care, and incorporates the contractual obligation of good faith and fair dealing. The duties stated in this section are subject to the partnership agreement, but Sections 105(c) and (d) contain important limitations on the

power of the partnership agreement to affect fiduciary and other duties and the obligation of good faith and fair dealing.

For the effect of dissociation on a person's duties under this section, see Section 603(b)(2).

Subsection (a)—This subsection recognizes two core managerial duties but, unlike UPA (1997), does not purport to be exhaustive. For example, many cases characterize a manager's duty to disclose as a fiduciary duty. *E.g.*, *Loneragan v. EPE Holdings, L.L.C.*, 5 A.3d 1008, 1023 (Del. Ch. 2010) (stating that “in the limited partnership context, absent contractual modification, a general partner owes fiduciary duties that include a duty of full disclosure”) (quotation marks omitted) (citation omitted); *Exxon Corp. v. Burglin*, 4 F.3d 1294, 1298 (5th Cir. 1993) (“Under Alaska law, a general partner stands in a fiduciary relationship with the limited partnership and thereby owes ‘a fiduciary duty . . . to disclose information concerning partnership affairs.’”) (quoting *Parker v. N. Mixing Co.*, 756 P.2d 881, 894 (Alaska 1988)).

Subsection (b)—This subsection states three core aspects of the fiduciary duty of loyalty: (i) not “usurping” partnership opportunities or otherwise wrongly benefiting from the partnership's operations or property; (ii) avoiding conflict of interests in dealing with the partnership (whether directly or on behalf of another); and (iii) refraining from competing with the partnership. Essentially the same duties exist in agency law and under the law of all types of business organizations.

This subsection applies beginning with “the partnership's business,” which by definition cannot exist before the partnership does; thus the stated duties do not apply to pre-formation activities.

The stated duties comprise a default rule. Under Section 105(d)(3)(A): “If not manifestly unreasonable, the partnership agreement may . . . alter or eliminate the aspects of the duty of loyalty stated in Section 409(b).”

Subsection (b)(1)—The phrase “hold as trustee” dates back to UPA (1914) § 21 and reflects the availability of disgorgement remedies, such as a constructive trust. In contrast to an actual trustee, a person subject to this duty does not: (i) face the special obstacles to consent characteristic of trust law; or (ii) enjoy protection for decisions taken in reliance on the governing instrument and other sources of information. *Cf.* Uniform Statutory Trust Entity Act (2009) (Last Amended 2013) § 506 (“A trustee [of a statutory trust]. . . is not liable to the trust or to a beneficial owner for breach of any duty, *including a fiduciary duty*, to the extent the breach results from reasonable reliance on: (i) a term of the governing instrument; (ii) a record of the statutory trust; or (iii) an opinion, report, or statement of another person that the person to which the opinion, report, or statement is made or delivered reasonably believes is within the other person's professional or expert competence and is made or delivered to the trustee”) (emphasis added).

Subsection (b)(1)(A)—This provision is consistent with a basic principle of agency law—namely, that an agent may not benefit at all from the performance of the agency unless the

principal consents. RESTATEMENT (THIRD) OF AGENCY § 8.06, cmt. c. (2006). Typically, however, the partnership agreement will legitimize particular benefits – *e.g.*, a management fee paid to a managing partner in addition to that partner’s share of distributions. Also, an agreed allocation of distributions takes those benefits outside the reach of this provision.

Subsection (b)(1)(B)—For the expansive meaning of “property,” see Section 102(16). The term includes confidential information.

Subsection (b)(1)(C)—This act does not specify what constitutes “a partnership opportunity,” but ample case law exists. *See, e.g., Triple Five of Minn., Inc. v. Simon*, 404 F.3d 1088, 1096 (8th Cir. 2005) (“An opportunity that is closely related to the entity’s existing or prospective line of business, would competitively advantage the partnership, and is one that the partnership has the financial ability, knowledge and experience to pursue is a partnership opportunity.”); *Knudson v. Kylo*, 831 N.W.2d 763, 767 (N.D. 2013) (explaining why conducting farming operations on land owned by others was a partnership opportunity while purchasing farmland was not).

The duty stated here continues through winding up, although in that context the scope of partnership opportunities inevitably narrows.

In most, if not all, situations, usurping a partnership opportunity also breaches the duty not to compete, Paragraph (b)(3), but not vice versa.

Subsection (b)(2)—In this context, the phrase “adverse interest” is a term of art, meaning “to be on the other side of the table” in some dealing with the partnership. Absent informed consent by the partnership, this duty is breached by the mere existence of the conflict of interest and the partnership need not prove that the outcome of the dealing was adverse to the partnership. *But see* Subsection (g) (permitting the defense of fairness). This duty continues through winding up.

Subsection (b)(3)—Although competition is often thought of in terms of potential customers, this duty applies equally to competition for resources, including employees. This duty ends when the partnership dissolves.

Subsection (c)—This act no longer refers to the duty of care as a fiduciary duty, because: (i) the duty of care applies in many non-fiduciary situations; and (ii) breach of the duty of care is remediable in damages while breach of a fiduciary duty gives rise also to equitable remedies, including disgorgement, constructive trust, and rescission.

The change in label is consistent with the Restatement (Third) of Agency section 8.02 (2006), which refers to the agent’s “fiduciary duty” to act loyally, but eschews the word “fiduciary” when stating the agent’s duties of “care, competence, and diligence.” *Id.* § 8.08. However, the label change is merely semantics; no change in the law is intended.

The partnership agreement can raise the standard of care, or subject to Sections 105(c)(8) and (d)(3)(C), lower it. A person’s practical exposure for breaching the duty of care involves not

only the standard of care but also any partnership agreement provision that: (i) exonerates the person from liability for breach of the duty of care, Section 105(c)(8); or (ii) entitles the person to indemnification despite such breach, Section 408(b), cmt.

Subsection (d)—This subsection refers to the “*contractual* obligation of good faith and fair dealing” (emphasis added) and thereby invokes the implied obligation that exists in every contract. *See* RESTATEMENT (SECOND) CONTRACTS § 205 (1981) (“Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.”). The adjective (“contractual”) should help avoid decisions like *Phelps v. Frampton*, 170 P.3d 474, 483 (Mont. 2007) (holding that Montana’s version of UPA (1997) creates a statutory obligation of good faith and fair dealing separate from the implied contractual covenant).

At first glance, it may seem strange to apply a contractual obligation to statutory duties and rights – *i.e.*, duties and rights “under this [act].” However, for the most part those duties and rights apply to relationships *inter se* the partners and the partnership and function only to the extent not displaced by the partnership agreement. Those statutory default rules are thus intended to function like a contract; applying the contractual notion of good faith and fair dealing therefore makes sense.

The contractual obligation of “good faith” has nothing to do with the corporate concept of good faith that for years bedeviled courts and attorneys trying to understand: (i) Delaware’s famous corporate law exoneration provision; and (ii) that provision’s exception “for acts or omissions not in good faith.” DEL. CODE ANN. tit. 8, § 102(b)(7) (2012). In that context, good faith is an aspect of the duty of loyalty. *See Stone ex rel. AmSouth Bancorporation v. Ritter*, 911 A.2d 362, 369–70 (Del. 2006).

Likewise, the contractual obligation of good faith and fair dealing has nothing to do with the “utmost good faith” sometimes used to describe the fiduciary duties that owners of closely held businesses owe each other. *See, e.g., Meinhard v. Salmon*, 477, 164 N.E. 545, 551 (NY 1928) (“[W]here parties engage in a joint enterprise each owes to the other the duty of the utmost good faith in all that relates to their common venture. Within its scope they stand in a fiduciary relationship.”); *Donahue v. Rodd Electrotpe Co. of New England, Inc.*, 328 N.E.2d 505, 515 (Mass. 1975) (“[S]tockholders in the close corporation owe one another substantially the same fiduciary duty in the operation of the enterprise that partners owe to one another. In our previous decisions, we have defined the standard of duty owed by partners to one another as the utmost good faith and loyalty.”) (footnotes omitted) (citations omitted) (internal quotations omitted).

To the contrary, the contractual obligation of good faith and fair dealing is not a fiduciary duty, does not command altruism or self-abnegation, and does not prevent a partner from acting in the partner’s own self-interest:

“Fair dealing” is not akin to the fair process component of entire fairness, *i.e.*, whether the fiduciary acted fairly when engaging in the challenged transaction as measured by duties of loyalty and care It is rather a commitment to deal “fairly” in the sense of consistently with the terms of the parties’ agreement and its purpose. Likewise “good faith” does not envision loyalty to the contractual

counterparty, but rather faithfulness to the scope, purpose, and terms of the parties' contract. Both necessarily turn on the contract itself and what the parties would have agreed upon had the issue arisen when they were bargaining originally.

Gerber v. Enter. Prods. Holdings, L.L.C., 67 A.3d 400, 418–19 (Del. 2013) (quoting *ASB Allegiance Real Estate Fund v. Scion Breckenridge Managing Member, L.L.C.*, 50 A.3d 434, 440–42 (Del. Ch. 2012), *aff'd in part, rev'd in part on other grounds*, 68 A.3d 665 (Del. 2013); *see also* Subsection (e)).

Courts should not use the contractual obligation to change *ex post facto* the parties' or this act's allocation of risk and power. To the contrary, the obligation should be used only to protect agreed-upon arrangements from conduct that is manifestly beyond what a reasonable person could have contemplated when the arrangements were made.

The partnership agreement or this act may grant discretion to a partner, and the contractual obligation of good faith and fair dealing is especially salient when discretion is at issue. However, a partner may properly exercise discretion even though another partner suffers as a consequence. Conduct does not violate the obligation of good faith and fair dealing merely because that conduct substantially prejudices a party. Indeed, parties allocate risk precisely because prejudice may occur.

The exercise of discretion constitutes a breach of the obligation of good faith and fair dealing only when the party claiming breach shows that the conduct has no honestly held purpose that legitimately comports with the parties' agreed-upon arrangements:

An implied covenant claim . . . looks to the past. It is not a free-floating duty unattached to the underlying legal documents. It does not ask what duty the law should impose on the parties given their relationship at the time of the wrong, but *rather what the parties would have agreed to themselves had they considered the issue in their original bargaining positions at the time of contracting.*

Gerber v. Enter. Prods. Holdings, L.L.C., 67 A.3d 400, 418 (Del. 2013) (quoting *ASB Allegiance Real Estate Fund v. Scion Breckenridge Managing Member, L.L.C.*, 50 A.3d 434, 440–42 (Del. Ch. 2012), *aff'd in part, rev'd in part on other grounds*, 68 A.3d 665 (Del. 2013)).

In sum, the purpose of the contractual obligation of good faith and fair dealing is to protect the arrangement the partners have chosen for themselves, not to restructure that arrangement under the guise of safeguarding it.

As to the power of the partnership agreement to affect the contractual obligation of good faith and fair dealing, see Section 105(c)(6) (prohibiting elimination but allowing the agreement to “prescribe standards, if not manifestly unreasonable, by which the performance of the obligation is to be measured”). For examples, see Section 105(c)(6), comment. As to whether the obligation stated in this subsection applies to the benefit of transferees, see Section 107(b), comment.

Subsection (e)—A partner in a general partnership has at least two different roles: (i) as a party to the partnership agreement, with rights and obligations under that agreement; and (ii) as co-manager of the enterprise. This provision pertains to the first role. A partner’s exercise of rights under the partnership agreement is subject to the obligation of good faith and fair dealing, Subsection (d), but a partner does not breach that contractual obligation “solely because the partner’s conduct furthers the partner’s own interest.” In contrast, this provision is ineffective with regard to a partner’s duties as co-manager. For example, a partner’s liability under Section 409(b)(3) (prohibiting competition) is not “solely because the partner’s conduct furthers the partner’s own interest.” Rather, the liability results from the breach of a specific obligation – *i.e.*, the codified aspect of the duty of loyalty that prohibits competition.

Subsection (f)—Here and elsewhere in this act, information “is material if there is a substantial likelihood that a reasonable [decision maker] would consider it important in deciding how to vote” or take other action under this act or the partnership agreements. *See Basic Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988) (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)).

The partnership agreement can provide additional or different methods of authorization or ratification, subject to the strictures of Section 105(c)(5), (d)(1), and (d)(3)(A)(B) and (D).

Subsection (g)—This subsection codifies judge-made law applicable to all business entities. *See, e.g., Kahn v. Lynch Commc’n Sys., Inc.*, 638 A.2d 1110, 1116 (Del. 1994) (discussing “entire fairness” in the context of a corporation’s merger with an affiliate); *Loneragan v. EPE Holdings, L.L.C.*, 5 A.3d 1008, 1019 (Del. Ch. 2010) (discussing “entire fairness” in the context of a limited partnership”); *Gottsacker v. Monnier*, 697 N.W.2d 436, 444 (Wis. 2005) (referring to “a willful failure to deal fairly with the LLC or its other members”).

Subsection (h)—This subsection is the modern, reformulated version of a language that sought to overturn the now-defunct notion that debts to partners were categorically inferior to debts to non-partner creditors. *See, e.g.,* ULPA (2001) § 112 (“A partner may lend money to and transact other business with the limited partnership and has the same rights and obligations with respect to the loan or other transaction as a person that is not a partner.”). The reformulation makes clear that this provision has nothing to do with the fiduciary duty pertaining to conflict of interests. *See BT-I v. Equitable Life Assurance Soc’y of the U.S.*, 75 Cal. App. 4th 1406, 1415 (Cal. Ct. App. 1999) (examining the prior formulation, explaining its history and stating “[w]e cannot discern anything in the purpose of [the prior formulation] that suggests an intent to affect a general partner’s fiduciary duty to limited partners”).

This subsection states a default rule. The partnership agreement may provide that debt to a partner (or partners generally) is subordinate to other partnership obligations. The agreement that creates the debt may do likewise.

SECTION 410. ACTIONS BY PARTNERSHIP AND PARTNERS.

(a) A partnership may maintain an action against a partner for a breach of the partnership

agreement, or for the violation of a duty to the partnership, causing harm to the partnership.

(b) A partner may maintain an action against the partnership or another partner, with or without an accounting as to partnership business, to enforce the partner's rights and protect the partner's interests, including rights and interests under the partnership agreement or this [act] or arising independently of the partnership relationship.

(c) A right to an accounting on dissolution and winding up does not revive a claim barred by law.

Comment

In UPA (1997) this section was Section 405. The Harmonization Project did not change the section other than to renumber it.

Subsection (a)—This subsection originated in UPA (1997) § 405(a) and reflects the entity theory of partnership.

Subsection (b)—This subsection is the successor to UPA (1914) § 22 but with significant changes.

UPA (1914) § 22 itself had made significant changes to the common law. “It . . . generally was established at common law that an equitable accounting was a condition precedent to an action in law between partners,” *Thompson v. Coughlin*, 997 P.2d 191, 194 (Or. 2000), and an accounting was generally not available before dissolution. Thus, claims among partners pertaining the partnership could not be asserted except through an action for dissolution and accounting. UPA (1914) § 22 modified this “exclusivity rule,” specifying certain circumstances in which an accounting action is available without requiring an action to dissolve the partnership.

UPA (1997) eliminated the “exclusivity rule” entirely; an action of dissolution and accounting remains available but is no longer “a condition precedent” to other claims.

This subsection authorizes a partner to bring claims “to enforce the partner's rights and protect the partner's interests” – *i.e.*, direct claims. The statutory language does not contemplate derivative claims; thus, this act neither authorizes nor precludes such claims. *See Tzolis v. Wolff*, 884 N.E.2d 1005 (N.Y. 2008) (rejecting the argument that “members of a limited liability company (LLC) may [not] bring derivative suits on the LLC's behalf, . . . [because] there are no provisions governing such suits in the Limited Liability Company Law”).

The case law does generally recognize the direct/derivative distinction in the context of general partnerships, and some cases permit a partner to sue derivatively. *E.g.*, *Hill v. Vanderbilt Capital Advisors, L.L.C.*, 834 F. Supp. 2d 1228, 1246 (D.N.M. 2011) (stating that “[t]he Supreme

Court of New Mexico extended the scope of derivative suits beyond the corporate context . . . and allowed a partner's derivative suit on behalf of a general partnership”) (citations omitted).

In general, however, the cases are conflicting and somewhat confused. A decision of the Maryland Court of Special Appeals illustrates the situation. At one point the court states:

We agree that the term “derivative” is an inappropriate and confusing term to use in the general partnership context. “Derivative” actions are necessary in the corporate and limited partnership context, where the shareholders and limited partners have no managerial rights and thus must “derive” the right to sue from the entity itself. Unlike shareholders and limited partners, however, general partners all have the ability to act on behalf of the partnership, and all have management rights [citations omitted]. Thus, general partners have no need for “derivative” action.

George Wasserman & Janice Wasserman Goldsten Family L.L.C. v. Kay, 14 A.3d 1193, 1215 (Md. Ct. Spec. App. 2011) (citing the comment to the UPA (1997) version of this section). However, later in the opinion the court recognizes that the partners’ “ability to act on behalf of the partnership, and . . . [the partners’] management rights” are ineffective when a partner with a controlling interest declines to cause the partnership to sue the controlling partner for alleged misconduct.

The court concludes that such a “partnership claim may be enforced by all of the *disinterested* partners.” *Wasserman*, 14 A.3d at 1216. In addition, the court cites with approval *Cates v. International Tel. & Tel. Corp.*, 756 F.2d 1161 (5th Cir.1985), which includes a lengthy discussion of circumstances in which a partner in a general partnership might be entitled to bring a derivative claim on behalf of the partnership. *Cates*, 756 F.2d at 1178 (referring to the possible “availability of a derivative action” but cautioning “[w]e do not hold that Texas law would *necessarily* allow a derivative action on the part of a minority partner”) (emphasis added).

Despite the conflict and confusion in the cases, one proposition does appear reasonably certain: A minority partner in a general partnership must have some right to sue “where the controlling partners, for improper, ulterior motives and not because of what they in good faith believe to be the best interests of the partnership, decline to sue on a valid, valuable *partnership cause of action* which it is advantageous to the partnership to pursue.” *Cates*, F.2d at 1179 (emphasis added).

Subsection (c)—This subsection originated as UPA (1997) § 405(c) and reversed the rule stated in UPA (1914) § 43. This subsection inevitably implies that other law governs the accrual of a claim under Subsection (b) as well as the statute of limitations applicable to those claims. As a result, partners must take care not to “sit on their claims” waiting for the partnership to dissolve. *Veloski v. State Farm Mut. Auto Ins. Co.*, 719 N.E.2d 574, 576 (Ohio Ct. App. 1998).

SECTION 411. CONTINUATION OF PARTNERSHIP BEYOND DEFINITE TERM OR PARTICULAR UNDERTAKING.

(a) If a partnership for a definite term or particular undertaking is continued, without an express agreement, after the expiration of the term or completion of the undertaking, the rights and duties of the partners remain the same as they were at the expiration or completion, so far as is consistent with a partnership at will.

(b) If the partners, or those of them who habitually acted in the business during the term or undertaking, continue the business without any settlement or liquidation of the partnership, they are presumed to have agreed that the partnership will continue.

Comment

This section originated as UPA (1997) § 406 and continues the approach of UPA (1997) (1914) § 23, with no substantive change.

Subsection (a)—Continuation beyond an agreed term or undertaking results in a partnership at will, not an automatic renewal of the term or extension of the undertaking. *See* the comment to Section 102(13 (partnership at will)).

Subsection (b)—In general, a pattern of conduct can imply a term in a partnership agreement. Section 102(12) (defining partnership agreement and referring to an agreement among all the partners, “whether oral, implied, in a record, or in any combination thereof”). In particular, this subsection creates a presumption that by their conduct the partners have agreed to continue the business. The presumption shifts the burden of persuasion to the person claiming that the partnership is dissolved.

[ARTICLE] 5

TRANSFERABLE INTERESTS AND RIGHTS

OF TRANSFEREES AND CREDITORS

SECTION 501. PARTNER NOT CO-OWNER OF PARTNERSHIP PROPERTY.

A partner is not a co-owner of partnership property and has no interest in partnership property which can be transferred, either voluntarily or involuntarily.

Comment

This section originated in UPA (1997), followed ineluctably from the concept of a partnership as an entity, Section 201, abolished the UPA (1914) construct of “partnership in tenancy,” and was retained during the Harmonization Project as a “belt and suspenders” approach to reinforcing the entity construct. *See* Section 203 (providing that property transferred to or otherwise acquired by the partnership is property of the partnership and not of the partners individually).

SECTION 502. NATURE OF TRANSFERABLE INTEREST. A transferable interest is personal property.

Comment

For the definition of transferable interest, see Section 102(23). Absent a contrary provision in the partnership agreement or the consent of the partners, a “transferable interest” is the only interest in a partnership that can be transferred to a person not already a partner. *See* Section 503. As to whether a partner may transfer governance rights to a fellow partner, the question is moot absent a provision in the partnership agreement changing the default rule, *see* Section 401(h) (allocating governance rights *per capita*). In the default mode, a partner’s transfer of governance rights to another partner: (i) does not increase the transferee’s governance rights; (ii) eliminates the transferor’s governance rights; (iii) and thereby changes the denominator but not the numerator in calculating governance rights.

EXAMPLE: LCN Company is a general partnership with three partners, Laura, Charles, and Nora. The partnership agreement does not displace this act’s default rule on the allocation of governance rights among general partners. Thus, each partner has 1/3 of those rights. Laura transfers her entire ownership interest to Charles. The transfer does not increase Charles’s governance rights but does eliminate Laura’s. After the transfer, Laura has no governance rights (regardless of whether Charles and Nora agree to expel Laura under Section 601(4)(B)). As a result, Charles and Nora each have 1/2 of the governance rights.

Whether a transferable interest pledged as security is governed by Article 8 or 9 of the Uniform Commercial Code depends on the rules stated in those Articles.

SECTION 503. TRANSFER OF TRANSFERABLE INTEREST.

(a) A transfer, in whole or in part, of a transferable interest:

(1) is permissible;

(2) does not by itself cause a person’s dissociation as a partner or a dissolution and winding up of the partnership business; and

(3) subject to Section 505, does not entitle the transferee to:

(A) participate in the management or conduct of the partnership's business; or

(B) except as otherwise provided in subsection (c), have access to records or other information concerning the partnership's business.

(b) A transferee has the right to:

(1) receive, in accordance with the transfer, distributions to which the transferor would otherwise be entitled; and

(2) seek under Section 801(5) a judicial determination that it is equitable to wind up the partnership business.

(c) In a dissolution and winding up of a partnership, a transferee is entitled to an account of the partnership's transactions only from the date of dissolution.

(d) A partnership need not give effect to a transferee's rights under this section until the partnership knows or has notice of the transfer.

(e) A transfer of a transferable interest in violation of a restriction on transfer contained in the partnership agreement is ineffective if the intended transferee has knowledge or notice of the restriction at the time of transfer.

(f) Except as otherwise provided in Section 601(4)(B), if a partner transfers a transferable interest, the transferor retains the rights of a partner other than the transferable interest transferred and retains all the duties and obligations of a partner.

(g) If a partner transfers a transferable interest to a person that becomes a partner with respect to the transferred interest, the transferee is liable for the partner's obligations under Sections 404 and 407 known to the transferee when the transferee becomes a partner.

Comment

One of the most fundamental characteristics of partnership law is its fidelity to the “pick your partner” principle. *See, e.g., Bynum v. Frisby*, 311 P.2d 972, 975 (Nev. 1957) (stating that (i) “the assignment of a partnership interest from one partner to a stranger does not bring that stranger into fiduciary relationship with the remaining partners”; and (ii) absent consent by the remaining partners “[t]he stranger remains a stranger” with no rights to management or even information). This section is the core of the act’s provisions reflecting and protecting that principle. A partner’s rights in a partnership are bifurcated into economic rights (the transferable interest) and governance rights (including management rights, consent rights, rights to information, rights to seek judicial intervention). Unless the partnership agreement otherwise provides, a partner acting without the consent of all other partners lacks both the power and the right to: (i) bestow partnership on a non-partner, Section 402(b)(3); or (ii) transfer to a non-partner anything other than some or all of the partner’s transferable interest, Section 503(a)(3). The rights of a mere transferee are quite limited (*i.e.*, to receive distributions), Section 503(b), and, if the partnership dissolves and winds up, to receive specified information pertaining to the partnership from the date of dissolution, Section 503(c).

This section applies regardless of whether the transferor is a partner, a transferee of a partner, a transferee of a transferee, etc. *See* Section 102(23) (defining “transferable interest” in terms of a right “initially owned by a person in the person’s capacity as a partner” regardless of “whether or not the person remains a partner or continues to own any part of the right”).

This section does not directly consider whether a partner may transfer governance rights to another partner without obtaining consent from all the other partners. As noted in Section 502, comment, the question is moot under this act’s default rule for allocating governance rights.

However, the question can be pivotal when the partnership agreement displaces the default rule on governance rights but does not determine whether transfer restrictions (whether contractual, statutory, or both) apply to transfers of governance rights from one partner to another. Case law is scant and pertains to limited liability companies. Nonetheless, the cases suggest that this act does not protect partners from control shifts that result from transfers among partners. *Blythe v. Bell*, No. 11 CVS 933, 2012 WL 7807800, at ¶ 6 (N.C. Dist. Dec. 10, 2012) (holding in a case of “first impression in North Carolina” that “in the absence of articles of incorporation or an operating agreement to the contrary . . . the assignment of control [*i.e.*, governance] interests between members is effective without unanimous member consent”); *Achaian, Inc. v. Leemon Family LLC*, 25 A.3d 800, 810 (Del. Ch. 2011) (Strine, Ch.) (holding that the terms of the LLC agreement did not preclude one member of a three-member LLC from transferring the member’s entire interest (including governance rights) to a second member without first having the consent of the third member; stating that the third member’s “argument relies on a very thinly sliced version of [the “pick-your-partner” principle, the strained version being] . . . that once one chooses his initial co-members, one continues to hold a veto over how much additional voting power they may acquire” explaining that “[t]he problem for [the third member] is that nothing in the LLC Agreement supports [that member’s] reading of it that would require an already admitted Member, like [the acquirer – *i.e.*, the second member], to become once, twice (or even three times) a Member each and every time that Member acquires an

additional block of Interests”).

Other law may affect the applicability of this section. *See* 11 U.S.C. § 541(c)(1) (providing that, initially at least, all property of a debtor becomes part of the bankruptcy estate regardless of restrictions on transfer); UCC §§ 9-406, 9-408 (overriding specified restrictions on assignment in specified circumstances, regardless of whether state law or a contract imposes the restrictions).

In any event, this section does not apply to the transfer of ownership interests in a partner that is an entity.

EXAMPLE: ABC, Partnership (“ABC”) has three partners: Ralph (an individual), Alice, Inc. (“Alice”), and Norton, LLC (“Norton”). Section 502 applies to any attempt by Ralph, Alice, or Norton to transfer their respective partnership interest in ABC. Section 502 is inapplicable, however, to a change in control of Alice or Norton or even a complete change in their respective ownership.

Subsection (a)—The definition of “transfer,” Section 102(22), and this subsection’s reference to “in whole or in part” combine to mean that this section encompasses not only unconditional, permanent, and complete transfers but also temporary, contingent, and partial ones. Thus, for example, a charging order under Section 504 effects a transfer of part of the judgment debtor’s transferable interest, as does the pledge of a transferable interest as collateral for a loan and the gift of a life-interest in a partner’s rights to distribution.

Subsection (a)(2)—The phrase “by itself” contemplates Section 601(4)(B), which creates a risk of dissociation via expulsion when a partner transfers all of the partner’s transferable interest.

Subsection (a)(3)—Mere transferees have no right to participate in management or otherwise intrude as the partners carry on the business of the partnership and their activities as partners.

Because Section 102(22)(G) defines “transfer” to include “a transfer by operation of law,” this section affects the power of other law to effect transfers of a partner’s ownership interest. For example, a divorce court lacks the power to award a partner’s spouse anything beyond the partner’s transferable interest. Nor does the partner have the power to enter into a property settlement purporting to effect any greater transfer.

For the divorce court, the best solution is to value the partner’s complete ownership interest (*i.e.*, the transferable interest as enhanced by the management and information rights and the standing to sue) and: (i) if possible, award the partner’s spouse marital property of equal value; or (ii) if not possible, award the partner’s spouse a money judgment and a charging order to enforce the judgment.

Granting the non-partner any part of a partner’s transferable interest is almost always imprudent; marital discord will almost inevitably carry over into the business relationship.

Granting the partner's ex-spouse the entire transferable interest is rarely a viable alternative. If the partner is active participant in the partnership, the approach is impossible. The partner's transferable interest will typically constitute much or all of the partner's remuneration for the partner's activity. Even if the partner is essentially passive, granting the transferable interest to the ex-spouse puts him or her at great risk as a "bare naked assignee." *See* the comment to Section 107(b).

When a partner dies, subject to the partnership agreement other law may effect a transfer of the partner's transferable interest to the partner's estate or personal representative. However, for the reasons just stated, other law lacks the power to transfer anything more than a transferable interest. (Section 505 does provide extra information rights for the purposes of settling the estate of the deceased partner.)

Subsection (a)(3)(B)—For a related provision, providing that that section's information rights do not apply to transferees, see Section 408(i).

Subsection (b)—Amounts due under this subsection are of course subject to offset for any amount owed to the partnership by the partner or person dissociated as a partner on whose account the distribution is made. Section 405(d). As to whether a partnership may properly offset for claims against a transferor that was never a partner is matter for other law, specifically the law of contracts dealing with assignments.

Subsection (c)—This very limited grant of information rights encompasses only transactions occurring at or after the date of the partnership's dissolution. The transferee has only the right to information as to the allocation of net assets among the partnership's creditors, partners, and transferees—and only from the date of dissolution.

This subsection does not prevent a transferee from contracting with a partner-transferor to require the partner-transferor to disclose further information to the transferee. Whether such an agreement would breach the partnership agreement, the implied contractual obligation of good faith and fair dealing, Section 409(d), or a fiduciary duty depends on the circumstances.

If a dissolved partnership rescinds its dissolution, Section 803, this subsection no longer applies.

Subsection (e)—This provision originated as UPA (1997) § 503(e), was then consistent with Uniform Commercial Code section 9-318(3), and is now consistent with section 9-406(a) (stating that "an account debtor . . . may discharge its obligation by paying the assignor until, but not after, the account debtor receives a notification, authenticated by the assignor or the assignee, that the amount due or to become due has been assigned and that payment is to be made to the assignee").

The term "notice" includes "reason to know," Section 103(b)(1), and ordinarily a potential transferee has reason to inquire about transfer restrictions that might be contained in the partnership agreement.

Subsection (f)—Under this subsection, a partner remains a partner (with all attendant

rights and obligations) even after permanently transferring the entirety of the transferable interest, unless: (i) the other partners opt for expulsion under Section 601(4)(B); or (ii) as otherwise provided in the partnership agreement.

SECTION 504. CHARGING ORDER.

(a) On application by a judgment creditor of a partner or transferee, a court may enter a charging order against the transferable interest of the judgment debtor for the unsatisfied amount of the judgment. A charging order constitutes a lien on a judgment debtor's transferable interest and requires the partnership to pay over to the person to which the charging order was issued any distribution that otherwise would be paid to the judgment debtor.

(b) To the extent necessary to effectuate the collection of distributions pursuant to a charging order in effect under subsection (a), the court may:

(1) appoint a receiver of the distributions subject to the charging order, with the power to make all inquiries the judgment debtor might have made; and

(2) make all other orders necessary to give effect to the charging order.

(c) Upon a showing that distributions under a charging order will not pay the judgment debt within a reasonable time, the court may foreclose the lien and order the sale of the transferable interest. The purchaser at the foreclosure sale obtains only the transferable interest, does not thereby become a partner, and is subject to Section 503.

(d) At any time before foreclosure under subsection (c), the partner or transferee whose transferable interest is subject to a charging order under subsection (a) may extinguish the charging order by satisfying the judgment and filing a certified copy of the satisfaction with the court that issued the charging order.

(e) At any time before foreclosure under subsection (c), a partnership or one or more partners whose transferable interests are not subject to the charging order may pay to the

judgment creditor the full amount due under the judgment and thereby succeed to the rights of the judgment creditor, including the charging order.

(f) This [act] does not deprive any partner or transferee of the benefit of any exemption law applicable to the transferable interest of the partner or transferee.

(g) This section provides the exclusive remedy by which a person seeking in the capacity of a judgment creditor to enforce a judgment against a partner or transferee may satisfy the judgment from the judgment debtor's transferable interest.

Comment

The charging order concept dates back to the English Partnership Act of 1890 and in the United States has been a fundamental part of law of unincorporated business organizations since 1914. *See* UPA (1914) § 28. As much a remedy limitation as a remedy, the charging order is the sole method by which a person acting as judgment creditor of a partner or transferee can extract value from the partner's or transferee's ownership interest in a partnership. *See* the comment to Subsection (g).

Under this section, the judgment creditor of a partner or transferee is entitled to a charging order against the relevant transferable interest. While in effect, that order entitles the judgment creditor to whatever distributions would otherwise be due to the partner or transferee whose interest is subject to the order. However, the judgment creditor has no say in the timing or amount of those distributions. The charging order does not entitle the judgment creditor to accelerate any distributions or to otherwise interfere with the management and activities of the partnership.

By its terms, this section does not apply to foreign partnerships. *See* Section 102(11) (defining "partnership" to mean "an association of two or more persons to carry on as co-owners a business for profit *formed under this [act]*") (emphasis added). *See also Fannie Mae v. Heather Apartments Ltd. P'ship*, A13-0562, 2013 WL 6223564, at *6 (Minn. Ct. App. Dec. 2, 2013) (considering the remedies available to a judgment creditor with respect to the judgment debtor's interest in a Cook Islands LLC; rejecting the debtor's argument that the creditor's "only remedy is to obtain a charging order under" the Minnesota LLC statute; explaining that "this argument fails because that statute only applies to Minnesota limited liability companies" which that statute "defines . . . as 'a limited liability company, other than a foreign limited liability company, *organized or governed by this chapter*'") (emphasis added) (statutory citations omitted).

The partnership agreement has no power to alter the provisions of this section to the prejudice of third parties. Section 105(c)(17).

Subsection (a)—The phrase “judgment debtor” encompasses both partners and transferees. The lien pertains only to a distribution, which excludes “amounts constituting reasonable compensation for present or past service or payments made in the ordinary course of business under a bona fide retirement plan or other bona fide benefits program.” Section 102(4)(B). A judgment creditor that wishes to levy on such amounts should use the appropriate creditor’s remedy, such as garnishment (which may be subject to exemptions or exclusions not relevant to a charging order). *Cf. PB Real Estate, Inc. v. Dem II Props.*, 719 A.2d 73, 76 (Conn. Ct. App. 1998) (rejecting the contention of an LLC’s two members that “payments of \$28,000 to each of them” should be treated “as expenses for wages” rather than as distributions).

Whether an application for a charging order must be served on the partnership, the judgment debtor, or both is a matter for other law, principally the law of remedies and civil procedure. The order itself must be served on the partnership. Whether the order must also be served on the judgment debtor is a matter for other law.

If a distribution consists of rights to acquire interests in a partnership, the charging order applies only to those rights within the definition of transferable interest. *See* Section 102(23) (defining transferable interest).

Subsection (b)—Paragraph (2) refers to “other orders” rather than “additional orders.” Therefore, given appropriate circumstances, a court may invoke Paragraph (1), Paragraph (2), or both.

Subsection (b)(1)—The receiver contemplated here is emphatically not a receiver for the partnership, but rather a receiver for the distributions subject to the charging order. The principal advantage provided by this paragraph is an expanded right to information. However, that right goes no further than “the extent necessary to effectuate the collections of distributions pursuant to a charging order.” For a correctly narrow reading of this provision, see *Wells Fargo Bank, Nat. Ass’n v. Continuous Control Solutions, Inc.*, No. 11–1285, 2012 WL 3195759 (Iowa Ct. App. Aug. 8, 2012).

Subsection (b)(2)—This paragraph must be understood in the context of: (i) the very limited nature of the charging order; and (ii) the importance of preventing overreaching on behalf of a person that is not a judgment creditor of the partnership, has no claim on the partnership’s assets, and has no right to interfere in the activities, affairs, and management of the partnership. In particular, the court’s power to make “all other orders” is limited to “orders necessary to give effect to the charging order.”

EXAMPLE: A judgment creditor with a charging order believes that the partnership should invest less of its surplus in operations, leaving more funds for distributions. The creditor moves the court for an order directing the partnership to restrict re-investment. Subsection (b)(2) does not authorize the court to grant the motion.

EXAMPLE: A judgment creditor with a judgment for \$10,000 against a partner obtains a charging order against the partner’s transferable interest. Having been properly served with the order, the partnership nonetheless fails to comply and makes a \$3000

distribution to the partner. The court has the power to order the partnership to pay \$3000 to the judgment creditor to “give effect to the charging order.”

Under Subsection (b)(2), the court has the power to decide whether a particular payment is a distribution, because that decision determines whether the payment is part of a transferable interest subject to a charging order.

EXAMPLE: Partner A of ABC, a general partnership, has for some years received distributions from the partnership. However, when a judgment creditor of Partner A obtains a charging order against Partner A’s transferable interest, the partnership ceases to make distributions to Partner A and instead provides a salary to Partner A equivalent to former distributions. A court might deem this salary a disguised distribution. (In any event, the salary will be subject to garnishment.)

This act has no specific rules for determining the fate or effect of a charging order when the partnership undergoes a merger, conversion, interest exchange, or domestication under Article 11. In the proper circumstances, such an organic change might trigger an order under Subsection (b)(2).

Subsection (c)—The phrase “that distributions under the charging order will not pay the judgment debt within a reasonable period of time” comes from case law. *See, e.g., Nigri v. Lotz*, 453 S.E.2d 780, 783 (Ga. Ct. App. 1995); *Stewart v. Lanier Park Med. Office Bldg., Ltd.*, 578 S.E.2d 572, 574 (Ga. Ct. App. 2003) (“Judicial sale may be appropriate where . . . it is apparent that distributions under the charging order will not pay the judgment debt within a reasonable amount of time.”). A purchaser at a foreclosure sale obtains only the very limited rights of a transferee under Section 503 and is in some ways more vulnerable and less powerful than the holder of a charging order. After foreclosure and sale, Subsection (b) no longer applies. More generally, the court is no longer involved in the matter. For the vulnerability of a transferee, see Sections 503(a)(3) comment; 107(b), comment.

Subsection (d)—This provision allows the judgment debtor to end the charging order without need for a hearing.

Subsection (e)—Traditionally, charging order provisions referred to the possibility of “redeeming” an interest subject to a charging order. That usage was confusing, leaving several important questions unanswered. This act substitutes a far simpler approach, contemplating the partnership or its partners buying the underlying judgment and thereby dispensing with any interference the judgment creditor might seek to inflict on the partnership.

In many circumstances, buying the judgment is superior to the mechanism provided by this subsection, because: (i) this subsection requires full satisfaction of the underlying judgment; and (ii) the partnership or the other partners might be able to buy the judgment for less than face value. On the other hand, this subsection operates without need for the judgment creditor’s consent, so it remains a valuable protection in the event a judgment creditor seeks to do mischief to the partnership.

Whether a partnership’s decision to invoke this subsection is “ordinary course” or “outside the ordinary course,” Section 401(k), depends on the circumstances. However, the involvement of this subsection does not by itself make the decision “outside the ordinary course.”

Subsection (f)—This subsection preserves otherwise applicable exemptions but does not create any. *In re Foos*, 405 B.R. 604, 609 (Bankr. N. D. Ohio 2009) (interpreting the comparable provision in UPA (1997) and stating that “it is clear that [the provision] does not create an exemption”).

Subsection (g)—This subsection does not override Uniform Commercial Code, Article 9, which may provide different remedies for a secured creditor acting in that capacity. A secured creditor with a judgment might decide to proceed under Article 9 alone, under this section alone, or under both Article 9 and this section. In the last-mentioned circumstance, the constraints of this section would apply to the charging order but not to the Article 9 remedies.

This subsection is not intended to prevent a court from effecting a “reverse pierce” where appropriate. In a reverse pierce, the court conflates the entity and its owner to hold the entity liable for a debt of the owner. *Litchfield Asset Mgmt. Corp. v. Howell*, 799 A.2d 298, 312 (Conn. App. Ct. 2002) (approving a reverse pierce where a judgment debtor had established a partnership in a patent attempt to frustrate the judgment creditor), *overruled on other grounds by, Robinson v. Coughlin*, 830 A.2d 1114 (Conn. 2003). Likewise, this subsection does not supplant fraudulent transfer law.

SECTION 505. POWER OF LEGAL REPRESENTATIVE OF DECEASED

PARTNER. If a partner dies, the deceased partner’s legal representative may exercise:

- (1) the rights of a transferee provided in Section 503(c); and
- (2) for purposes of settling the estate, the rights the deceased partner had under Section

408.

Comment

The estate and those claiming through the estate are transferees, and as such they have very limited rights to information. This section provides temporary, additional information rights to the legal representative of the estate. Sections 408 and 503(c) pertain only to information rights.

[ARTICLE] 6

DISSOCIATION

SECTION 601. EVENTS CAUSING DISSOCIATION. A person is dissociated as a partner when:

(1) the partnership knows or has notice of the person's express will to withdraw as a partner, but, if the person has specified a withdrawal date later than the date the partnership knew or had notice, on that later date;

(2) an event stated in the partnership agreement as causing the person's dissociation occurs;

(3) the person is expelled as a partner pursuant to the partnership agreement;

(4) the person is expelled as a partner by the affirmative vote or consent of all the other partners if:

(A) it is unlawful to carry on the partnership business with the person as a partner;

(B) there has been a transfer of all of the person's transferable interest in the partnership, other than:

(i) a transfer for security purposes; or

(ii) a charging order in effect under Section 504 which has not been foreclosed;

(C) the person is an entity and:

(i) the partnership notifies the person that it will be expelled as a partner because the person has filed a statement of dissolution or the equivalent, the person has been administratively dissolved, the person's charter or the equivalent has been revoked, or the person's right to conduct business has been suspended by the person's jurisdiction of formation;

and

(ii) not later than 90 days after the notification, the statement of dissolution or the equivalent has not been withdrawn, rescinded, or revoked, or the person's charter or the equivalent or right to conduct business has not been reinstated; or

(D) the person is an unincorporated entity that has been dissolved and whose activities and affairs are being wound up;

(5) on application by the partnership or another partner, the person is expelled as a partner by judicial order because the person:

(A) has engaged or is engaging in wrongful conduct that has affected adversely and materially, or will affect adversely and materially, the partnership's business;

(B) has committed willfully or persistently, or is committing willfully or persistently, a material breach of the partnership agreement or a duty or obligation under Section 409; or

(C) has engaged or is engaging in conduct relating to the partnership's business which makes it not reasonably practicable to carry on the business with the person as a partner;

(6) the person:

(A) becomes a debtor in bankruptcy;

(B) signs an assignment for the benefit of creditors; or

(C) seeks, consents to, or acquiesces in the appointment of a trustee, receiver, or liquidator of the person or of all or substantially all the person's property;

(7) in the case of an individual:

(A) the individual dies;

(B) a guardian or general conservator for the individual is appointed; or

(C) a court orders that the individual has otherwise become incapable of performing the individual's duties as a partner under this [act] or the partnership agreement;

(8) in the case of a person that is a testamentary or inter vivos trust or is acting as a partner by virtue of being a trustee of such a trust, the trust's entire transferable interest in the partnership is distributed;

(9) in the case of a person that is an estate or is acting as a partner by virtue of being a personal representative of an estate, the estate's entire transferable interest in the partnership is distributed;

(10) in the case of a person that is not an individual, the existence of the person terminates;

(11) the partnership participates in a merger under [Article] 11 and:

(A) the partnership is not the surviving entity; or

(B) otherwise as a result of the merger, the person ceases to be a partner;

(12) the partnership participates in an interest exchange under [Article] 11 and, as a result of the interest exchange, the person ceases to be a partner;

(13) the partnership participates in a conversion under [Article] 11;

(14) the partnership participates in a domestication under [Article] 11 and, as a result of the domestication, the person ceases to be a partner; or

(15) the partnership dissolves and completes winding up.

Comment

This section mostly states default rules, which the partnership agreement may vary. However, it makes no sense to vary some of the rules – *e.g.*, that the death of a partner who is an individual does *not* cause the individual's dissociation as a partner, Paragraph (7)(A), or that a entity remains a partner even *after* the existence of the entity has terminated, Paragraph (10).

Paragraph (1)—Partnership agreements often require notice of dissociation to be in

writing and to specify the effective date of the dissociation. The partnership cannot eliminate the power of a partner to dissociate by express will, Section 110(c)(9), but can eliminate the right and thereby make the dissociation wrongful.

Paragraph (3)—General partnership agreements often provide for “no cause” expulsion, and courts differ somewhat in how they approach such provisions. *Compare Gelder Med. Grp. v. Webber*, 363 N.E.2d 573, 576 (N.Y. 1977), with *Winston & Strawn v. Nosal*, 664 N.E.2d 239, 245 (Ill. App. Ct. 1996). See also the comment to Section 409(d) (stating and explaining the implied contractual covenant of good faith and fair dealing).

Paragraph (4)(B)—This paragraph permits expulsion when a partner no longer has any “skin in the game.” Although Article 7 provides for the buy-out of a dissociated partner’s transferable interest, in this context the dissociated partner has no transferable interest.

Paragraph (5)—For examples of conduct warranting an expulsion order, see *Della Ratta v. Dias*, 961 A.2d 629, 642 (Md. Ct. Spec. App. 2008), *aff’d*, 996 A.2d 382 (Md. 2010) (noting that “[t]he trial court expressly found that [two major capital] calls ‘were issued in bad faith’ . . . [and the] court also found that, ‘[by] another improper accounting movement’ in [the partnership], \$580,000 was taken ‘for executive office expenses which was improper’”); *Brennan v. Brennan Assocs.*, 977 A.2d 107, 117–18 (Conn. 2009) (referring to the expelled partner’s “moral turpitude, criminal fraud, and failure to be honest in court as to the extent of his criminal wrongdoing” as well as “his baseless claims of fraud” against a fellow partner; stating “he has rung the bell and it cannot be unring”).

For an analysis that helps distinguish Paragraph (5)(C) from Paragraphs (5)(A) and (B), see *All Saints University of Medicine Aruba v. Chilana*, A-2628-09T1, 2012 WL 6652510, at *15 (N.J. Super. Ct. App. Div. Dec. 24, 2012) (interpreting predecessor law and noting that the “not reasonably practicable standard” does not require a showing of wrongful conduct). Cf. *Dunnagan v. Watson*, 204 S.W.3d 30, 40 (Tex. Ct. App. 2006) (same issue in the context of dissolution).

Where grounds exist for both dissociation and dissolution, a court has the discretion to choose between the alternatives. *Robertson v. Jacobs Cattle Co.*, 830 N.W.2d 191, 201–02 (Neb. 2013). “[T]here is no textual basis for imposing a higher burden of proof for dissociation than dissolution.” *Brennan v. Brennan Assocs.*, 977 A.2d 107, 121 (Conn. 2009).

The partnership agreement cannot vary the stated grounds for expulsion, Section 105(c)(10), but can choose an alternate forum – e.g., arbitration. *Compare* Section 801(a)(4) (containing analogous grounds for dissolution by court order), with Section 105(c)(11) (making the Section 701(a)(4) grounds non-waivable).

Paragraph (6)(A)—This provision is subject to bankruptcy law. See, e.g., 11 U.S.C.A. § 365(e) (invalidating “ipso facto” clauses, subject to some exceptions).

Paragraphs (8) and (9)—A change in trustee or personal representative does not cause dissociation.

Paragraph (11)(A)—If a partnership disappears as part of a merger, no person can continue as a partner of the partnership. When the merger takes effect, those partners of the disappearing company are perforce dissociated. Depending on the plan of merger, those persons may become partners of a surviving partnership. In those circumstances, the merger will have dissociated them from one partnership and admitted them into partnership in the surviving partnership. *See* Sections 402(b)(2) and 1126(a)(10).

Paragraph (11)(B)—It is possible for a plan of merger to “shuffle the equity” of the surviving entity, even to the extent of “taking out” some or all of the owners of the surviving entity. A reverse triangular merger involving a partnership as the surviving entity would dissociate all the partners of the partnership.

Paragraph (13)—By definition, a partnership that converts ceases to be a partnership. *See* Section 1146. Thus, when the plan of conversion takes effect, all the partners of the converted entity are dissociated from that entity. In many cases, those persons will all be owners of the converted entity. In some cases, the conversion will “shuffle the equity” and “take out” some of the partners of the converting partnership.

Paragraph (14)—Domestication does not by itself dissociate a partner, because the domesticated entity remains both a partnership and “the same entity without interruption as the domesticating company.” Section 1156(a)(1)(B). However, an “equity shuffle” could dissociate a partner.

SECTION 602. POWER TO DISSOCIATE AS PARTNER; WRONGFUL DISSOCIATION.

(a) A person has the power to dissociate as a partner at any time, rightfully or wrongfully, by withdrawing as a partner by express will under Section 601(1).

(b) A person’s dissociation as a partner is wrongful only if the dissociation:

(1) is in breach of an express provision of the partnership agreement; or

(2) in the case of a partnership for a definite term or particular undertaking, occurs before the expiration of the term or the completion of the undertaking and:

(A) the person withdraws as a partner by express will, unless the withdrawal follows not later than 90 days after another person’s dissociation by death or otherwise under Section 601(6) through (10) or wrongful dissociation under this subsection;

(B) the person is expelled as a partner by judicial order under Section

601(5);

(C) the person is dissociated under Section 601(6); or

(D) in the case of a person that is not a trust other than a business trust, an estate, or an individual, the person is expelled or otherwise dissociated because it willfully dissolved or terminated.

(c) A person that wrongfully dissociates as a partner is liable to the partnership and to the other partners for damages caused by the dissociation. The liability is in addition to any debt, obligation, or other liability of the partner to the partnership or the other partners.

Comment

Subsection (a)—A general partnership is a voluntary association, *see* Section 105(c)(9), and voluntary in this context means “proceeding from the will or from one’s own choice or consent . . . having power of free choice.” BLACK’S LAW DICTIONARY (9th ed. 2009). Necessarily therefore, a general partner always has the power to dissociate by express will. Accordingly, the partnership agreement cannot vary this subsection except to the extent of requiring the notice of dissociation to be in writing. Section 105(c)(9).

The phrase “rightfully or wrongfully” reflects the distinction between a partner’s *power* to withdraw in contravention of the partnership agreement and a partner’s *right* to do so. Thus, although a partner cannot be enjoined from exercising the power to dissociate, the dissociation may be wrongful under Subsection (b).

Subsection (b)—This subsection list exhaustively (“only if”) the dissociations that are “wrongful.” The label has three consequences:

- under Subsection (c) liability for resulting damages, which, under Section 701(c), may be offset against the amount of the buyout price due to the partner under Section 701(a);
- under Section 701(h) postponement of payment of the buyout price until the term expires or the undertaking is completed; and
- under Section 804, exclusion from the winding up process, if the dissociation results in dissolution of the partnership.

This subsection states a default rule. The partnership agreement can expand the list (*e.g.*, by making wrongful a dissociation that breaches the implied contractual covenant of good faith and fair dealing). In theory, the partnership agreement can provide for liquidated damages (subject to the requirements of contract law) and, in theory, can also shrink or even eliminate the list of wrongful dissociations.

Subsection (b)(2)(A)—This paragraph protects a partner’s reactive withdrawal from a term partnership after the premature departure of another partner, such as the partnership’s rainmaker or main supplier of capital, under the same circumstances that may result in the dissolution of the partnership under Section 801(2)(A). Under that provision, a term partnership is dissolved ninety days after the bankruptcy, incapacity, death (or similar dissociation of a partner that is an entity), or wrongful dissociation of any partner, unless a majority in interest of the remaining partners agree to continue the partnership. Under this provision, a partner’s exercise of the right of withdrawal by express will under those circumstances is rendered “rightful,” even if the partnership is continued by others, and does not expose the withdrawing partner to damages for wrongful dissociation under Section 602(c).

Subsection (b)(2)(C)—This provision refers to Section 601(6), which involves *inter alia* dissociation on account of bankruptcy, which in turn is subject to bankruptcy law. *See, e.g.*, 11 U.S.C.A. § 365(e) (invalidating “ipso facto” clauses, subject to some exceptions).

Subsection (c)—A partner who prematurely dissociates from a partnership for an agreed term or undertaking risks liability for any resulting damages. For example, the partnership might incur substantial expenses in replacing the general partner’s expertise, reputation, or creditworthiness.

In effect, this subsection equates wrongful dissociation with breach of contract. Accordingly, courts should look to contract law to determine what consequential damages are recoverable. *See Hadley v. Baxendale*, 9 Exch. 341 (1854); RESTATEMENT (SECOND) OF CONTRACTS § 351 (1981); *see also Williams v. Hildebrand*, 247 S.W.2d 356, 358 (Ark. 1952) (interpreting UPA (1914) § 38(2)(a)(II), pertaining to wrongful dissolution, and stating that “the measure of damages, when the partnership was to have continued for a fixed term, is the profits that the injured partner would have received”).

SECTION 603. EFFECT OF DISSOCIATION.

(a) If a person’s dissociation results in a dissolution and winding up of the partnership business, [Article] 8 applies; otherwise, [Article] 7 applies.

(b) If a person is dissociated as a partner:

(1) the person’s right to participate in the management and conduct of the partnership’s business terminates, except as otherwise provided in Section 802(c); and

(2) the person’s duties and obligations under Section 409 end with regard to matters arising and events occurring after the person’s dissociation, except to the extent the partner participates in winding up the partnership’s business pursuant to Section 802.

(c) A person's dissociation does not of itself discharge the person from any debt, obligation, or other liability to the partnership or the other partners which the person incurred while a partner.

Comment

Subsection (a)—This subsection is a “switching” provision, invoking either Article 7 or 8 depending on whether a person's dissociation as a partner results in dissolution.

Subsection (b)—This section originated as UPA (1997) § 603(b) and deals with some of the internal effects of a person's dissociation as a partner.

Subsection (b)(1)—A person's dissociation as a partner ends immediately the person's right to participate in the management of the business, unless the dissociation results in dissolution of the partnership. *See* Section 802(c) (“A person whose dissociation as a partner resulted in dissolution may participate in winding up as if still a partner, unless the dissociation was wrongful.”).

Subsection (b)(2)—Unless a person's dissociation as a partner results in dissolution and the person participates in winding up, Section 802(c), this provision establishes a dividing line, separating out “matters arising and events occurring after the person's dissociation.” If the partnership has continuing projects with clients, ongoing relationships with clients, or both, the dividing line requires special attention with regard to non-competition and partnership opportunities duties. *See* Section 409(b)(1), (3).

Disputes involving law firms have generated much of the relevant case law. *See, e.g., Meehan v. Shaughnessy*, 535 N.E.2d 1255, 1257 (Mass. 1989); *Jewel v. Boxer*, 156 Cal. App. 3d 171, 175 (Cal. Ct. App. 1984). To a large extent a well-drawn partnership agreement can delineate the parties' respective rights and responsibilities and thereby avoid problems. However, if the partnership becomes insolvent, the bankruptcy court may well scrutinize the partners' *inter se* arrangements. *See Geron v. Robinson & Cole L.L.P.*, 476 B.R. 732, 743 (Bankr. S.D.N.Y. 2012) (considering whether a law firm had “fraudulently transferred . . . assets when its partners adopted the Jewel Waiver [releasing rights recognized by *Jewel v. Boxer*] on the eve of dissolution without consideration”).

This provision does not determine the effect of a person's dissociation as a partner on the person's future obligations or rights under the partnership agreement. Some contractual obligations typically extend beyond dissociation – *e.g.*, non-competition agreements, buyout arrangements. To the extent provisions of the partnership agreement continue to apply, the common law obligation of good faith continues to apply as well. *See* the comment to Section 409(d) (explaining that the subsection “invokes the implied obligation that exists in every contract” as a matter of common law).

Subsection (c)—A partner's obligation to safeguard trade secrets and other confidential

or proprietary information is incurred when the partner learns or otherwise obtains the information. This subsection preserves the obligation post-dissociation.

[ARTICLE] 7

PERSON'S DISSOCIATION AS A PARTNER WHEN BUSINESS NOT WOUND UP

SECTION 701. PURCHASE OF INTEREST OF PERSON DISSOCIATED AS PARTNER.

(a) If a person is dissociated as a partner without the dissociation resulting in a dissolution and winding up of the partnership business under Section 801, the partnership shall cause the person's interest in the partnership to be purchased for a buyout price determined pursuant to subsection (b).

(b) The buyout price of the interest of a person dissociated as a partner is the amount that would have been distributable to the person under Section 806(b) if, on the date of dissociation, the assets of the partnership were sold and the partnership were wound up, with the sale price equal to the greater of:

(1) the liquidation value; or

(2) the value based on a sale of the entire business as a going concern without the person .

(c) Interest accrues on the buyout price from the date of dissociation to the date of payment, but damages for wrongful dissociation under Section 602(b), and all other amounts owing, whether or not presently due, from the person dissociated as a partner to the partnership, must be offset against the buyout price.

(d) A partnership shall defend, indemnify, and hold harmless a person dissociated as a partner whose interest is being purchased against all partnership liabilities, whether incurred before or after the dissociation, except liabilities incurred by an act of the person under Section

702.

(e) If no agreement for the purchase of the interest of a person dissociated as a partner is reached not later than 120 days after a written demand for payment, the partnership shall pay, or cause to be paid, in money to the person the amount the partnership estimates to be the buyout price and accrued interest, reduced by any offsets and accrued interest under subsection (c).

(f) If a deferred payment is authorized under subsection (h), the partnership may tender a written offer to pay the amount it estimates to be the buyout price and accrued interest, reduced by any offsets under subsection (c), stating the time of payment, the amount and type of security for payment, and the other terms and conditions of the obligation.

(g) The payment or tender required by subsection (e) or (f) must be accompanied by the following:

- (1) a statement of partnership assets and liabilities as of the date of dissociation;
- (2) the latest available partnership balance sheet and income statement, if any;
- (3) an explanation of how the estimated amount of the payment was calculated;

and

(4) written notice that the payment is in full satisfaction of the obligation to purchase unless, not later than 120 days after the written notice, the person dissociated as a partner commences an action to determine the buyout price, any offsets under subsection (c), or other terms of the obligation to purchase.

(h) A person that wrongfully dissociates as a partner before the expiration of a definite term or the completion of a particular undertaking is not entitled to payment of any part of the buyout price until the expiration of the term or completion of the undertaking, unless the person establishes to the satisfaction of the court that earlier payment will not cause undue hardship to

the business of the partnership. A deferred payment must be adequately secured and bear interest.

(i) A person dissociated as a partner may maintain an action against the partnership, pursuant to Section 410(b)(2), to determine the buyout price of that person's interest, any offsets under subsection (c), or other terms of the obligation to purchase. The action must be commenced not later than 120 days after the partnership has tendered payment or an offer to pay or within one year after written demand for payment if no payment or offer to pay is tendered. The court shall determine the buyout price of the person's interest, any offset due under subsection (c), and accrued interest, and enter judgment for any additional payment or refund. If deferred payment is authorized under subsection (h), the court shall also determine the security for payment and other terms of the obligation to purchase. The court may assess reasonable attorney's fees and the fees and expenses of appraisers or other experts for a party to the action, in amounts the court finds equitable, against a party that the court finds acted arbitrarily, vexatiously, or not in good faith. The finding may be based on the partnership's failure to tender payment or an offer to pay or to comply with subsection (g).

Comment

Article 7 originated in UPA (1997) and provides for the buyout of the interest of a person dissociated as a partner if the dissociation does not result in a dissolution and winding up of the partnership's business under Article 8. *See* Section 603(a). If there is no dissolution, the remaining partners have a right to continue the business and the person dissociated as a partner has a right to be bought out. These rights can, of course, be varied in the partnership agreement. *See* Section 105. A person dissociated as a partner has a continuing relationship with the partnership and third parties as provided in Sections 603(b), 702, and 703. *See* Section 408(e) (access to information of person dissociated as a partner).

The rules in this section are merely default rules. The partners may, in the partnership agreement, fix the method or formula for determining the buyout price and all of the other terms and conditions of the buyout right. Indeed, the very right to a buyout itself may be modified, although a provision providing for a complete forfeiture would probably not be enforceable. *See* Section 119 (Supplemental Principles of Law).

Subsection (a)—This subsection provides that, if a person’s dissociation as a partner does not result in a windup of the business, the partnership shall cause the interest of the dissociating partner to be purchased for a buyout price determined pursuant to Subsection (b). The buyout is mandatory, unless the partnership provides otherwise. The “cause to be purchased” language is intended to accommodate a purchase by the partnership, one or more of the remaining partners, or a third party.

Subsection (b)—This subsection provides how the “buyout price” is to be determined. The terms “fair market value” or “fair value” were not used because they are often considered terms of art having a special meaning depending on the context, such as in tax or corporate law. “Buyout price” was a new term in UPA (1997). Under Subsection (b), the buyout price is the amount that would have been distributable to the dissociating partner under Section 807(b) if, on the date of dissociation, the assets of the partnership were sold at a price equal to the greater of liquidation value or going concern value without the departing partner. Liquidation value is not intended to mean distress sale value. Under general principles of valuation, the hypothetical selling price in either case should be the price that a willing and informed buyer would pay a willing and informed seller, with neither being under any compulsion to deal. The notion of a minority discount in determining the buyout price is negated by valuing the business as a going concern. Other discounts, such as for a lack of marketability or the loss of a key partner, may be appropriate, however. For a case applying the concept, see *Fotouhi v. Mansdorf*, 427 B.R. 798, 803–05 (Bankr. N.D. Cal. 2010)

Since the buyout price is based on the value of the business at the time of dissociation, the partnership must pay interest on the amount due from the date of dissociation until payment to compensate the dissociating partner for the use of his interest in the firm. Under UPA (1914) § 42, the person dissociated as a partner could elect a share of the profits in lieu of interest. UPA (1997) eliminated that option.

UPA (1914) § 38(2)(c)(II) provides that the good will of the business not be considered in valuing a wrongfully dissociating partner’s interest. UPA (1997) implicitly rejected that approach. Under this section, unless the partnership’s goodwill is damaged by the wrongful dissociation, the value of the wrongfully dissociating partner’s interest will include any goodwill value of the partnership. If the firm’s goodwill is damaged, the amount of the damages suffered by the partnership and the remaining partners will be offset against the buyout price.

Subsection (c)—This subsection provides that the partnership may offset against the buyout price all amounts owing by the person dissociated as a partner to the partnership, whether or not presently due, including any damages for wrongful dissociation under Section 602(c). This rule has the effect of accelerating payment of amounts not yet due from the former partner to the partnership, including a long-term loan by the partnership to the former partner. Where appropriate, the amounts not yet due should be discounted to present value. A dissociating partner, on the other hand, is not entitled to an add-on for amounts owing to him by the partnership. Thus, a departing partner who has made a long-term loan to the partnership must wait for repayment, unless the terms of the loan agreement provide for acceleration upon dissociation.

The partnership's right of setoff does not limit the amount of damages the partnership may claim for the wrongful dissociation and does not alter any other amounts owed to the partnership. Those amounts may result in a net sum due to the partnership from the person dissociated as a partner.

Subsection (d)—Following the rule stated in UPA (1914) § 38, this section requires the partnership to indemnify a person dissociated as a partner against all partnership liabilities, whether incurred before or after the dissociation, except those incurred by the person under Section 702. The rationale for covering post-dissociation liabilities is the fact of dissociation; the person dissociated as a partner is no longer a co-owner of the enterprise. As for pre-existing liabilities, the determination of the buyout price necessarily assumes that these liabilities will be paid. Thus, in effect the person's share of these liabilities has already been paid through the valuation process.

Subsection (e)—If a person dissociated as a partner makes a written demand for payment and no agreement for the purchase of the interest is reached within 120 days after the demand, the partnership must pay, or cause to be paid, in cash the amount it estimates to be the buyout price, adjusted for any offsets allowed and accrued interest. Thus, the person dissociated as a partner will receive in cash within 120 days of dissociation the undisputed minimum value of the person's partnership interest. If the person claims that the buyout price should be higher, suit may thereafter be brought as provided in Subsection (i) to have the amount of the buyout price determined by the court. This is similar to the procedure for determining the value of dissenting shareholders' shares under the Model Business Corporation Act §§ 13.20–13.28.

The “cause to be paid” language of Subsection (a) is repeated here to permit either the partnership, one or more of the continuing partners, or a third-party purchaser to tender payment of the estimated amount due.

Subsection (f)—Under this subsection, when deferred payment is authorized in the case of a wrongfully dissociating partner, a written offer stating the amount the partnership estimates to be the purchase price should be tendered within the 120-day period, even though actual payment of the amount may be deferred, possibly for many years. *See* the comment to Subsection (h). The dissociated partner is entitled to know at the time of dissociation what amount the remaining partners think is due, including the estimated amount of any damages allegedly caused by the partner's wrongful dissociation that may be offset against the buyout price.

Subsection (g)—This subsection provides that the payment of the estimated price (or tender of a written offer under Subsection (f)) by the partnership must be accompanied by: (i) a statement of the partnership's assets and liabilities as of the date of the person's dissociation as a partner; (ii) the latest available balance sheet and income statement, if the partnership maintains such financial statements; (iii) an explanation of how the estimated amount of the payment was calculated; and (iv) a written notice that the payment will be in full satisfaction of the partnership's buyout obligation unless the person dissociated as a partner commences an action to determine the price within 120 days of the notice. Subsection (g) is based in part on the

dissenters' rights provisions of Model Business Corporation Act Section 13.25(b).

Those disclosures should serve to identify and narrow substantially the items of dispute between the person dissociated as a partner and the partnership over the valuation of the partnership interest. The disclosures will also serve to pin down the parties as to their claims of partnership assets and values and as to the existence and amount of all known liabilities. Lastly, the disclosures will force the remaining partners to consider thoughtfully the difficult and important questions as to the appropriate method of valuation under the circumstances, and in particular, whether they should use going concern or liquidation value. Simply getting that information on the record in a timely fashion should increase the likelihood of a negotiated resolution of the parties' differences during the 120-day period within which the person dissociated as a partner must bring suit.

Subsection (h)—UPA (1914) § 38 contemplates a buyout in the context of the partnership business being continued after a partner's wrongful dissociation has (inevitably) caused dissolution. UPA (1914) § 38(2)(c) entitles the wrongfully dissociating partner to have the buyout price "paid to him in cash, or the payment secured by bond approved by the court." UPA (1997) took a different approach, which the Harmonization Project did not change. Under Subsection (h), a wrongfully dissociating partner is not entitled to receive any portion of the buyout price before the expiration of the term or completion of the undertaking, unless the person dissociated as a partner establishes to the satisfaction of the court that earlier payment will not cause undue hardship to the business of the partnership.

Subsection (i)—This subsection provides that a person dissociated as a partner may maintain an action against the partnership to determine the buyout price, any offsets, or other terms of the purchase obligation. The action must be commenced within 120 days after the partnership tenders payment of the amount it estimates to be due or, if deferred payment is authorized, its written offer. This provision creates a 120-day "cooling off" period. It also allows the parties an opportunity to negotiate their differences after disclosure by the partnership of its financial statements and other required information.

If the partnership fails to tender payment of the estimated amount due (or a written offer, if deferred payment is authorized), the person dissociated as a partner has one year after written demand for payment in which to commence suit.

SECTION 702. POWER TO BIND AND LIABILITY OF PERSON

DISSOCIATED AS PARTNER.

(a) After a person is dissociated as a partner without the dissociation resulting in a dissolution and winding up of the partnership business and before the partnership is merged out of existence, converted, or domesticated under [Article] 11, or dissolved, the partnership is bound by an act of the person only if:

(1) the act would have bound the partnership under Section 301 before dissociation; and

(2) at the time the other party enters into the transaction:

(A) less than two years has passed since the dissociation; and

(B) the other party does not know or have notice of the dissociation and reasonably believes that the person is a partner.

(b) If a partnership is bound under subsection (a), the person dissociated as a partner which caused the partnership to be bound is liable:

(1) to the partnership for any damage caused to the partnership arising from the obligation incurred under subsection (a); and

(2) if a partner or another person dissociated as a partner is liable for the obligation, to the partner or other person for any damage caused to the partner or other person arising from the liability.

Comment

A person's dissociation as a partner ends immediately the person's actual authority to act for the partnership, unless the dissociation results in a dissolution and winding up of the business of the partnership. *See* Section 603(b)(1). However, the person's apparent authority may linger.

This section does not affect a person's power to bind a partnership in another capacity – *e.g.*, as an employee with actual authority.

Subsection (a)—This subsection codifies and constrains the lingering apparent authority of a person dissociated as a partner. The constraint is in the phrase “only if.”

The provision applies until the partnership dissolves or under Article 11 ceases to be governed by this act. Once a partnership dissolves, Section 804 applies.

With respect to authority of a person dissociated as a partner to transfer partnership real property, Section 303(e) provides that third parties are deemed to have knowledge of a limitation on the person's authority to transfer real property held in the partnership name upon the proper recording of a statement containing such a limitation. Section 704(b) provides that a statement of dissociation operates as a limitation on the person's authority for the purposes of Section 303(e).

Thus, a properly recorded statement of dissociation provides, immediately upon recording, constructive knowledge of the lack of authority of a person dissociated as a partner to transfer real property held in the partnership name.

Subsection (a)(1)—It is the statutory apparent authority from Section 301 which lingers.

Subsection (a)(2)(A)—In any event, any lingering apparent authority ends two years after the dissociation.

Subsection (a)(2)(B)—A person might have notice under Section 103(d)(2)(A) (statement of dissociation) as well as under Section 103(b)(1) (person “ha[ving] reason to know the fact from all the facts known to the person at the time in question”).

Subsection (b)—The liability stated in this subsection is not exhaustive. For example, if a person dissociated as a partner causes a partnership to be bound under Subsection (a) and, due to a guaranty, some other person—not a partner nor a person dissociated as a partner—is liable on the resulting obligation, that other person may have a claim under other law against the person dissociated as a partner.

SECTION 703. LIABILITY OF PERSON DISSOCIATED AS PARTNER TO OTHER PERSONS.

(a) Except as otherwise provided in subsection (b), a person dissociated as a partner is not liable for a partnership obligation incurred after dissociation.

(b) A person that is dissociated as a partner is liable on a transaction entered into by the partnership after the dissociation only if:

(1) a partner would be liable on the transaction; and

(2) at the time the other party enters into the transaction:

(A) less than two years has passed since the dissociation; and

(B) the other party does not have knowledge or notice of the dissociation and reasonably believes that the person is a partner.

(c) By agreement with a creditor of a partnership and the partnership, a person dissociated as a partner may be released from liability for a debt, obligation, or other liability of the partnership.

(d) A person dissociated as a partner is released from liability for a debt, obligation, or other liability of the partnership if the partnership’s creditor, with knowledge or notice of the person’s dissociation but without the person’s consent, agrees to a material alteration in the nature or time of payment of the debt, obligation, or other liability.

Comment

To the extent a partnership has been a limited liability partnership throughout its existence, the liability rules stated in this section are moot. *See* Subsection (b)(1).

This section parallels Section 805.

Subsection (a)—As stated in Section 306(b), comment and 306(c), comment, other law determines when a partnership obligation is “incurred.”

Subsection (b)—The rule stated here for the “lingering liability” of a person dissociated a partner parallels the rule stated in Section 702 for the lingering apparent authority of a person dissociated as a partner.

Subsection (b)(2)(A)—In any event, the lingering liability ends two years after the dissociation.

Subsection (b)(2)(B)—A person might have notice under Section 103(d)(2)(A) (statement of dissociation) as well as under Section 103(b)(1) (person “ha[ving] reason to know the fact from all the facts known to the person at the time in question”).

Subsections (c) and (d)—These provisions trace back to UPA (1914) § 36(2), (3).

SECTION 704. STATEMENT OF DISSOCIATION.

(a) A person dissociated as a partner or the partnership may deliver to the [Secretary of State] for filing a statement of dissociation stating the name of the partnership and that the person has dissociated from the partnership.

(b) A statement of dissociation is a limitation on the authority of a person dissociated as a partner for the purposes of Section 303.

Comment

A partnership and a person dissociated as a partner each have the right (but not an

obligation) to deliver to the filing office a statement of dissociation, and each has an incentive to do so. *See* Sections 702(a)(2)(B) (extinguishing the lingering apparent authority of a person dissociated as a partner as to any party that has notice of the dissociation), 703(b)(2)(B) (extinguishing the lingering liability of a person dissociated as a partner as to any party that has notice of the dissociation).

This section originated as UPA (1997) § 704 and was unchanged by the Harmonization Project.

Subsection (a)—“A person not a partner is deemed . . . to have notice of a person’s dissociation as a partner 90 days after a statement of dissociation under Section 704 becomes effective.” Section 103(d)(2)(A). This constructive notice ends both the lingering apparent authority and lingering liability exposure of the person dissociated as a partner. *See* Sections 702(a)(2)(B), 703(b)(2)(B).

Subsection (b)—This subsection interrelates a statement of dissociation with the act’s intricate section on statements of authority. *See* Section 303.

SECTION 705. CONTINUED USE OF PARTNERSHIP NAME. Continued use of a partnership name, or the name of a person dissociated as a partner as part of the partnership name, by partners continuing the business does not of itself make the person dissociated as a partner liable for an obligation of the partners or the partnership continuing the business.

Comment

Section 705 originated in UPA (1997) and is an edited version of UPA (1914) § 41(10). The section merely protects a person dissociated as a person from liability in case the partnership continues to use the person’s name. Whether a partnership has a right to the continued use is a matter for the partnership agreement; this act states no rule on the subject.

If the partnership agreement does not expressly address the issue, custom may imply a term. *See Gignilliat v. Gignilliat, Savitz & Bettis, L.L.P.*, 684 S.E.2d 756, 762, n.6 (S.C. 2009) (“This Court takes judicial notice of the custom and practice in this state of law firms continuing to use the names of deceased members in their firm names. Heretofore, the basis has been the taking for granted that the deceased partner would consent. Hereafter, it is presumed, unless proven otherwise, that the deceased partner consented to the continued use of his or her name in the partnership’s name.”).

[ARTICLE] 8

DISSOLUTION AND WINDING UP

SECTION 801. EVENTS CAUSING DISSOLUTION. A partnership is dissolved, and its business must be wound up, upon the occurrence of any of the following:

(1) in a partnership at will, the partnership knows or has notice of a person's express will to withdraw as a partner, other than a partner that has dissociated under Section 601(2) through (10), but, if the person has specified a withdrawal date later than the date the partnership knew or had notice, on the later date;

(2) in a partnership for a definite term or particular undertaking:

(A) within 90 days after a person's dissociation by death or otherwise under Section 601(6) through (10) or wrongful dissociation under Section 602(b), the affirmative vote or consent of at least half of the remaining partners to wind up the partnership business, for which purpose a person's rightful dissociation pursuant to Section 602(b)(2)(A) constitutes that partner's consent to wind up the partnership business;

(B) the affirmative vote or consent of all the partners to wind up the partnership business; or

(C) the expiration of the term or the completion of the undertaking;

(3) an event or circumstance that the partnership agreement states causes dissolution;

(4) on application by a partner, the entry by [the appropriate court] of an order dissolving the partnership on the grounds that:

(A) the conduct of all or substantially all the partnership's business is unlawful;

(B) the economic purpose of the partnership is likely to be unreasonably frustrated;

(C) another partner has engaged in conduct relating to the partnership business which makes it not reasonably practicable to carry on the business in partnership with that partner; or

(D) it is otherwise not reasonably practicable to carry on the partnership business in conformity with the partnership agreement;

(5) on application by a transferee, the entry by [the appropriate court] of an order dissolving the partnership on the ground that it is equitable to wind up the partnership business:

(A) after the expiration of the term or completion of the undertaking, if the partnership was for a definite term or particular undertaking at the time of the transfer or entry of the charging order that gave rise to the transfer; or

(B) at any time, if the partnership was a partnership at will at the time of the transfer or entry of the charging order that gave rise to the transfer; or

(6) the passage of 90 consecutive days during which the partnership does not have at least two partners.

Comment

“Dissolution” has been a term of art in the law of unincorporated business organizations since at least the time of Roman law. JOSEPH STORY, COMMENTARIES ON THE LAW OF PARTNERSHIP § 266, at 408 (2d ed. 1850) (“The Roman law . . . declared, that partnership might be dissolved in various ways . . .”). Dissolution does not end a partnership’s existence but rather changes the purpose of that existence: “A dissolved partnership shall wind up its business and . . . the partnership continues after dissolution only for the purpose of winding up.” Section 802(a). The partnership may, but need not, file a statement of dissolution. Section 802(b)(2)(A). The partnership terminates when winding up is complete. The partnership may, but need not, file a statement of termination. Section 802(b)(2)(F).

UPA (1914) took a strictly aggregate approach to dissolution; under UPA (1914) § 29, the departure of any partner under any circumstances inevitably caused the partnership to dissolve. A partnership agreement had no power to avoid this result, although many partnership agreements purported to do so. A partnership agreement could provide for the continuation of the partnership business in a successor partnership, UPA (1914) § 38(2)(b), but that approach was often problematic. *See* the comment to Section 201(a).

UPA (1997) fundamentally changed this aspect of the law of general partnerships, making the partnership entity much more durable than the UPA (1914) aggregate. For example, expelling a partner does not cause the partnership to dissolve, even if the partnership is at-will. Section 801(1). More generally, the grounds for dissolution stated in Section 801 are exhaustive, unless the partnership agreement states otherwise.

Given this act's built-in transfer restrictions, Section 503, increasing the partnership's durability necessarily decreases each partner's exit rights. Under UPA (1914), each partner has a non-waivable power to exit the enterprise; dissociation inevitably causes dissolution, which in most instances will lead to a buyout of the dissociating partner, subject to any damages for wrongful dissolution. UPA (1914) § 38. Eliminating that power creates a risk of "lock-in."

UPA (1997) addressed the lock-in issue through UPA (1997) § 701. When a person dissociates as a partner, whether rightfully or wrongfully, the partnership is obligated to buy out the person's interest. Note, however, that Section 701, like UPA (1997) § 701, is a default rule.

Except for Paragraphs 4 and 5, this section comprises default rules. Paragraphs 4 and 5 are mandatory only with regard to the stated grounds for dissolution. *See* the comment to Section 105(c)(11). Variations to the statutory causes of dissolution are commonplace.

Section 803 permits rescission of dissolution in some circumstances. In some circumstances, an amendment to the partnership agreement might avert dissolution – *e.g.*, by revising an agreed-upon deadline for selling the partnership assets and winding up the business. A retroactive amendment may also be possible. *See Kindred Ltd. P'ship v. Screen Actors Guild, Inc.*, CV082220PSGPJWX, 2009 WL 279080, at *5–6 (C.D. Cal. Feb. 3, 2009) (giving effect to an amendment that retroactively eliminated an event of dissolution; noting that UPA (1997) § 802(b) permitted a partnership to rescind dissolution).

The Harmonization Project added Paragraph 6 but otherwise made no significant changes to this section.

Paragraph (1)—This paragraph: (i) recognizes the power of any partner in a partnership at will to dissolve the partnership at any time "by express will"; and (ii) provides that a partner who has already been dissociated under some other provision of this section lacks the power to dissolve the partnership. The latter proposition seems self-evident; a person dissociated as a partner is no longer a partner.

Paragraph (2)—This paragraph provides three ways in which a term partnership may be dissolved before the expiration of the term.

Paragraph (2)(A)—This provision: (i) originated in UPA (1997); (ii) helps make the partnership entity more durable; (iii) protects the remaining partners where the dissociating partner is crucial to the successful continuation of the business; and (iv) reverses the approach of UPA (1914).

Under UPA (1914), any dissociation dissolves the partnership, and unanimous consent of the remaining partners to continue the business. Thus each partner has the right to cause liquidation. *See* UPA (1914) § 38(2)(b). Under this act, a term partnership is more durable.

A person's dissociation as a partner by death or otherwise under Section 601(6) to (10) or wrongful dissociation under Section 602(b), makes a term partnership *susceptible* to dissolution. If within ninety days after the dissociation at least half of the remaining partners express their will to dissolve the partnership, the partnership dissolves. Section 601(6) to (10) pertain, respectively, to a partner's bankruptcy or similar financial impairment (6); a partner's death or incapacity (7); the distribution by a trust-partner of its entire transferable interest (8); the distribution by an estate-partner of its entire transferable interest; and the termination of an entity-partner (10).

During the same ninety-day window, Section 602(b)(2)(A) permits each remaining partner to withdraw rightfully by express will. A partner does not express a desire to withdraw solely by reason of voting for or consenting to the winding up of the partnership business. However, the converse is true: "[A] person's rightful dissociation pursuant to Section 602(b)(2)(A) constitutes the expression of that partner's consent to wind up the partnership business." Section 801(2)(A).

EXAMPLE: A term partnership has seven partners, and one of the partners dissociates by dying before the end of the term. Section 601(7). The partnership will dissolve if within ninety days after the dissociation three of the remaining five partners affirmatively vote or consent to dissolution.

EXAMPLE: Same facts, except the partner dissociates in breach of the partnership agreement. Same result.

EXAMPLE: Same facts, except that the partner is "a person that . . . is acting as a partner by virtue of being a trustee of . . . a trust, [and] the trust's entire transferable interest in the partnership [has been] distributed. Section 601(8). Same result.

Paragraph (2)(B)—This provision states that a term partnership may be dissolved and wound up at any time by the express will of all the partners. The provision merely reflects the general rule that the partnership agreement may override the statutory default rules and that the partnership agreement, like any contract, can be amended at any time by unanimous consent.

Paragraph (2)(C)—This rule is inherent in the concept of a partnership for a specified term or undertaking. This provision must be read in conjunction with Section 411. Under Section 411(a), if the partners continue the business after the expiration of the term or the completion of the undertaking, the partnership will be treated as a partnership at will. Moreover, if the partners continue the business without any settlement or liquidation of the partnership, under Section 411(b) they are presumed to have agreed that the partnership will continue, despite the lack of a formal agreement.

Paragraph (3)—The partners can avoid the effects of this paragraph either by amending

the partnership agreement before dissolution occurs or using Section 803 to rescind dissolution. A retroactive amendment may also be possible. *See Kindred Ltd. P'ship v. Screen Actors Guild, Inc.*, CV082220PSGPJWX, 2009 WL 279080, at *5–6 (C.D. Cal. Feb. 3, 2009) (giving effect to an amendment that retroactively eliminated an event of dissolution; noting that UPA (1997) § 802(b) permitted a partnership to rescind dissolution).

Paragraph (4)—The partnership agreement cannot vary the stated grounds for dissolution.

Paragraph (4)(A)—The “all or substantially all” proviso is intended to avoid dissolution for insubstantial or innocent regulatory violations.

Paragraph (4)(B)–(D)—The Virginia Supreme Court has referred to “these statutory bases for judicial dissolution as the economic purpose test, the partner conduct test, and the business operations test, respectively.” *Russell Realty Assocs. v. Russell*, 724 S.E.2d 690, 693 (Va. 2012). These tests somewhat overlap and are often pled together. *E.g., Wood v. Apodaca*, 375 F. Supp. 2d 942, 948 (N.D. Cal. 2005).

Some courts have held that, if the trial court finds grounds for dissolution under one or more of these provisions, that court has no power to order a lesser remedy, such as a buyout. *Pankratz Farms, Inc. v. Pankratz*, 95 P.3d 671, 679–80 (Mont. 2004) (so holding even though: (i) “judicial dissolution of the Partnership would trigger significant adverse tax consequences to all the parties involved, including Marvin [who commenced the action seeking dissolution]”; and (ii) “Marvin [had] requested monetary damages as an alternative to dissolution”); *Navarro v. Perron*, 122 Cal. App. 4th 797, 801, 19 Cal. Rptr. 3d 198, 201 (2004) (“Where the court determines it is not reasonably practical to carry on the partnership, the court has no discretion to deny a partner’s application to dissolve it.”).

Paragraph (4)(B)—“[P]oor financial performance” is neither sufficient nor necessary to satisfy this provision. *Russell Realty Assocs. v. Russell*, 724 S.E.2d 690, 694 (Va. 2012). The provision’s history substantiates the first point (not by itself sufficient). *See* UPA (1997) § 801, cmt. 8 (“RUPA deletes UPA Section 32(1)(e) which provides for dissolution when the business can only be carried on at a loss. That provision might result in a dissolution contrary to the partners’ expectations in a start-up or tax shelter situation, in which case ‘book’ or ‘tax’ losses do not signify business failure.”).

As for the second point (not always necessary), see *Russell Realty Assocs. v. Russell*, 724 S.E.2d 690, 694–55 (Va. 2012) (noting that the partnership’s purpose was “to acquire, hold, invest in, and lease and sell investment properties”; stating with regard to the Virginia analog to Paragraph 4(B) that “[t]he partners’ expectations for realizing these purposes included not only expectations of economic success, but also the ability to undertake these activities in an efficient and productive manner to maximize return to the partnership”; and listing numerous ways in which the relationship between the partners frustrated the economic purpose of the partnership).

Paragraph (4)(C)—A partner can trigger this provision without necessarily breaching the partnership agreement. *E.g., Robertson v. Jacobs Cattle Co.*, 830 N.W.2d 191, 202 (Neb.

2013) (stating that “the somewhat autocratic manner in which Ardith conducted the affairs of the partnership in recent years, even if not in violation of the partnership agreement, would constitute grounds for dissolution under [the UPA (1997) version of] this provision”).

Paragraph (4)(D)—The specific terms of the partnership agreement are the frame of reference for applying this provision. *Sriram v. Preferred Income Fund III Ltd. P'ship*, 22 F.3d 498, 502 (2d Cir. 1994) (“The issue is not whether the partnerships can effectively carry out the general purpose of the Agreements after considerable modification of their terms. Rather, the query . . . is whether the purpose of the Agreements can be carried out ‘in conformity with the partnership agreement,’ that is, in conformity with the terms and conditions of the Agreements to which the limited partners ascribed and on which they relied when choosing to part with their capital.”) (applying the provision of RULPA (1976/1985) that is analogous to Paragraph (4)(C)).

Paragraph (5)—This paragraph gives a transferee rights comparable to a partner who seeks dissolution because the other partners are continuing the business in derogation of the partner’s rights to obtain dissolution. The paragraph is based on UPA (1914) § 32(2) but UPA (1997) added the requirement that the court determine that it is equitable to wind up the business. The rights of a transferee under this section cannot be varied in the partnership agreement. *See* Section 105(c)(11). Neither ULPA (2001) (Last Amended 2013) nor ULLCA (2006) (Last Amended 2013) have a comparable provision, because both those acts provide for perpetual existence. *See* ULPA (2001) (Last Amended 2013) § 110 and ULLCA (2006) (Last Amended 2013) § 108.

Paragraph (6)—The Harmonization Project added this provision, which is consistent with Section 202(a) (stating that “the association of two or more persons to carry on as co-owners a business for profit forms a partnership”). *See* the comment to Section 302(d); *Pemstein v. Pemstein*, G030217, 2004 WL 1260034 (Cal. Ct. App. June 9, 2004) (“‘Can one person carry on a partnership?’ In short, the answer is no Just as it takes two to form a marriage, it takes a minimum of two to run a viable partnership. We were unable to find any contrary authority, and appellants fail to provide any, holding a partnership can be carried on by less than two persons.”)

SECTION 802. WINDING UP.

(a) A dissolved partnership shall wind up its business and, except as otherwise provided in Section 803, the partnership continues after dissolution only for the purpose of winding up.

(b) In winding up its business, the partnership:

(1) shall discharge the partnership’s debts, obligations, and other liabilities, settle and close the partnership’s business, and marshal and distribute the assets of the partnership; and

(2) may:

(A) deliver to the [Secretary of State] for filing a statement of dissolution

stating the name of the partnership and that the partnership is dissolved;

(B) preserve the partnership business and property as a going concern for a reasonable time;

(C) prosecute and defend actions and proceedings, whether civil, criminal, or administrative;

(D) transfer the partnership's property;

(E) settle disputes by mediation or arbitration;

(F) deliver to the [Secretary of State] for filing a statement of termination stating the name of the partnership and that the partnership is terminated; and

(G) perform other acts necessary or appropriate to the winding up.

(c) A person whose dissociation as a partner resulted in dissolution may participate in winding up as if still a partner, unless the dissociation was wrongful.

(d) If a dissolved partnership does not have a partner and no person has the right to participate in winding up under subsection (c), the personal or legal representative of the last person to have been a partner may wind up the partnership's business. If the representative does not exercise that right, a person to wind up the partnership's business may be appointed by the affirmative vote or consent of transferees owning a majority of the rights to receive distributions at the time the consent is to be effective. A person appointed under this subsection has the powers of a partner under Section 804 but is not liable for the debts, obligations, and other liabilities of the partnership solely by reason of having or exercising those powers or otherwise acting to wind up the partnership's business.

(e) On the application of any partner or person entitled under subsection (c) to participate in winding up, the [appropriate court] may order judicial supervision of the winding up of a

dissolved partnership, including the appointment of a person to wind up the partnership's business, if:

- (1) the partnership does not have a partner and within a reasonable time following the dissolution no person has been appointed under subsection (d); or
- (2) the applicant establishes other good cause.

Comment

Under the default rules of this act, dissolution does not change governance arrangements. However, dissolution does change the context for determining whether a matter is in or outside “the ordinary course of business of [the] partnership.” Section 401(k). In addition, dissolution triggers a default rule entitling each partner to “reasonable compensation for services rendered in winding up the business of the partnership.” Section 401(j).

Section 804 governs the post-dissolution power of a partner to bind the partnership, and Section 805 governs the “liability after dissolution of partner and person dissociated as general partner.”

Subsection (a)—For more information on the impact of a partnership's dissolution, see Section 801, comment.

Subsection (b)—The particular circumstances determine how long winding up may continue without giving “good cause” for court intervention under Section 802(e). There is no “hard and fast” rule. *See, e.g., Mathis v. Meyeres*, 574 P.2d 447, 450 (Alaska 1978) (stating “we are aware of [no authority] requiring that deadlines be set in the winding up of a partnership”); *8182 Md. Assocs., Ltd. P'ship v. Sheehan*, 14 S.W.3d 576, 581 (Mo. 2000) (“The Uniform Partnership Law contemplates that dissolved partnerships may continue in business for a short, long or indefinite period of time.”) (quoting *Schoeller v. Schoeller*, 497 S.W.2d 860, 867 (Mo. Ct. App. 1973)).

“Winding up usually entails the time necessary for the partners to finish old business, collect and pay debts, and finally distribute remaining assets to the partners.” *Gibson v. Deuth*, 270 N.W.2d 632, 635 (Iowa 1978). “Generally the best interests of the partnership will be served by winding up the partnership affairs as quickly as possible.” *Doting v. Trunk*, 856 P.2d 536, 540 (Mont. 1993). However, in some circumstances, a long period of winding up is not only appropriate but necessary. *Lebanon Trotting Ass'n v. Battista*, 306 N.E.2d 769, 772 (Ohio Ct. App. 1972) (“[I]f the only means of availing the partners of the benefit of the value of the lease would be to continue to operate under such lease until its expiration, then such operation may continue as part of the winding up of the partnership affairs after dissolution. It is not necessary that a partnership, in the absence of the consent of all the partners, abandon a valuable asset upon dissolution merely because it may have no ready market value, but the value of such asset can continue to inure to the benefit of the partners through the continuation of the partnership after

dissolution.”).

Subsection (b)(2)(A) and (F)—For the constructive notice effect of a statement of dissolution or termination, see Sections 103(d)(2)(A) and (B) and 303.

Subsection (c)—This provision applies only to “[a] partner whose [rightful] dissociation resulted in dissolution.”

EXAMPLE: Partner A dissociates from the Killarney Company (“Killarney”), a general partnership. Partner A’s dissociation does not result in dissolution, and, per the Killarney partnership agreement, Partner A’s transferable interest is being redeemed over five years. One year after Partner A’s dissociation, Partner B dissociates rightfully, and dissolution results. Partner B may participate in Killarney’s winding up; Partner A may not.

EXAMPLE: Partner A wrongfully dissociates from Killarney, and the dissociation results in the dissolution of Killarney. Partner A may not participate in winding up.

A partner’s duties and obligation under Section 409 extend to winding up. Section 603(b)(2). However, under Section 409(b)(3), each partner’s duty not to compete ends when the partnership dissolves.

Subsection (d)—A person appointed under this section will normally be an agent of the dissolved partnership, acting pursuant to a contract. Agency and contract law will determine the person’s duties; by its terms Section 409 does not apply.

SECTION 803. RESCINDING DISSOLUTION.

(a) A partnership may rescind its dissolution, unless a statement of termination applicable to the partnership has become effective or [the appropriate court] has entered an order under Section 801(4) or (5) dissolving the partnership.

(b) Rescinding dissolution under this section requires:

(1) the affirmative vote or consent of each partner; and

(2) if the partnership has delivered to the [Secretary of State] for filing a statement of dissolution and:

(A) the statement has not become effective, delivery to the [Secretary of State] for filing of a statement of withdrawal under Section 115 applicable to the statement of dissolution; or

(B) the statement of dissolution has become effective, delivery to the [Secretary of State] for filing of a statement of rescission stating the name of the partnership and that dissolution has been rescinded under this section.

(c) If a partnership rescinds its dissolution:

(1) the partnership resumes carrying on its business as if dissolution had never occurred;

(2) subject to paragraph (3), any liability incurred by the partnership after the dissolution and before the rescission has become effective is determined as if dissolution had never occurred; and

(3) the rights of a third party arising out of conduct in reliance on the dissolution before the third party knew or had notice of the rescission may not be adversely affected.

Comment

The Harmonization Project added this section, replacing UPA (1997) § 802(b) (permitting the partners to “waive the right to have the partnership’s business wound up and the partnership terminated” after which “the partnership resumes carrying on its business as if dissolution had never occurred”).

Subsection (a)—The first exclusion results inevitably from the effect of a statement of termination, Section 802(b)(2)(F) – *i.e.*, the partnership ceases to exist. A “dead” entity lacks both the capacity and power to bring itself back from the dead.

The second and third exclusions pertain to dissolutions effected by outsiders – *i.e.*, the court and the filing office.

Subsections (b)(1)—The requirement of unanimous consent protects any vested rights or reliance by partners. However, the partnership agreement may vary this provision.

Subsection (c)(3)—This paragraph protects third parties. *E.g.*, *Neurobehavioral Associates, P.A. v. Cypress Creek Hosp., Inc.*, 995 S.W.2d 326, 331 (Tex. App. 1999) (“If the Hospital had the right to terminate the Agreement when it did because the Association was then dissolved, then even though the Association can revoke articles of dissolution and have that relate back to the date of dissolution, it would be grossly unfair to let the Association assert its ex post facto change as a defense. Surely the Association would be estopped from doing so, having created the very conditions that gave the Hospital the correct impression that it was then

dissolved.”).

SECTION 804. POWER TO BIND PARTNERSHIP AFTER DISSOLUTION.

(a) A partnership is bound by a partner’s act after dissolution which:

(1) is appropriate for winding up the partnership business; or

(2) would have bound the partnership under Section 301 before dissolution if, at the time the other party enters into the transaction, the other party does not know or have notice of the dissolution.

(b) A person dissociated as a partner binds a partnership through an act occurring after dissolution if:

(1) at the time the other party enters into the transaction:

(A) less than two years has passed since the dissociation; and

(B) the other party does not know or have notice of the dissociation and reasonably believes that the person is a partner; and

(2) the act:

(A) is appropriate for winding up the partnership’s business; or

(B) would have bound the partnership under Section 301 before dissolution and at the time the other party enters into the transaction the other party does not know or have notice of the dissolution.

Comment

This section provides the “power to bind” rules applicable once dissolution occurs. The section originated in UPA (1997), which significantly departed from the approach of UPA (1914). The Harmonization Project revised this section to conform to ULPA (2001). However, the revisions are essentially stylistic.

In general, this section parallels Section 702 (power to bind of a person dissociated as partner when dissolution does not result from the dissociation). However, one significant difference exists. Section 702(a)(2)(A) contains a provision analogous to a statute of repose. A

person's power to bind the partnership terminates two years after the date of dissociation. Subsection (b) contains a comparable provision, but Subsection (a) does not.

Subsections (a) and (b)—Subsection (a) states the power-to-bind rules for persons still partners when dissolution occurs. Subsection (b) pertains to persons dissociated before dissolution, including a partner whose dissociation results in dissolution. *Compare* Section 804, *with* Section 802(c) (stating that as an *inter se* matter a person whose rightful dissociation results in dissolution may participate in winding up “as if still a partner.”).

Subsection (a)(1)—This paragraph states a rule of inherent agency power. *See* RESTATEMENT (SECOND) OF AGENCY § 8A (defining “inherent agency power” as “the power of an agent which is derived not from authority, apparent authority or estoppel, but solely from the agency relation and exists for the protection of persons harmed by or dealing with a servant or other agent”). Thus, a partner might act without actual or apparent authority and still bind the partnership. The partnership agreement cannot change the stated rule because the rule pertains to the rights under this act of third parties. *See* Section 105(c)(17).

If a partner's words or conduct trigger this paragraph, thereby binding the partnership, and the partner lacks the actual authority to do so, the partner breaches an agent's duty to act within authority, and is liable to the partnership for any resulting damages. RESTATEMENT (THIRD) OF AGENCY § 8.09(1) (“An agent has a duty to take action only within the scope of the agent's actual authority”). The partner might also be liable for breach of the partnership agreement.

Subsection (a)(2)—A person might have notice under Section 103(d)(2)(B)(i) (statement of dissolution) as well as under Section 103(b)(1) (reason to know).

Subsection (b)—This subsection deals with the post-dissolution power to bind of a person dissociated as a partner. For the most part: (i) Paragraph 1 replicates Section 702, pertaining to the pre-dissolution power to bind of a person dissociated as a partner; and (ii) Paragraph 2 replicates Subsection (a) of this section, which states the post-dissolution power to bind of a person is still a partner.

For a person dissociated as a partner to bind a dissolved partnership:

- the person's dissociation must have:
 - been rightful; and
 - resulted in dissolution; and
- the person's act must satisfy both Paragraphs 1 and 2.

Subsection (b)(1)(B)—A person might have notice under Section 103(d)(2)(B)(i) (statement of dissolution) as well as under Section 103(b)(1) (reason to know).

Subsection (b)(2)(B)—A person might have notice under Section 103(d)(2)(B)(i) (statement of dissolution) as well as under Section 103(b)(1) (reason to know).

**SECTION 805. LIABILITY AFTER DISSOLUTION OF PARTNER AND
PERSON DISSOCIATED AS PARTNER.**

(a) If a partner having knowledge of the dissolution causes a partnership to incur an obligation under Section 804(a) by an act that is not appropriate for winding up the partnership business, the partner is liable:

(1) to the partnership for any damage caused to the partnership arising from the obligation; and

(2) if another partner or person dissociated as a partner is liable for the obligation, to that other partner or person for any damage caused to that other partner or person arising from the liability.

(b) Except as otherwise provided in subsection (c), if a person dissociated as a partner causes a partnership to incur an obligation under Section 804(b), the person is liable:

(1) to the partnership for any damage caused to the partnership arising from the obligation; and

(2) if a partner or another person dissociated as a partner is liable for the obligation, to the partner or other person for any damage caused to the partner or other person arising from the obligation.

(c) A person dissociated as a partner is not liable under subsection (b) if:

(1) Section 802(c) permits the person to participate in winding up; and

(2) the act that causes the partnership to be bound under Section 804(b) is appropriate for winding up the partnership's business.

Comment

This section parallels Section 702. It is possible for more than one person to be liable under this section on account of the same partnership obligation. This act does not provide any

rule for apportioning liability in that circumstance.

Subsection (a)(2)—If the partnership is not a limited liability partnership, the liability created by this paragraph includes liability under Sections 306(a) and 703(b). The paragraph also applies when a partner or person dissociated as a general partner suffers damage due to a contract of guaranty.

Other law determines liability (if any) to a person that is neither a partner nor dissociated as a partner.

SECTION 806. DISPOSITION OF ASSETS IN WINDING UP; WHEN CONTRIBUTIONS REQUIRED.

(a) In winding up its business, a partnership shall apply its assets, including the contributions required by this section, to discharge the partnership's obligations to creditors, including partners that are creditors.

(b) After a partnership complies with subsection (a), any surplus must be distributed in the following order, subject to any charging order in effect under Section 504:

(1) to each person owning a transferable interest that reflects contributions made and not previously returned, an amount equal to the value of the unreturned contributions; and

(2) among persons owning transferable interests in proportion to their respective rights to share in distributions immediately before the dissolution of the partnership.

(c) If a partnership's assets are insufficient to satisfy all its obligations under subsection (a), with respect to each unsatisfied obligation incurred when the partnership was not a limited liability partnership, the following rules apply:

(1) Each person that was a partner when the obligation was incurred and that has not been released from the obligation under Section 703(c) and (d) shall contribute to the partnership for the purpose of enabling the partnership to satisfy the obligation. The contribution due from each of those persons is in proportion to the right to receive distributions in the

capacity of a partner in effect for each of those persons when the obligation was incurred.

(2) If a person does not contribute the full amount required under paragraph (1) with respect to an unsatisfied obligation of the partnership, the other persons required to contribute by paragraph (1) on account of the obligation shall contribute the additional amount necessary to discharge the obligation. The additional contribution due from each of those other persons is in proportion to the right to receive distributions in the capacity of a partner in effect for each of those other persons when the obligation was incurred.

(3) If a person does not make the additional contribution required by paragraph (2), further additional contributions are determined and due in the same manner as provided in that paragraph.

(d) A person that makes an additional contribution under subsection (c)(2) or (3) may recover from any person whose failure to contribute under subsection (c)(1) or (2) necessitated the additional contribution. A person may not recover under this subsection more than the amount additionally contributed. A person's liability under this subsection may not exceed the amount the person failed to contribute.

(e) If a partnership does not have sufficient surplus to comply with subsection (b)(1), any surplus must be distributed among the owners of transferable interests in proportion to the value of the respective unreturned contributions.

(f) All distributions made under subsections (b) and (c) must be paid in money.

Comment

Subsection (a)—This subsection is non-waivable as to creditors who are not partners. *See* Section 105(c)(17) (stating that the partnership agreement may not “restrict the rights under this [act] of a person other than a partner”). However, if a creditor is willing, a dissolved partnership may certainly make agreements with the creditor specifying the terms under which the partnership will “discharge its obligations” to the creditor. If under Section 306(a) one or more partners are also liable on a partnership obligation, any agreement between the partnership

and the creditor should take in account Section 703(d).

Subsection (b)—For the most part, this subsection states default rules. For example, partnership agreements often provide for different distribution rights upon liquidation than during operations. However, distributions under this subsection (or otherwise under the partnership agreement) are subject to Section 504 (charging orders). As to the extent the partnership agreement can be amended to affect the distribution rights of persons already transferees, see Section 107(b).

Subsection (c)—This section applies obligation by obligation, because a person—*qua* partner or person dissociated as a partner—is required to contribute to the partnership to satisfy a partnership obligation only if, when the obligation was incurred: (i) the person was a partner; and (ii) the partnership was not an LLP. *See* Section 306(b), (c). As for when a partnership obligation is incurred, see Section 306(b) and (c), comments.

The allocation of contribution obligations parallels the default rule stated in Section 401(a) (providing that, “except in the case of a limited liability partnership, [each partner] is chargeable with a share of the partnership losses in proportion to the partner’s share of the profits”). The partnership agreement can change the allocation *inter se* partners and persons dissociated as partners but cannot prejudice the rights of non-partner creditors.

EXAMPLE: The A-B Partnership (the “Partnership”) owes Creditor \$150, an obligation incurred when Partners A and B were the only partners, sharing distributions equally, and the Partnership was not an LLP. The Partnership has no funds to pay Creditor. Although Subsection (c)(1) would require Partners A and B each to contribute equally (*i.e.*, \$75), the A-B Partnership Agreement provides that Partner A has the entire contribution obligation and Partner B has none. As between Partners A and B, Partner A is obligated to contribute \$150 and Partner B nothing. However, as to Creditor, Partner B still has a contribution obligation of \$75.

This formal distinction will have practical consequences only if A does not contribute the full \$150. Also, Creditor may have problems establishing standing. *Cf.* the comment to Section 407.

Subsection (c)(2) and (3)—These provisions are analogous to buy-sell provisions that: (i) provide that an owner’s effort to sell the ownership interest triggers an option to purchase allocated among all the other owners; (ii) make the option conditional on the entire interest being purchased; and (iii) provide for successive allocations to take up any previous allocations that were not unexercised.

Subsection (e)—If a partnership has been a limited liability partnership throughout the partnership’s existence, this subsection is consistent with this act’s approach to loss sharing. If a partnership has been a limited liability partnership during only part of the partnership’s existence, the issue of loss sharing upon dissolution: (i) can be exceedingly complicated, varying radically depending on the circumstances; (ii) is therefore not amenable to a statutory “gap filler”; and (iii) thus should always be addressed in the partnership agreement.

However, in case the partnership agreement does not address the issue, this act must provide a default rule. *See* the comment to Section 105(b) (“To the extent the partnership agreement does not determine an inter se matter, this act determines the matter.”). This subsection applies to fill the gap. This approach has the virtues of simplicity and certainty but in no way resembles what “typical” partners might agree if they were to consider the matter *ab initio*, especially if the partnership was never an LLP. *Cf.* Robert W. Hillman, *Private Ordering Within Partnerships*, 41 U. MIAMI L. REV. 425, 448 (1987) (“[T]he various norms established by the Act, applicable in the absence of agreements to the contrary, represent the supposed understandings partners most likely reach if they choose to bargain on the various issues.”).

SECTION 807. KNOWN CLAIMS AGAINST DISSOLVED LIMITED LIABILITY PARTNERSHIP.

(a) Except as otherwise provided in subsection (d), a dissolved limited liability partnership may give notice of a known claim under subsection (b), which has the effect provided in subsection (c).

(b) A dissolved limited liability partnership may in a record notify its known claimants of the dissolution. The notice must:

- (1) specify the information required to be included in a claim;
- (2) state that a claim must be in writing and provide a mailing address to which the claim is to be sent;
- (3) state the deadline for receipt of a claim, which may not be less than 120 days after the date the notice is received by the claimant;
- (4) state that the claim will be barred if not received by the deadline; and
- (5) unless the partnership has been throughout its existence a limited liability partnership, state that the barring of a claim against the partnership will also bar any corresponding claim against any partner or person dissociated as a partner which is based on Section 306.

(c) A claim against a dissolved limited liability partnership is barred if the requirements

of subsection (b) are met and:

(1) the claim is not received by the specified deadline; or

(2) if the claim is timely received but rejected by the limited liability partnership:

(A) the partnership causes the claimant to receive a notice in a record stating that the claim is rejected and will be barred unless the claimant commences an action against the partnership to enforce the claim not later than 90 days after the claimant receives the notice; and

(B) the claimant does not commence the required action not later than 90 days after the claimant receives the notice.

(d) This section does not apply to a claim based on an event occurring after the date of dissolution or a liability that on that date is contingent.

Comment

Source—Added during the Harmonization Project, this section is derived almost verbatim from Model Business Corporation Act section 14.06.

Subsection (b)(5)—For additional information on when a claim against a partnership is barred, see Section 810, comment.

SECTION 808. OTHER CLAIMS AGAINST DISSOLVED LIMITED LIABILITY PARTNERSHIP.

(a) A dissolved limited liability partnership may publish notice of its dissolution and request persons having claims against the partnership to present them in accordance with the notice.

(b) A notice under subsection (a) must:

(1) be published at least once in a newspaper of general circulation in the [county] in this state in which the dissolved limited liability partnership's principal office is located or, if

the principal office is not located in this state, in the [county] in which the office of the partnership's registered agent is or was last located;

(2) describe the information required to be contained in a claim, state that the claim must be in writing, and provide a mailing address to which the claim is to be sent;

(3) state that a claim against the partnership is barred unless an action to enforce the claim is commenced not later than three years after publication of the notice; and

(4) unless the partnership has been throughout its existence a limited liability partnership, state that the barring of a claim against the partnership will also bar any corresponding claim against any partner or person dissociated as a partner which is based on Section 306.

(c) If a dissolved limited liability partnership publishes a notice in accordance with subsection (b), the claim of each of the following claimants is barred unless the claimant commences an action to enforce the claim against the partnership not later than three years after the publication date of the notice:

(1) a claimant that did not receive notice in a record under Section 807;

(2) a claimant whose claim was timely sent to the partnership but not acted on;

and

(3) a claimant whose claim is contingent at, or based on an event occurring after, the date of dissolution.

(d) A claim not barred under this section or Section 807 may be enforced:

(1) against a dissolved limited liability partnership, to the extent of its undistributed assets;

(2) except as otherwise provided in Section 809, if assets of the partnership have

been distributed after dissolution, against a partner or transferee to the extent of that person's proportionate share of the claim or of the partnership's assets distributed to the partner or transferee after dissolution, whichever is less, but a person's total liability for all claims under this paragraph may not exceed the total amount of assets distributed to the person after dissolution; and

(3) against any person liable on the claim under Sections 306, 703, and 805.

Comment

Source—Added during the Harmonization Project, this section is derived almost verbatim from Model Business Corporation Act section 14.07.

Subsection (b)(4)—For additional information on when a claim against a partnership is barred, see Section 810, comment

Subsection (d)(2)—Liability under this paragraph extends to those who have received distributions under a charging order. *See* the comment to Section 504(a) (explaining that the beneficiary of a charging order is a transferee). Unlike Section 407(c) (recapture of improper distributions), this paragraph contains no “knowledge” element.

Subsection (d)(3)—The referenced sections address the vicarious liability of partners and persons dissociated as partners for obligations of a partnership that is not an LLP.

SECTION 809. COURT PROCEEDINGS.

(a) A dissolved limited liability partnership that has published a notice under Section 808 may file an application with [the appropriate court] in the [county] where the partnership's principal office is located or, if the principal office is not located in this state, where the office of its registered agent is or was last located, for a determination of the amount and form of security to be provided for payment of claims that are reasonably expected to arise after the date of dissolution based on facts known to the partnership and:

(1) at the time of the application:

(A) are contingent; or

(B) have not been made known to the partnership; or

(2) are based on an event occurring after the date of dissolution.

(b) Security is not required for any claim that is or is reasonably anticipated to be barred under Section 807.

(c) Not later than 10 days after the filing of an application under subsection (a), the dissolved limited liability partnership shall give notice of the proceeding to each claimant holding a contingent claim known to the partnership.

(d) In any proceeding under this section, the court may appoint a guardian ad litem to represent all claimants whose identities are unknown. The reasonable fees and expenses of the guardian, including all reasonable expert witness fees, must be paid by the dissolved limited liability partnership.

(e) A dissolved limited liability partnership that provides security in the amount and form ordered by the court under subsection (a) satisfies the partnership's obligations with respect to claims that are contingent, have not been made known to the partnership, or are based on an event occurring after the date of dissolution, and such claims may not be enforced against a partner or transferee on account of assets received in liquidation.

Comment

Source—Added during the Harmonization Project, this section is derived almost verbatim from Model Business Corporation Act section 14.08.

SECTION 810. LIABILITY OF PARTNER AND PERSON DISSOCIATED AS PARTNER WHEN CLAIM AGAINST PARTNERSHIP BARRED. If a claim against a dissolved partnership is barred under Section 807, 808, or 809, any corresponding claim under Section 306, 703, or 805 is also barred.

Comment

A partner's liability under Sections 306, 703 and 805 is vicarious liability—liability solely by status and solely for the “debts, obligations, and other liabilities of the partnership.” To the extent a claim pertaining to the underlying debt, obligation, or other liability is barred, a claim pertaining to the corresponding vicarious liability should likewise be barred.

[ARTICLE] 9

LIMITED LIABILITY PARTNERSHIP

SECTION 901. STATEMENT OF QUALIFICATION.

(a) A partnership may become a limited liability partnership pursuant to this section.

(b) The terms and conditions on which a partnership becomes a limited liability partnership must be approved by the affirmative vote or consent necessary to amend the partnership agreement except, in the case of a partnership agreement that expressly addresses obligations to contribute to the partnership, the affirmative vote or consent necessary to amend those provisions.

(c) After the approval required by subsection (b), a partnership may become a limited liability partnership by delivering to the [Secretary of State] for filing a statement of qualification. The statement must contain:

- (1) the name of the partnership which must comply with Section 902;
- (2) the street and mailing addresses of the partnership's principal office and, if different, the street address of an office in this state, if any;
- (3) the name and street and mailing addresses in this state of the partnership's

registered agent; and

(4) a statement that the partnership elects to become a limited liability partnership.

(d) A partnership's status as a limited liability partnership remains effective, regardless of changes in the partnership, until it is canceled pursuant to subsection (f) or administratively revoked pursuant to Section 903.

(e) The status of a partnership as a limited liability partnership and the protection against liability of its partners for the debts, obligations, or other liabilities of the partnership while it is a limited liability partnership is not affected by errors or later changes in the information required to be contained in the statement of qualification.

(f) A limited liability partnership may amend or cancel its statement of qualification by delivering to the [Secretary of State] for filing a statement of amendment or cancellation. The statement must be approved by the affirmative vote or consent of all the partners and state the name of the limited liability partnership and in the case of:

(1) an amendment, state the text of the amendment; and

(2) a cancellation, state that the statement of qualification is canceled.

Comment

Subsection (a)—Every partnership governed by this act may become a limited liability partnership, and the necessary formalities are straightforward: approval of the decision by the partners and delivering to the filing office for filing a simple statement of qualification. A partnership becomes a limited liability partnership when the filing office files the statement of qualification and the statement takes effect. For the consequences of LLP status, see Section 306(c), comment.

Subsection (b)—In the default mode, becoming a limited liability partnership requires the agreement of all partners, because in the default mode amending the partnership agreement requires the affirmative vote or consent of all partners, Section 401(k) (stating the voting/consent requirement to amend the partnership agreement). The unanimous vote/consent default rule reflects the significance of the transformation *inter se* the partners. See the comment to Section 306(c) (Effect of LLP Status on Relations Inter Se the Partners).

In the event a partnership agreement provides different quanta of consent for different matters, this subsection chooses (as a default rule) “the affirmative vote or consent necessary to amend those provisions” of “partnership agreement that expressly addresses obligations to contribute to the partnership.” This choice makes good sense, given the effect of LLP status on contribution obligations. *See* the comment to Section 306(c).

Subsection (c)—Although a statement of qualification does not create a new entity, Section 201(b), the requirements stated here are comparable to the requirements for a certificate of formation for a limited liability company, ULLCA (2006) (Last Amended 2013), and a certificate of limited partnership, ULPA (2001) (Last Amended 2013). The liability shield—a privilege granted by state—justifies requiring an LLP to meet these requirements.

Subsection (d)—Under some early LLP statutes, an LLP’s failure to file an annual renewal ended LLP status and terminated the shield. This subsection eschews that draconian result. However, an LLP’s failure to file an annual/biennial report, Section 913, is grounds for administrative revocation. *See* Section 903(d); *see also* Section 306(c)(2) (stating that the liability shield continues despite dissolution).

Neither this subsection nor Section 306(c)(2) expressly addresses the effect of an LLP’s termination on the liability shield. However, neither logic nor policy supports the retroactive destruction of the shield.

Subsection (f)—The unanimity requirement for amending a statement of qualification is a default rule. The unanimity requirement for cancelling a statement of qualification is mandatory. Section 105(c)(13). The difference reflects the very different consequences of amendment and cancellation. Subsection (b) requires very little information in a statement of qualification and does not contemplate additional information. *Compare* Section 901(f), *with* ULLCA (2006) (Last Amended 2013) § 201(c) (authorizing a certificate of formation to include additional information) *and* ULPA (2001) (Last Amended 2013) § 201(c) (same). Therefore, an amendment can do no substantial harm to any partner’s interest. In contrast, cancelling a statement of qualification makes every partner vicariously liable for all partnership obligations. *Compare* Section 901(f), *with* Section 105(c)(14) (stating that the partnership agreement may not “vary the right of a partner to approve a merger, interest exchange, conversion, or domestication” the result of which is to impose vicarious liability on the person for the obligations of the resulting entity).

SECTION 902. PERMITTED NAMES.

(a) The name of a partnership that is not a limited liability partnership may not contain the phrase “Registered Limited Liability Partnership” or “Limited Liability Partnership” or the abbreviation “R.L.L.P.”, “L.L.P.”, “RLLP”, or “LLP”.

(b) The name of a limited liability partnership must contain the phrase “Registered Limited Liability Partnership” or “Limited Liability Partnership” or the abbreviation “R.L.L.P.”,

“L.L.P.”, “RLLP”, or “LLP”.

(c) Except as otherwise provided in subsection (f), the name of a limited liability partnership, and the name under which a foreign limited liability partnership may register to do business in this state, must be distinguishable on the records of the [Secretary of State] from any:

(1) name of an existing person whose formation required the filing of a record by the [Secretary of State] and which is not at the time administratively dissolved;

(2) name of a limited liability partnership whose statement of qualification is in effect;

(3) name under which a person that is registered to do business in this state by the filing of a record by the [Secretary of State];

(4) name that is reserved under Section 903 or other law of this state providing for the reservation of a name by a filing of a record by the [Secretary of State];

(5) name that is registered under Section 904 or other law of this state providing for the registration of a name by a filing of a record by the [Secretary of State]; and

(6) a name registered under [this state’s assumed or fictitious name statute].

(d) If a person consents in a record to the use of its name and submits an undertaking in a form satisfactory to the [Secretary of State] to change its name to a name that is distinguishable on the records of the [Secretary of State] from any name in any category of names in subsection (c), the name of the consenting person may be used by the person to which the consent was given.

(e) Except as otherwise provided in subsection (f), in determining whether a name is the same as or not distinguishable on the records of the [Secretary of State] from the name of another person, words, phrases, or abbreviations indicating a type of entity, such as “corporation”,

“corp.”, “incorporated”, “Inc.”, “professional corporation”, “PC”, “P.C.”, “professional association”, “PA”, “P.A.”, “Limited”, “Ltd.”, “limited partnership”, “LP”, “L.P.”, “limited liability partnership”, “LLP”, “L.L.P.”, “registered limited liability partnership”, “RLLP”, “R.L.L.P.”, “limited liability limited partnership”, “LLLLP”, “L.L.L.P.”, “registered limited liability limited partnership”, “RLLLLP”, “R.L.L.L.P.”, “limited liability company”, “LLC”, or “L.L.C.”, “limited cooperative association”, “limited cooperative”, “LCA”, or “L.C.A.” may not be taken into account.

(f) A person may consent in a record to the use of a name that is not distinguishable on the records of the [Secretary of State] from its name except for the addition of a word, phrase, or abbreviation indicating the type of person as provided in subsection (e). In such a case, the person need not change its name pursuant to subsection (d).

(g) The name of a limited liability partnership or foreign limited liability partnership may not contain the words [insert prohibited words or words that may be used only with approval by an appropriate state agency].

(h) A limited liability partnership or foreign limited liability partnership may use a name that is not distinguishable from a name described in subsection (c)(1) through (6) if the partnership delivers to the [Secretary of State] a certified copy of a final judgment of a court of competent jurisdiction establishing the right of the partnership to use the name in this state.

Comment

This section adopts the “distinguishable on the records” test for name availability and rejects the “deceptively similar” test widely used in the past in business entity statutes.

For name requirements for foreign registered limited partnerships, see Section 1003(1).

SECTION 903. ADMINISTRATIVE REVOCATION OF STATEMENT OF QUALIFICATION.

(a) The [Secretary of State] may commence a proceeding under subsection (b) to revoke the statement of qualification of a limited liability partnership administratively if the partnership does not:

(1) pay any fee, tax, interest, or penalty required to be paid to the [Secretary of State] not later than [six months] after it is due;

(2) deliver [an annual] [a biennial] report to the [Secretary of State] not later than [six months] after it is due; or

(3) have a registered agent in this state for [60] consecutive days.

(b) If the [Secretary of State] determines that one or more grounds exist for administratively revoking a statement of qualification, the [Secretary of State] shall serve the partnership with notice in a record of the [Secretary of State's] determination.

(c) If a limited liability partnership, not later than [60] days after service of the notice under subsection (b), does not cure or demonstrate to the satisfaction of the [Secretary of State] the nonexistence of each ground determined by the [Secretary of State], the [Secretary of State] shall administratively revoke the statement of qualification by signing a statement of administrative revocation that recites the grounds for revocation and the effective date of the revocation. The [Secretary of State] shall file the statement and serve a copy on the partnership pursuant to Section 116.

(d) An administrative revocation under subsection (c) affects only a partnership's status as a limited liability partnership and is not an event causing dissolution of the partnership.

(e) The administrative revocation of a statement of qualification of a limited liability

partnership does not terminate the authority of its registered agent.

Comment

Many failures to comply with statutory requirements that may give rise to administrative revocation occur because of oversight or inadvertence and are usually corrected promptly when brought to the LLP's attention. Subsections (b) and (c) therefore provide a mandatory notice by the filing office to each LLP whose statement of qualification is subject to administrative revocation and a sixty-day grace period following the notice before the statement of administrative revocation may be filed.

In most instances, the issue whether a statement of qualification is subject to administrative revocation will not be controverted. If an LLP's statement of qualification is administratively revoked, the statement is no longer in effect. However, the partnership may petition the filing office for reinstatement under Section 904 and, if reinstatement is denied, the company may appeal to the courts under Section 905.

As a practical matter, administrative revocation permits the filing office to clear the record of "dead wood" and free up names.

However, the consequences for the partners can be quite serious. The liability shield remains effective for debts, liabilities, and other obligations incurred before revocation but disappears as to those incurred subsequently. A reinstated statement of qualification has retroactive effect generally, but exceptions can exist with regard to partnership obligations incurred before reinstatement. *See* Section 904(d)(3). For a discussion of when a partnership obligation is incurred, see the comment to Section 304(c) (The Temporal Nexus – When Claim Incurred).

Subsection (d)—This rule follows from Section 201(b) ("A partnership is the same entity regardless of whether the partnership has a statement of qualification in effect under Section 901.").

SECTION 904. REINSTATEMENT.

(a) A partnership whose statement of qualification has been revoked administratively under Section 903 may apply to the [Secretary of State] for reinstatement of the statement of qualification [not later than [two] years after the effective date of the revocation]. The application must state:

(1) the name of the partnership at the time of the administrative revocation of its statement of qualification and, if needed, a different name that satisfies Section 902;

(2) the address of the principal office of the partnership and the name and street and mailing addresses of its registered agent;

(3) the effective date of administrative revocation of the partnership's statement of qualification; and

(4) that the grounds for revocation did not exist or have been cured.

(b) To have its statement of qualification reinstated, a partnership must pay all fees, taxes, interest, and penalties that were due to the [Secretary of State] at the time of the administrative revocation and all fees, taxes, interest, and penalties that would have been due to the [Secretary of State] while the partnership's statement of qualification was revoked administratively.

(c) If the [Secretary of State] determines that an application under subsection (a) contains the required information, is satisfied that the information is correct, and determines that all payments required to be made to the [Secretary of State] by subsection (b) have been made, the [Secretary of State] shall:

(1) cancel the statement of revocation and prepare a statement of reinstatement that states the [Secretary of State's] determination and the effective date of reinstatement; and

(2) file the statement of reinstatement and serve a copy on the partnership.

(d) When reinstatement under this section has become effective, the following rules apply:

(1) The reinstatement relates back to and takes effect as of the effective date of the administrative revocation.

(2) The partnership's status as a limited liability partnership continues as if the revocation had not occurred.

(3) The rights of a person arising out of an act or omission in reliance on the revocation before the person knew or had notice of the reinstatement are not affected.

Comment

This section is analogous to statutes authorizing reinstatement following administrative dissolution. *See* ULLCA (2006) (Last Amended 2013) § 709; ULPA (2001) (Last Amended 2013) § 812. In that context:

- some states require that reinstatement be sought within two years of administrative dissolution;
- other states provide a longer time, or do not impose any time limit;
- imposing no limit risks abuse by unscrupulous people seeking to reinstate and appropriate for improper ends a dormant entity that has been abandoned by its owners; but
- on the other hand, reinstatement is intended as a safety net for the inattentive and, if the deadline comes too soon, the safety net may be gone before the inattentive even learn that administrative dissolution has occurred.

Subsection (a)(1)—This provision will apply if, before the statement of qualification is reinstated, another entity has taken the company's name. *See* Section 902(c)(2).

Subsection (d)(3)—This paragraph provides an exception to the retroactive effect provided by Paragraphs (1) and (2). The greatest risk resulting from the exception is a creditor's claim of having entered into a contract with the partnership, knowing of the revocation and relying on the vicarious liability of each partner. The exception could also preclude a reinstated LLP's use of its own name. *See* Section 902(c)(2) (indirectly permitting an LLP to use the name of another partnership whose statement of qualification has been administratively revoked). Comparable provisions exist in other uniform acts pertaining to entities. *E.g.*, ULLCA (2006) (Last Amended 2013) § 112(b)(1) .

SECTION 905. JUDICIAL REVIEW OF DENIAL OF REINSTATEMENT.

(a) If the [Secretary of State] denies a partnership's application for reinstatement following administrative revocation of the partnership's statement of qualification, the [Secretary of State] shall serve the partnership with a notice in a record that explains the reasons for the denial.

(b) A partnership may seek judicial review of denial of reinstatement in [the appropriate court] not later than [30] days after service of the notice of denial.

Comment

Because the grounds for administrative revocation under Section 904 are limited and straight forward, it is unlikely there will be a dispute about whether a partnership has corrected the reasons for the administrative revocation of the partnership's statement of qualification. But in the event a partnership disagrees with a determination by the filing office to deny the partnership's application for reinstatement, this section gives the partnership a limited right to seek judicial review of the denial of reinstatement.

SECTION 906. RESERVATION OF NAME.

(a) A person may reserve the exclusive use of a name that complies with Section 902 by delivering an application to the [Secretary of State] for filing. The application must state the name and address of the applicant and the name to be reserved. If the [Secretary of State] finds that the name is available, the [Secretary of State] shall reserve the name for the applicant's exclusive use for [120] days.

(b) The owner of a reserved name may transfer the reservation to another person by delivering to the [Secretary of State] a signed notice in a record of the transfer which states the name and address of the person to which the reservation is being transferred.

Comment

This section does not provide for the renewal of a name reservation for successive 120-day periods. A new reservation may be filed upon the expiration of a reservation, but by requiring a new filing this section creates the possibility that another party may timely submit a reservation for the same name. It was considered appropriate to allow for that possibility so that the procedure in this section cannot be used to block a name indefinitely. *Compare* Section 906, *with* Section 907(d) (authorizing a renewable registration of certain names).

SECTION 907. REGISTRATION OF NAME.

(a) A foreign limited liability partnership not registered to do business in this state under [Article] 10 may register its name, or an alternate name adopted pursuant to Section 902, if the name is distinguishable on the records of the [Secretary of State] from the names that are not available under Section 902.

(b) To register its name or an alternate name adopted pursuant to Section 902, a foreign limited liability partnership must deliver to the [Secretary of State] for filing an application stating the partnership's name, the jurisdiction and date of its formation, and any alternate name adopted pursuant to Section 902. If the [Secretary of State] finds that the name applied for is available, the [Secretary of State] shall register the name for the applicant's exclusive use.

(c) The registration of a name under this section is effective for [one year] after the date of registration.

(d) A foreign limited liability partnership whose name registration is effective may renew the registration for successive [one-year] periods by delivering, not earlier than [three months] before the expiration of the registration, to the [Secretary of State] for filing a renewal application that complies with this section. When filed, the renewal application renews the registration for a succeeding [one-year] period.

(e) A foreign limited liability partnership whose name registration is effective may register as a foreign limited liability partnership under the registered name or consent in a signed record to the use of that name by another person that is not an individual.

Comment

Unlike the reservation of a name under Section 906, a registration of a name under this section may be renewed for successive periods thus permitting a name to be protected for a period longer than the initial registration period. Use of the procedure in this section is limited, however, to the names of foreign limited partnerships, which are not registered to do business in the state. The purpose of this section is to permit a foreign entity to make sure its name will be available if the entity chooses to register in the state in the future.

SECTION 908. REGISTERED AGENT.

(a) Each limited liability partnership and each registered foreign limited liability partnership shall designate and maintain a registered agent in this state. The designation of a registered agent is an affirmation of fact by the partnership or foreign partnership that the agent

has consented to serve.

(b) A registered agent for a limited liability partnership or registered foreign limited liability partnership must have a place of business in this state.

(c) The only duties under this [act] of a registered agent that has complied with this [act] are:

(1) to forward to the limited liability partnership or registered foreign limited liability partnership at the address most recently supplied to the agent by the partnership or foreign partnership any process, notice, or demand pertaining to the partnership or foreign partnership which is served on or received by the agent;

(2) if the registered agent resigns, to provide the notice required by Section 907(c) to the partnership or foreign partnership at the address most recently supplied to the agent by the partnership or foreign partnership; and

(3) to keep current the information with respect to the agent in the statement of qualification or foreign registration statement.

Comment

This section is limited to prescribing the duties of a registered agent under this act. The partnership agreement cannot vary this section. Section 105(c)(16)(A). However, an agent may undertake other responsibilities to a represented limited liability partnership or foreign limited liability partnership, such as by contract or course of dealing, but those duties will be determined under other law.

SECTION 909. CHANGE OF REGISTERED AGENT OR ADDRESS FOR REGISTERED AGENT BY LIMITED LIABILITY PARTNERSHIP.

(a) A limited liability partnership or registered foreign limited liability partnership may change its registered agent or the address of its registered agent by delivering to the [Secretary of State] for filing a statement of change that states:

(1) the name of the partnership or foreign partnership; and

(2) the information that is to be in effect as a result of the filing of the statement of change.

(b) The partners of a limited liability partnership need not approve the delivery to the [Secretary of State] for filing of:

(1) a statement of change under this section; or

(2) a similar filing changing the registered agent or registered office, if any, of the partnership in any other jurisdiction.

(c) A statement of change under this section designating a new registered agent is an affirmation of fact by the limited liability partnership or registered foreign limited liability partnership that the agent has consented to serve.

(d) As an alternative to using the procedure in this section, a limited liability partnership may amend its statement of qualification.

Comment

A change in the identity of the registered agent of an LLP or registered foreign LLP or a change of the office address of a partnership's registered agent are usually routine matters that do not affect the rights of the partners of the represented LLP. This section permits those changes to be made without: (i) amendment of an LLP's statement of qualification or a registered foreign LLPs registration; and (ii) any approval by an LLP's partners. For the registered agent's power to resign, see Section 910. For the registered agent's power to change its name, address, or both, see Section 911.

Subsection (c)—This subsection avoids the need to file with a statement of change consent of the new registered agent being designated.

Subsection (d)—This subsection makes clear that the procedures in this section are not exclusive. A common way in which a limited liability partnership changes its registered agent is to include the change in its annual/biennial report. *See* Section 913(e).

SECTION 910. RESIGNATION OF REGISTERED AGENT.

(a) A registered agent may resign as an agent for a limited liability partnership or

registered foreign limited liability partnership by delivering to the [Secretary of State] for filing a statement of resignation that states:

- (1) the name of the partnership or foreign partnership;
- (2) the name of the agent;
- (3) that the agent resigns from serving as registered agent for the partnership or foreign partnership; and
- (4) the address of the partnership or foreign partnership to which the agent will send the notice required by subsection (c).

(b) A statement of resignation takes effect on the earlier of:

- (1) the 31st day after the day on which it is filed by the [Secretary of State]; or
- (2) the designation of a new registered agent for the limited liability partnership or registered foreign limited liability partnership.

(c) A registered agent promptly shall furnish to the limited liability partnership or registered foreign limited liability partnership notice in a record of the date on which a statement of resignation was filed.

(d) When a statement of resignation takes effect, the registered agent ceases to have responsibility under this [act] for any matter thereafter tendered to it as agent for the limited liability partnership or registered foreign limited liability partnership. The resignation does not affect any contractual rights the partnership or foreign partnership has against the agent or that the agent has against the partnership or foreign partnership.

(e) A registered agent may resign with respect to a limited liability partnership or registered foreign limited liability partnership whether or not the partnership or foreign partnership is in good standing.

Comment

Resignation under this section may be accomplished solely by action of the registered agent and does not require the cooperation or consent of the represented LLP or registered foreign LLP. Whether a resignation violates a contract between the registered agent and the partnership is beyond the scope of this act, and Subsection (d) preserves whatever claims a represented LLC may have against its registered agent for a wrongful termination. Even if a resignation were to violate such a contract, the resignation would still be effective if the provisions of this section were followed.

Subsection (b)—This subsection delays the effectiveness of a statement of resignation for thirty-one days to allow the notice of the resignation that must be sent under Subsection (c) to reach the represented LLP or registered foreign LLP and to allow the represented LLP to arrange for a substitute registered agent.

Subsection (e)—This subsection makes clear that a registered agent may resign with respect to an LLP or registered foreign LLP that is not in good standing and supersedes the contrary administrative practice in some states of refusing to accept any filings with respect to an entity that is not in good standing until the problem with the entity's standing is cured.

SECTION 911. CHANGE OF NAME OR ADDRESS BY REGISTERED AGENT.

(a) If a registered agent changes its name or address, the agent may deliver to the [Secretary of State] for filing a statement of change that states:

(1) the name of the limited liability partnership or registered foreign limited liability partnership represented by the registered agent;

(2) the name of the agent as currently shown in the records of the [Secretary of State] for the partnership or foreign partnership;

(3) if the name of the agent has changed, its new name; and

(4) if the address of the agent has changed, its new address.

(b) A registered agent promptly shall furnish notice to the represented limited liability partnership or registered foreign limited liability partnership of the filing by the [Secretary of State] of the statement of change and the changes made by the statement.

Legislative Note: *Many registered agents act in that capacity for many entities, and the Model Registered Agents Act (2006) (Last Amended 2013) provides a streamlined method through*

which a commercial registered agent can make a single filing to change its information for all represented entities. The single filing does not prevent an enacting state from assessing filing fees on the basis of the number of entity records affected. Alternatively the fees can be set on an incremental sliding fee or capitated amount based upon potential economies of costs for a bulk filing.

Comment

This section permits a registered agent to change the name and address of the agent that appears in the registered agent filing of an LLP or registered foreign LLP represented by the agent. This act does not provide for commercial registered agents, *contra* UBOC (2011) (Last Amended 2013) §§ 1-405, 1-406, 1-409. As a result, a registered agent will need to make a separate filing under this section for each LLP and registered foreign LLP represented by the agent, unless, if authorized by rule or administrative policy, the filing office establishes procedures for a bulk filing with one filing listing the names of all the registered agent's represented entities.

SECTION 912. SERVICE OF PROCESS, NOTICE, OR DEMAND.

(a) A limited liability partnership or registered foreign limited liability partnership may be served with any process, notice, or demand required or permitted by law by serving its registered agent.

(b) If a limited liability partnership or registered foreign limited liability partnership ceases to have a registered agent, or if its registered agent cannot with reasonable diligence be served, the partnership or foreign partnership may be served by registered or certified mail, return receipt requested, or by similar commercial delivery service, addressed to the partnership or foreign partnership at its principal office. The address of the principal office must be as shown in the partnership's or foreign partnership's most recent [annual] [biennial] report filed by the [Secretary of State]. Service is effected under this subsection on the earliest of:

(1) the date the partnership or foreign partnership receives the mail or delivery by the commercial delivery service;

(2) the date shown on the return receipt, if signed by the partnership or foreign partnership; or

(3) five days after its deposit with the United States Postal Service, or with the commercial delivery service, if correctly addressed and with sufficient postage or payment.

(c) If process, notice, or demand cannot be served on a limited liability partnership or registered foreign limited liability partnership pursuant to subsection (a) or (b), service may be made by handing a copy to the individual in charge of any regular place of business of the partnership or foreign partnership if the individual served is not a plaintiff in the action.

(d) Service of process, notice, or demand on a registered agent must be in a written record.

(e) Service of process, notice, or demand may be made by other means under law other than this [act].

Comment

Subsection (b)—This subsection offers three alternative methods for establishing the date service is effected, a date important for determining the time within which an LLP or registered foreign LLP must respond to the process, notice, or demand served. Under Subsection (b)(1), service is effected on the date of receipt by the partnership of the mail or commercial delivery. Under Subsection (b)(2), service is effected on the date shown on the return receipt, if signed on behalf of the partnership. Under Subsection (b)(3), service is effected five days after it is deposited with the Postal Service or with a similar commercial delivery service, if correctly addressed and with correct postage or payment. Service is effective at the earliest of the three listed circumstances.

However, for the party effecting service there are difficulties of proof under the first two circumstances. Under Subsection (b)(1) the exact date of the receipt by the LLP or registered foreign LLP of mail or commercial delivery is peculiarly within the knowledge of the partnership. Under Subsection (b)(2) the return receipt must be signed on behalf of the partnership. That requirement is designed to assure that the service is actually received by the partnership, but the signature on the return receipt may not always show unambiguously that the signer was acting for the partnership and was authorized to do so. As a practical matter, therefore, parties effecting service under Subsection (b) may find it most convenient to rely on Subsection (b)(3) and to maintain their own records so that the date of deposit in the mails or with a commercial delivery service can easily be established.

Subsection (c)—This subsection provides a means for serving process on an LLP or registered foreign LLP that cannot be served under Subsection (a) or (b). In such circumstances, some statutes require or permit service of process to be made on the filing office.

Subsection (e)—For an example, see, *e.g.*, FED. R. CIV. P. 4(h)(1)(B) (authorizing service on “a domestic or foreign corporation, or a partnership or other unincorporated association that is subject to suit under a common name” to be made on “an officer, a managing or general agent, or any other agent authorized by appointment or by law to receive service of process”).

SECTION 913. [ANNUAL] [BIENNIAL] REPORT FOR [SECRETARY OF STATE].

(a) A limited liability partnership or registered foreign limited liability partnership shall deliver to the [Secretary of State] for filing [an annual] [a biennial] report that states:

- (1) the name of the partnership or registered foreign partnership;
- (2) the name and street and mailing addresses of its registered agent in this state;
- (3) the street and mailing addresses of its principal office;
- (4) the name of at least one partner; and
- (5) in the case of a foreign partnership, its jurisdiction of formation and any

alternate name adopted under Section 1006.

(b) Information in the [annual] [biennial] report must be current as of the date the report is signed by the limited liability partnership or registered foreign limited liability partnership.

(c) The first [annual] [biennial] report must be delivered to the [Secretary of State] for filing after [January 1] and before [April 1] of the year following the calendar year in which the limited liability partnership’s statement of qualification became effective or the registered foreign limited liability partnership registered to do business in this state. Subsequent [annual] [biennial] reports must be delivered to the [Secretary of State] for filing after [January 1] and before [April 1] of each [second] calendar year thereafter.

(d) If [an annual] [a biennial] report does not contain the information required by this section, the [Secretary of State] promptly shall notify the reporting limited liability partnership or registered foreign limited liability partnership in a record and return the report for

correction.

(e) If [an annual] [a biennial] report contains the name or address of a registered agent which differs from the information shown in the records of the [Secretary of State] immediately before the report becomes effective, the differing information is considered a statement of change under Section 909.

Comment

In some states, an annual or biennial report by a limited liability partnership or a registered foreign limited liability partnership will be a new requirement.

Subsection (a)(4)—The requirement that the report include the name of at least one partner will be a new requirement in some states. There has been increasing pressure from law enforcement agencies for access to more information about the ownership and control of legal entities. This requirement will enable law enforcement to contact a person with some knowledge about the affairs of the limited liability partnership. Members of the public will also have that ability.

[ARTICLE] 10

FOREIGN LIMITED LIABILITY PARTNERSHIP

SECTION 1001. GOVERNING LAW.

(a) The law of the jurisdiction of formation of a foreign limited liability partnership governs:

- (1) the internal affairs of the partnership; and
- (2) the liability of a partner as partner for a debt, obligation, or other liability of the foreign partnership.

(b) A foreign limited liability partnership is not precluded from registering to do business in this state because of any difference between the law of its jurisdiction of formation and the law of this state.

(c) Registration of a foreign limited liability partnership to do business in this state does

not authorize the foreign partnership to engage in any business or exercise any power that a limited liability partnership may not engage in or exercise in this state.

Comment

For the purposes of this section, “jurisdiction of formation” refers to the jurisdiction under whose law a foreign partnership became a limited liability partnership. Strictly speaking, becoming an LLP involves transforming an already existing entity, not forming a new one. *Cf.* Section 201(b) (making this point as to domestic LLPs).

Subsection (a)—This subsection provides that the laws of the jurisdiction of formation of a foreign LLP, rather than the laws of this state, govern both the internal affairs of the foreign LLP and the liability of its partners for the obligations of the LLP. A partnership agreement cannot change this provision. Section 105(c)(17).

This subdivision parallels Section 104(1) (pertaining to the governing law for domestic LLPs). *See* the comment to Section 104(1).

Subsections (b) and (c)—These sections together make clear that, although a foreign LLP may not be denied registration simply because of a difference between the laws of its jurisdiction of formation and the laws of this state, the foreign limited liability partnership “may not engage in any activity or exercise any power a domestic LLP may not engage in or exercise in this state.” Subsection (c).

SECTION 1002. REGISTRATION TO DO BUSINESS IN THIS STATE.

(a) A foreign limited liability partnership may not do business in this state until it registers with the [Secretary of State] under this [article].

(b) A foreign limited liability partnership doing business in this state may not maintain an action or proceeding in this state unless it has registered to do business in this state.

(c) The failure of a foreign limited liability partnership to register to do business in this state does not impair the validity of a contract or act of the foreign partnership or preclude it from defending an action or proceeding in this state.

(d) A limitation on the liability of a partner of a foreign limited liability partnership is not waived solely because the foreign partnership does business in this state without registering to do business in this state.

(e) Section 1001(a) and (b) applies even if a foreign limited liability partnership fails to register under this [article].

Comment

Subsection (a)—Following a long-established tradition, this act does not state what constitutes “do[ing] business in this state.” Instead, Section 1005 provides a non-exhaustive list of “[a]ctivities of a foreign limited liability partnership which do not constitute doing business in this state.”

Subsection (b)—The purpose of this subsection is to induce foreign limited liability partnerships to register without imposing harsh or erratic sanctions. Often the failure to register is a result of inadvertence or bona fide disagreement as to the scope of Section 1005, which is necessarily imprecise. Thus, the imposition of harsh sanctions in those situations is inappropriate. The sanction of closing the courts of the state to suits brought by foreign LLPs that should have registered is not a punitive one. If a foreign LLP should have registered and failed to do so, it may still enforce its contractual and other rights simply by registering.

However, if a court dismisses a case under this subsection rather than staying the proceedings pending the foreign LLP’s registration, a statute of limitations problem may occur. *Corco, Inc. v. Ledar Transport, Inc.* 946 P.2d 1009, 1010 (Kan. Ct. App. 1997) (“[T]he proper remedy was to dismiss [the unregistered entity’s] counterclaim without prejudice rather than with prejudice. This would leave [the entity] the opportunity to comply with the statutes and then reassert its claim against [the defendant]. On the other hand, it would also leave the risk that the statute of limitations might run against [the entity].”).

This subsection does not prevent a foreign LLP that has failed to register from “defending” an action or proceeding. The distinction between “maintaining” an action or proceeding under this subsection and “defending” an action or proceeding under Subsection (c) is determined on the basis of whether affirmative relief is sought. A nonregistered foreign LLP may interpose any defense or permissive or mandatory counterclaim to defeat a claimed recovery, but may not obtain an affirmative judgment based on the counterclaim without first registering.

Subsection (c)—In addition to permitting a non-registered foreign LLP doing business in this state to defend (but not maintain) an action or proceeding, this section makes clear that failure to register does not impair the validity of a foreign LLP’s acts.

Subsection (d)—This subsection preserves the effectiveness of a foreign LLP’s liability shield applicable under the LLP’s governing law.

SECTION 1003. FOREIGN REGISTRATION STATEMENT. To register to do business in this state, a foreign limited liability partnership must deliver a foreign registration

statement to the [Secretary of State] for filing. The statement must state:

- (1) the name of the partnership and, if the name does not comply with Section 902, an alternate name adopted pursuant to Section 1006(a);
- (2) that the partnership is a foreign limited liability partnership;
- (3) the partnership's jurisdiction of formation;
- (4) the street and mailing addresses of the partnership's principal office and, if the law of the partnership's jurisdiction of formation requires the partnership to maintain an office in that jurisdiction, the street and mailing addresses of the required office; and
- (5) the name and street and mailing addresses of the partnership's registered agent in this state.

Comment

The foreign registration statement provides certain basic information about the foreign limited liability partnership to ensure that citizens of the state have access to that information in their dealings with the foreign partnership. The statement also facilitates making the foreign partnership subject to the jurisdiction of the courts of the state.

Once registered, a foreign limited liability partnership must file an annual/biennial report. Section 913.

For the purposes of this section, "jurisdiction of formation" refers to the jurisdiction under whose law a foreign partnership became a limited liability partnership. Strictly speaking, becoming an LLP involves transforming an already existing entity, not forming a new one. *See* Section 201(b).

SECTION 1004. AMENDMENT OF FOREIGN REGISTRATION STATEMENT.

A registered foreign limited liability partnership shall deliver to the [Secretary of State] for filing an amendment to its foreign registration statement if there is a change in:

- (1) the name of the partnership;
- (2) the partnership's jurisdiction of formation;
- (3) an address required by Section 1003(4); or

(4) the information required by Section 1003(5).

Comment

This section works in tandem with the annual/biennial report required by Section 913 to keep up to date the information of record in the filing office about a registered foreign limited partnership.

SECTION 1005. ACTIVITIES NOT CONSTITUTING DOING BUSINESS.

(a) Activities of a foreign limited liability partnership which do not constitute doing business in this state under this [article] include:

- (1) maintaining, defending, mediating, arbitrating, or settling an action or proceeding;
- (2) carrying on any activity concerning its internal affairs, including holding meetings of its partners;
- (3) maintaining accounts in financial institutions;
- (4) maintaining offices or agencies for the transfer, exchange, and registration of securities of the partnership or maintaining trustees or depositories with respect to those securities;
- (5) selling through independent contractors;
- (6) soliciting or obtaining orders by any means if the orders require acceptance outside this state before they become contracts;
- (7) creating or acquiring indebtedness, mortgages, or security interests in property;
- (8) securing or collecting debts or enforcing mortgages or security interests in property securing the debts and holding, protecting, or maintaining property;
- (9) conducting an isolated transaction that is not in the course of similar

transactions;

(10) owning, without more, property; and

(11) doing business in interstate commerce.

(b) A person does not do business in this state solely by being a partner of a foreign limited liability partnership that does business in this state.

(c) This section does not apply in determining the contacts or activities that may subject a foreign limited liability partnership to service of process, taxation, or regulation under law of this state other than this [act].

Comment

This act does not attempt to formulate an inclusive definition of what constitutes doing business in a state. Rather, the concept is defined in a negative fashion by Subsections (a) and (b), which state that certain activities do not constitute doing business.

In general terms, any conduct more regular, systematic, or extensive than that described in Subsection (a) constitutes doing business and requires the foreign limited liability partnership to register to do business. Typical conduct requiring registration includes maintaining an office to conduct local intrastate business, selling personal property not in interstate commerce, entering into contracts relating to the local business or sales, and owning or using real estate for general purposes. But the passive owning of real estate for investment purposes does not constitute doing business. *See* Subsection (a)(10).

The test of “doing business” defined in a negative way in Subsections (a) and (b) applies only to the question whether a foreign limited liability partnership’s contacts with the state are such that it must register under this section. The test is not applicable to other questions such as whether the foreign LLP is amenable to service of process under state “long-arm” statutes or liable for state or local taxes. A foreign LLP that has registered (or is required to register) will generally be subject to suit and state taxation in the state, while a foreign LLP that is subject to service of process or state taxation in a state will not necessarily be required to register.

Subsection (a)—The list of activities set forth in this subsection is not exhaustive.

Subsection (a)(1)—A foreign limited liability partnership is not “doing business” solely because it resorts to the courts of the state to recover an indebtedness, enforce an obligation, recover possession of personal property, obtain the appointment of a receiver, intervene in a pending proceeding, bring a petition to compel arbitration, file an appeal bond, or pursue appellate remedies. Similarly, a foreign LLP is not required to register merely because it files a complaint with a governmental agency or participates in an administrative proceeding within the

state.

Subsection (a)(2)—A foreign limited liability partnership does not “do business” within a state under this section merely because some of its internal affairs occur within a state. Thus, a foreign LLP may hold meetings of its partners within a state without first registering. A foreign LLP also may maintain offices or agencies within a state relating solely to the transfer, exchange or registration of its interests without registering. Other activities relating to the internal affairs of the foreign LLP that do not constitute doing business under this section include having officers or representatives who reside within or are physically present in the state; while there, the officers or representatives may make executive decisions relating to the internal affairs of the foreign LLP without imposing on the foreign LLP the requirement that it register, if these activities are not so regular and systematic as to cause the residence to be viewed as a business office.

Subsection (a)(5)—Under this paragraph, a foreign limited liability partnership need not register if it sells goods in the state through independent contractors. These transactions are viewed as transactions by the independent contractors, not by the foreign LLP itself even though the foreign LLP sets some limits or ground rules for its contractors. If these controls are sufficiently pervasive, however, the foreign LLP may be deemed to be selling for itself in intrastate commerce, and not through the independent contractors and therefore engaged in doing business in the state.

Subsection (a)(7) and (8)—The mere act of making a loan by a foreign limited liability partnership that is not in the business of making loans does not constitute doing business in the state in which the loan is made. On the same theory, a foreign LLP may obtain security for the repayment of a loan, and foreclose or enforce the lien or security interest to collect the loan, without being deemed to be doing business. Similarly, a refunding or “roll over” of a loan or its adjustment or compromise does not involve doing business.

Subsection (a)(9)—The concept of “doing business” involves regular, repeated, and continuing business contacts of a local nature. A single agreement or isolated transaction within a state does not constitute doing business if there is no intention to repeat the transaction or engage in similar transactions. This act does not impose the limitation found in some statutes, such as Section 15.01(b)(10) of the Model Business Corporation Act, that the isolated transaction be completed within thirty days. A foreign LLP should not be required to register simply because it engages in an isolated transaction that takes longer than thirty days to complete.

Subsection (a)(11)—A foreign limited liability partnership is not “doing business” within the meaning of this section if it is transacting business in interstate commerce. *See* Subsection (a)(6) (stating that soliciting or obtaining orders that must be accepted outside the state before they become contracts is not “doing business” within the meaning of this section).

These exclusions reflect the provisions of the United States Constitution that grant to the United States Congress exclusive power over interstate commerce, and preclude states from imposing restrictions or conditions upon this commerce. This subsection should be construed in a manner consistent with judicial decisions under the United States Constitution. Under these

decisions, a foreign entity is not required to register even though it sells goods within the state if they are shipped to the purchasers in interstate commerce. Thus a foreign LLP need not register even if it also does work and performs acts within the state incidental to the interstate business (*e.g.*, if it takes or enforces a security interest incidental to these transactions). Nor is it required to register merely because it sends traveling salespeople or solicitors into a state so long as contracts are not made within the state. Similarly, an office may be maintained by a foreign LLP in this state without registering if the office's functions relate solely to interstate commerce. Purchases of goods may of course be in interstate commerce as readily as sales. Thus, the purchase of personal property in this state by a foreign limited liability partnership for shipment in interstate commerce out of the state does not require the entity to register.

SECTION 1006. NONCOMPLYING NAME OF FOREIGN LIMITED LIABILITY PARTNERSHIP.

(a) A foreign limited liability partnership whose name does not comply with Section 902 may not register to do business in this state until it adopts, for the purpose of doing business in this state, an alternate name that complies with Section 902. A partnership that registers under an alternate name under this subsection need not comply with [this state's assumed or fictitious name statute]. After registering to do business in this state with an alternate name, a partnership shall do business in this state under:

- (1) the alternate name;
- (2) the partnership's name, with the addition of its jurisdiction of formation; or
- (3) a name the partnership is authorized to use under [this state's assumed or fictitious name statute].

(b) If a registered foreign limited liability partnership changes its name to one that does not comply with Section 902, it may not do business in this state until it complies with subsection (a) by amending its registration to adopt an alternate name that complies with Section 902.

Comment

A foreign limited liability partnership must register under its true name if that name

satisfies the requirements of Section 902. If the true name is unavailable because it is not distinguishable upon the records of the filing office from a name already in use or reserved or registered, the foreign LLP may use an alternate name.

A foreign limited liability partnership that registers to do business in the state may do business under a fictitious name to the same extent as a domestic entity.

SECTION 1007. WITHDRAWAL DEEMED ON CONVERSION TO DOMESTIC FILING ENTITY OR DOMESTIC LIMITED LIABILITY PARTNERSHIP. A registered foreign limited liability partnership that converts to a domestic limited liability partnership or to a domestic entity whose formation requires the delivery of a record to the [Secretary of State] for filing is deemed to have withdrawn its registration on the effective date of the conversion.

Comment

When a registered foreign limited liability partnership has converted to a domestic “filing entity” or domestic limited liability partnership, information about the entity in its capacity as a domestic entity will continue to be of record in the filing office. At that point, there is no further reason for the entity to be registered as a foreign LLP, and this section automatically treats its prior registration as withdrawn.

SECTION 1008. WITHDRAWAL ON DISSOLUTION OR CONVERSION TO NONFILING ENTITY OTHER THAN LIMITED LIABILITY PARTNERSHIP.

(a) A registered foreign limited liability partnership that has dissolved and completed winding up or has converted to a domestic or foreign entity whose formation does not require the public filing of a record, other than a limited liability partnership, shall deliver a statement of withdrawal to the [Secretary of State] for filing. The statement must state:

(1) in the case of a partnership that has completed winding up:

(A) its name and jurisdiction of formation;

(B) that the partnership surrenders its registration to do business in this

state; and

(2) in the case of a partnership that has converted:

(A) the name of the converting partnership and its jurisdiction of formation;

(B) the type of entity to which the partnership has converted and its jurisdiction of formation;

(C) that the converted entity surrenders the converting partnership's registration to do business in this state and revokes the authority of the converting partnership's registered agent to act as registered agent in this state on behalf of the partnership or the converted entity; and

(D) a mailing address to which service of process may be made under subsection (b).

(b) After a withdrawal under this section becomes effective, service of process in any action or proceeding based on a cause of action arising during the time the foreign limited liability partnership was registered to do business in this state may be made pursuant to Section 909.

Comment

When a registered foreign limited liability partnership has dissolved and completed winding up, or has converted to a "nonfiling entity" other than a limited liability partnership, there is no further reason for information about the entity to appear in the records of the filing office. This section thus requires delivery of a statement of withdrawal for the purpose of removing the foreign LLP from the rolls of registered foreign entities.

Subsection (a)—The exclusion of limited liability partnerships from this provision is merely technical; Section 1007 covers conversion to a domestic LLP.

SECTION 1009. TRANSFER OF REGISTRATION.

(a) When a registered foreign limited liability partnership has merged into a foreign entity that is not registered to do business in this state or has converted to a foreign entity required to register with the [Secretary of State] to do business in this state, the foreign entity

shall deliver to the [Secretary of State] for filing an application for transfer of registration. The application must state:

(1) the name of the registered foreign limited partnership before the merger or conversion;

(2) that before the merger or conversion the registration pertained to a foreign limited liability partnership;

(3) the name of the applicant foreign entity into which the foreign limited liability partnership has merged or to which it has been converted and, if the name does not comply with Section 902, an alternate name adopted pursuant to Section 1006(a);

(4) the type of entity of the applicant foreign entity and its jurisdiction of formation;

(5) the street and mailing addresses of the principal office of the applicant foreign entity and, if the law of that entity's jurisdiction of formation requires the entity to maintain an office in that jurisdiction, the street and mailing addresses of that office; and

(6) the name and street and mailing addresses of the applicant foreign entity's registered agent in this state.

(b) When an application for transfer of registration takes effect, the registration of the foreign limited liability limited partnership to do business in this state is transferred without interruption to the foreign entity into which the partnership has merged or to which it has been converted.

Comment

The purpose of this section is to clarify the status of the foreign limited liability partnership in the public records of the state. A filing under this section has the two-fold effect of canceling the authority of the foreign LLP to do business in the state while at the same time reregistering the former foreign LLP as the new type of foreign entity. If the reregistered foreign

entity subsequently wishes to cancel its registration to do business in the state, it may do so under the statute of this state pertaining the registration of the new type of foreign entity.

SECTION 1010. TERMINATION OF REGISTRATION.

(a) The [Secretary of State] may terminate the registration of a registered foreign limited liability partnership in the manner provided in subsections (b) and (c) if the partnership does not:

(1) pay, not later than [60] days after the due date, any fee, tax, interest, or penalty required to be paid to the [Secretary of State] under this [act] or law other than this [act];

(2) deliver to the [Secretary of State] for filing, not later than [60] days after the due date, [an annual] [a biennial] report required under Section 913;

(3) have a registered agent as required by Section 908; or

(4) deliver to the [Secretary of State] for filing a statement of a change under Section 909 not later than [30] days after a change has occurred in the name or address of the registered agent.

(b) The [Secretary of State] may terminate the registration of a registered foreign limited liability partnership by:

(1) filing a notice of termination or noting the termination in the records of the [Secretary of State]; and

(2) delivering a copy of the notice or the information in the notation to the partnership's registered agent or, if the partnership does not have a registered agent, to the partnership's principal office.

(c) A notice or information in a notation under subsection (b) must include:

(1) the effective date of the termination, which must be at least [60] days after the

date the [Secretary of State] delivers the copy; and

(2) the grounds for termination under subsection (a).

(d) The authority of a registered foreign limited liability partnership to do business in this state ceases on the effective date of the notice of termination or notation under subsection (b), unless before that date the partnership cures each ground for termination stated in the notice or notation. If the partnership cures each ground, the [Secretary of State] shall file a record so stating.

Comment

This section is analogous to the procedures for administrative revocation under Section 903.

SECTION 1011. WITHDRAWAL OF REGISTRATION OF REGISTERED FOREIGN LIMITED LIABILITY PARTNERSHIP.

(a) A registered foreign limited liability partnership may withdraw its registration by delivering a statement of withdrawal to the [Secretary of State] for filing. The statement of withdrawal must state:

(1) the name of the partnership and its jurisdiction of formation;

(2) that the partnership is not doing business in this state and that it withdraws its registration to do business in this state;

(3) that the partnership revokes the authority of its registered agent to accept service on its behalf in this state; and

(4) an address to which service of process may be made under subsection (b).

(b) After the withdrawal of the registration of a foreign limited liability partnership, service of process in any action or proceeding based on a cause of action arising during the time the partnership was registered to do business in this state may be made pursuant to Section 909.

Comment

The statement of withdrawal must set forth an address where service of process may be made on the foreign limited liability partnership pursuant to Section 912. There is no limit on how long the withdrawn partnership must keep that address up to date.

SECTION 1012. ACTION BY [ATTORNEY GENERAL]. The [Attorney General] may maintain an action to enjoin a foreign limited liability partnership from doing business in this state in violation of this [article].

Comment

The authority stated here has been part of corporate law for more than a century and has been carried over into the law of unincorporated business entities. Nowadays, the authority is rarely if ever invoked in either realm of entity law.

[ARTICLE] 11

MERGER, INTEREST EXCHANGE, CONVERSION, AND DOMESTICATION

Introductory Comment

This article deals comprehensively with both same-type and cross-type mergers and interest exchanges and with conversions and domestications. For this article to apply, at least one participant organization must be a domestic general partnership (regardless of whether the partnership is an LLP). For a foreign organization to be involved, its organic law must permit the organization's participation.

Part 1 contains definitions specific to this article as well as provisions applicable to all transactions authorized by this article.

Part 2 governs mergers and is an amalgamation of existing entity law, both unincorporated and incorporated.

Part 3 governs interest exchanges, previously a feature only of corporate law. Part 3 is derived from the share exchange provisions in Chapter 11 of the Model Business Corporation Act.

Part 4 governs conversions, a one-step procedure by which an entity changes from one type of entity to another type while nonetheless continuing in existence as the same legal entity.

Part 5 governs domestications, a procedure by which a domestic limited liability partnership can become a foreign limited liability partnership or vice versa, in each instance with the partnership remaining the same legal entity.

Part 2 sets the paradigm for Parts 3, 4, and 5, because mergers are long established, and merger rules and concepts are familiar to business lawyers. Moreover, conversions and domestications could formerly be accomplished via mergers (with a new entity), and an interest exchange produces the same result as a triangular merger. The comments to Part 2 are thus relevant to understanding Parts 3, 4, and 5.

This article contemplates transactions in which the surviving entity is neither a filing entity nor otherwise of record in the filing office (*e.g.*, the merger of an LLC into a non-LLP general partnership). As a result, a filing under this article may be the first time that a filing office takes cognizance of an entity's existence.

[PART] 1

GENERAL PROVISIONS

SECTION 1101. DEFINITIONS. In this [article]:

(1) “Acquired entity” means the entity, all of one or more classes or series of interests of which are acquired in an interest exchange.

(2) “Acquiring entity” means the entity that acquires all of one or more classes or series of interests of the acquired entity in an interest exchange.

(3) “Conversion” means a transaction authorized by [Part] 4.

(4) “Converted entity” means the converting entity as it continues in existence after a conversion.

(5) “Converting entity” means the domestic entity that approves a plan of conversion pursuant to Section 1143 or the foreign entity that approves a conversion pursuant to the law of its jurisdiction of formation.

(6) “Distributional interest” means the right under an unincorporated entity's organic law and organic rules to receive distributions from the entity.

(7) “Domestic”, with respect to an entity, means governed as to its internal affairs by the law of this state.

(8) “Domesticated limited liability partnership” means a domesticating limited liability

partnership as it continues in existence after a domestication.

(9) “Domesticating limited liability partnership” means the domestic limited liability partnership that approves a plan of domestication pursuant to Section 1153 or the foreign limited liability partnership that approves a domestication pursuant to the law of its jurisdiction of formation.

(10) “Domestication” means a transaction authorized by [Part] 5.

(11) “Entity”:

(A) means:

- (i) a business corporation;
- (ii) a nonprofit corporation;
- (iii) a general partnership, including a limited liability partnership;
- (iv) a limited partnership, including a limited liability limited partnership;
- (v) a limited liability company;
- [(vi) a general cooperative association;]
- (vii) a limited cooperative association;
- (viii) an unincorporated nonprofit association;
- (ix) a statutory trust, business trust, or common-law business trust; or
- (x) any other person that has:

(I) a legal existence separate from any interest holder of that person; or

(II) the power to acquire an interest in real property in its own name; and

(B) does not include:

- (i) an individual;
- (ii) a trust with a predominantly donative purpose or a charitable trust;
- (iii) an association or relationship that is not an entity listed in

subparagraph (A) and is not a partnership under the rules stated in [Section 202(c) of the Uniform Partnership Act (1997) (Last Amended 2013)] [Section 7 of the Uniform Partnership Act (1914)] or a similar provision of the law of another jurisdiction;

(iv) a decedent's estate; or

(v) a government or a governmental subdivision, agency, or

instrumentality.

(12) "Filing entity" means an entity whose formation requires the filing of a public organic record. The term does not include a limited liability partnership.

(13) "Foreign", with respect to an entity, means an entity governed as to its internal affairs by the law of a jurisdiction other than this state.

(14) "Governance interest" means a right under the organic law or organic rules of an unincorporated entity, other than as a governor, agent, assignee, or proxy, to:

(A) receive or demand access to information concerning, or the books and records of, the entity;

(B) vote for or consent to the election of the governors of the entity; or

(C) receive notice of or vote on or consent to an issue involving the internal affairs of the entity.

(15) "Governor" means:

(A) a director of a business corporation;

(B) a director or trustee of a nonprofit corporation;

- (C) a general partner of a general partnership;
- (D) a general partner of a limited partnership;
- (E) a manager of a manager-managed limited liability company;
- (F) a member of a member-managed limited liability company;
- [(G) a director of a general cooperative association;]
- (H) a director of a limited cooperative association;
- (I) a manager of an unincorporated nonprofit association;
- (J) a trustee of a statutory trust, business trust, or common-law business trust; or
- (K) any other person under whose authority the powers of an entity are exercised and under whose direction the activities and affairs of the entity are managed pursuant to the organic law and organic rules of the entity.

(16) “Interest” means:

- (A) a share in a business corporation;
- (B) a membership in a nonprofit corporation;
- (C) a partnership interest in a general partnership;
- (D) a partnership interest in a limited partnership;
- (E) a membership interest in a limited liability company;
- [(F) a share in a general cooperative association;]
- (G) a member’s interest in a limited cooperative association;
- (H) a membership in an unincorporated nonprofit association;
- (I) a beneficial interest in a statutory trust, business trust, or common-law business trust; or
- (J) a governance interest or distributional interest in any other type of

unincorporated entity.

(17) “Interest Exchange” means a transaction authorized by [Part] 3.

(18) “Interest holder” means:

(A) a shareholder of a business corporation;

(B) a member of a nonprofit corporation;

(C) a general partner of a general partnership;

(D) a general partner of a limited partnership;

(E) a limited partner of a limited partnership;

(F) a member of a limited liability company;

[(G) a shareholder of a general cooperative association;]

(H) a member of a limited cooperative association;

(I) a member of an unincorporated nonprofit association;

(J) a beneficiary or beneficial owner of a statutory trust, business trust, or

common-law business trust; or

(K) any other direct holder of an interest.

(19) “Interest holder liability” means:

(A) personal liability for a liability of an entity which is imposed on a person:

(i) solely by reason of the status of the person as an interest holder; or

(ii) by the organic rules of the entity which make one or more specified

interest holders or categories of interest holders liable in their capacity as interest holders for all

or specified liabilities of the entity; or

(B) an obligation of an interest holder under the organic rules of an entity to

contribute to the entity.

(20) “Merger” means a transaction authorized by [Part] 2.

(21) “Merging entity” means an entity that is a party to a merger and exists immediately before the merger becomes effective.

(22) “Organic law” means the law of an entity’s jurisdiction of formation governing the internal affairs of the entity.

(23) “Organic rules” means the public organic record and private organic rules of an entity.

(24) “Plan” means a plan of merger, plan of interest exchange, plan of conversion, or plan of domestication.

(25) “Plan of conversion” means a plan under Section 1142.

(26) “Plan of domestication” means a plan under Section 1152.

(27) “Plan of interest exchange” means a plan under Section 1132.

(28) “Plan of merger” means a plan under Section 1122.

(29) “Private organic rules” means the rules, whether or not in a record, that govern the internal affairs of an entity, are binding on all its interest holders, and are not part of its public organic record, if any. The term includes:

(A) the bylaws of a business corporation;

(B) the bylaws of a nonprofit corporation;

(C) the partnership agreement of a general partnership;

(D) the partnership agreement of a limited partnership;

(E) the operating agreement of a limited liability company;

[(F) the bylaws of a general cooperative association;]

(G) the bylaws of a limited cooperative association;

(H) the governing principles of an unincorporated nonprofit association; and

(I) the trust instrument of a statutory trust or similar rules of a business trust or common-law business trust.

(30) “Protected agreement” means:

(A) a record evidencing indebtedness and any related agreement in effect on [the effective date of this [act]]; or

(B) an agreement that is binding on an entity on [the effective date of this [act]]; or

(C) the organic rules of an entity in effect on [the effective date of this [act]]; or

(D) an agreement that is binding on any of the governors or interest holders of an entity on [the effective date of this [act]].

(31) “Public organic record” means the record the filing of which by the [Secretary of State] is required to form an entity and any amendment to or restatement of that record. The term includes:

(A) the articles of incorporation of a business corporation;

(B) the articles of incorporation of a nonprofit corporation;

(C) the certificate of limited partnership of a limited partnership;

(D) the certificate of organization of a limited liability company;

[(E) the articles of incorporation of a general cooperative association;]

(F) the articles of organization of a limited cooperative association; and

(G) the certificate of trust of a statutory trust or similar record of a business trust.

(32) “Registered foreign entity” means a foreign entity that is registered to do business in this state pursuant to a record filed by the [Secretary of State].

(33) “Statement of conversion” means a statement under Section 1145.

(34) “Statement of domestication” means a statement under Section 1155.

(35) “Statement of interest exchange” means a statement under Section 1135.

(36) “Statement of merger” means a statement under Section 1125.

(37) “Surviving entity” means the entity that continues in existence after or is created by a merger.

(38) “Type of entity” means a generic form of entity:

(A) recognized at common law; or

(B) formed under an organic law, whether or not some entities formed under that organic law are subject to provisions of that law that create different categories of the form of entity.

Comment

This section defines the terms that are used in this article. Many of the definitions describe attributes that are significant in some forms of entity and not in others. For example, the concept of separate “distributional” and “governance” interests are inherent in unincorporated entities but have no counterpart in corporations. In addition, because some statutes use different terms to describe the same transaction, the definitions are intended to be broad enough to encompass those similar transactions, regardless of how described. *See, e.g.*, the comment to Paragraph 8.

“Acquired entity” [(1)]—This definition recognizes that an interest exchange may involve only the acquisition of a particular “class” or “series” of interests in an entity. Model Business Corporation Act section 6.01 does not expressly define “classes” or “series.” Because the interests of members in an unincorporated business organization often tend to be distinctive, it may be that each member’s interest will comprise a separate class or series. For an explanation of a new and different meaning of the word “series,” see Section 1131, comment. The term “acquired entity” does not encompass series under that new meaning.

“Acquiring entity” [(2)]—An “acquiring entity” is an entity that acquires the interests of the acquired entity in an interest exchange governed by Part 3 of this article.

“Conversion” [(3)]—The term “conversion” means a transaction authorized by Part 4 pursuant to which an entity of one type is converted into an entity of another type. As used in this act, the term “conversion” does not include a transaction in which an entity changes the jurisdiction in which it is organized but does not change to a different form of entity; that type of transaction is referred to in this act as a “domestication” and is governed by Article 5.

“Converted entity” [(4)]—This term is used in Part 4 to refer to the entity that results from a conversion.

“Converting entity” [(5)]—A converting entity is the entity that becomes the converted entity under Part 4.

“Distributional interest” [(6)]—This term is similar to the concept of a “transferable interest” found in this act and the organic laws of several other types of unincorporated entities, but has a broader meaning because the scope of this act includes entities in addition to those whose organic law uses the term “transferable interest.”

“Domestic” [(7)]—The term “domestic”, when used in this article with respect to an entity, refers to an entity whose internal affairs are governed by the organic laws of this state. In the case of a general partnership organized under UPA (1997) (Last Amended 2013), the term will mean a general partnership whose governing law under UPA (1997) § 104 is the law of the adopting state. Under that section, the governing law is determined by the location of the partnership’s principal office, except for limited liability partnerships whose governing law is the law of the state where the LLP’s statement of qualification is filed.

“Domesticated limited liability partnership” [(8)]—This term is used in Part 5 and means the entity limited liability partnership that is domesticated pursuant to Part 5. By the nature of the transaction, the domesticated entity will be of the same type as the domesticating entity – *i.e.*, a limited liability partnership.

“Domesticating limited liability partnership” [(9)]—This term is used in Part 5 and means the entity that is domesticated pursuant to Part 5.

Sections 1101(8) and (9) and 1151(a) exclude non-LLP general partnerships from domestications. However, a non-LLP general partnership that seeks to change its governing law may obtain that result through other means. *See* the comment to Section 1151(a).

“Domestication” [(10)]—The term “domestication” means a transaction of the kind authorized by Part 5 pursuant to which an entity may change its *jurisdiction* of formation *but not its type* so long as the laws of the foreign jurisdiction permit the domestication. The legal effect of the domestication of an LLP out of this state will be governed by the laws of both this state and the foreign jurisdiction. Some statutes include what is described in this act as “domestication” in their definition of a “conversion.” *See, e.g.*, COLO. REV. STAT. § 7-90-201. It is intended that the domestication provisions of this act will apply to a transaction that may be characterized under another act as a “conversion” if the transaction meets the definition of “domestication” under this act.

“Entity” [(11)]—This definition determines the overall scope of the act because only an “entity” may participate in the transactions authorized by Parts 2 (mergers), 3 (interest exchanges), 4 (conversions), and 5 (domestications). *See* Sections 1121 (authorization of mergers), 1131 (authorization of interest exchanges), 1141 (authorization of conversions), 1151 (authorization of domestications).

Subparagraph (A)(x) is a “catch-all” provision that includes within the definition of “entity” any type of organization recognized under the law of this state which is not listed specifically in the preceding paragraphs of this definition. Subparagraph (A)(x) is intended to include all forms of private organizations, regardless of whether organized for profit, and artificial legal persons other than those excluded by Subparagraph (B). This definition does not exclude regulated entities such as public utilities, banks, and insurance companies. Should a state desire to exclude certain types of regulated entities or any of the entities listed in Subparagraph (A)(i)–(x) from participating in transactions permitted by this act for policy reasons, that may be done by listing those types of entities in Section 1107(a), or by permitting those type of entities to engage in transactions under this act generally but prohibiting certain types of transactions by listing those transactions in Section 1107(b).

Unincorporated nonprofit associations are treated as a type of entity in Subparagraph (A)(viii) because Section 5 of the Uniform Unincorporated Nonprofit Association Act (2008) (Last Amended 2013) specifically states that an unincorporated nonprofit association is an entity. In many states, the status of a nonprofit association may not be clear. Nevertheless, in most states a nonprofit association has the power to acquire an interest in real property in its own name and therefore would qualify as an “entity” under Subparagraph (A)(x). *See* UUNAA § 6 (giving an unincorporated nonprofit association the power to acquire in its own name an interest in real property).

Subparagraph (B)(i) of this definition excludes a sole proprietorship from the concept of an “entity.”

Trusts with a predominately donative purpose, such as inter vivos and testamentary trusts and charitable trusts, are treated in many states as having a separate legal existence, but they have been excluded from the definition of “entity” (and thus are not within the scope of this article) under Subparagraph (B)(ii) because they should not be able to engage in transactions under this act as a matter of public policy. Trusts that carry on a business, however, such as business and statutory entity trusts, are “entities.” *See* Subparagraph (A)(ix).

Subparagraph (B)(iii) of this definition excludes from the concept of an “entity” any form of co-ownership of property or sharing of returns from property that is not listed in Subparagraph (A) and is not a partnership under this act. In that connection, Section 202(c) of this act provides in part:

In determining whether a partnership is formed, the following rules apply:

(1) Joint tenancy, tenancy in common, tenancy by the entireties, joint property, common property, or part ownership does not by itself establish a partnership, even if the co-owners share profits made by the use of the property.

(2) The sharing of gross returns does not by itself establish a partnership, even if the persons sharing them have a joint or common right or interest in property from which the returns are derived.

Limited liability partnerships and limited liability limited partnerships are “entities”

because they are general partnerships and limited partnerships respectively that have taken the necessary steps to obtain LLP or LLLP status. A limited liability partnership is not, therefore, a separate type of entity from the underlying general or limited partnership that has elected limited liability partnership status. Thus, for example, the election of a general partnership to become a limited liability partnership is not a conversion subject to Article 4.

Under Subparagraph (B)(iv), decedent's estates are excluded from the definition of an entity for the same policy reason as trusts with a predominately donative purpose and charitable trusts.

This same public policy rationale is the justification for the exclusion of governmental subdivisions, agencies, or instrumentalities in Subparagraph (B)(v).

“Filing entity” [Paragraph (12)]—Whether an entity is a filing entity is determined by reference to whether its legal existence requires the filing of a document with the state filing officer. To fit within this definition, the filing must be necessary but need not be sufficient to form the entity. *See, e.g.*, ULLCA (2006) (Last Amended 2013) § 201(d) (“A limited liability company is formed when the company’s certificate of organization becomes effective *and* at least one person becomes a member.”) (emphasis added).

While the statute refers to the “formation” of an entity, the term is intended to encompass corporations that are “incorporated,” as well as other filing entities whose statutes refer to them as being “organized.” Business trusts present a special problem. In some states a business trust could be a filing entity or a common law relationship, while in other states business trusts are only recognized at common law. A statutory trust entity formed under the Uniform Statutory Trust Entity Act (2009) (Last Amended 2013) § 201(a) is a filing entity, because a statutory trust entity is formed by the filing office filing a certificate of trust pertaining to the entity.

The term “filing entity” does not include a limited liability partnership because, while a filed document is precondition to LLP status, that document (a statement of qualification under Section 901) does not form the underlying entity. A limited liability limited partnership, on the other hand, is a filing entity because the underlying limited partnership is formed by filing a certificate of limited partnership. ULPA (2001) (Last Amended 2013) § 201(a).

“Foreign” [(13)]—The term “foreign entity” includes any non-domestic entity of any type. Where a foreign entity is a filing entity, the entity is governed by the laws of the state of filing. A nonfiling foreign entity is governed by the laws governing its internal affairs. It is a factual question whether a general partnership whose internal affairs are governed by UPA (1914) is a domestic or foreign partnership. A UPA (1914) partnership will likely be deemed to be a domestic entity where the greatest nexus of contacts are found. The domestic or foreign characterization of partnerships under this act that are not limited liability partnerships will be governed by Section 104(2) (“the law of the jurisdiction in which the partnership has its principal office”) or the partnership agreement. (Section 104(2) is a default rule.)

“Governance interest” [(14)]—A governance interest is typically only part of the interest that a person will hold in an unincorporated entity and is usually coupled with a

distributional interest (or economic rights). Memberships in some nonprofit corporations and unincorporated nonprofit associations consist solely of governance interests and memberships in other nonprofit entities may not include either governance interests or distributional interests. In some unincorporated business entities, including partnerships, there is a more limited right to transfer governance interests than there is to transfer distributional interests. An interest holder in such an unincorporated business entity who transfers only a distributional interest and retains the governance interest will also retain the status of an interest holder. Whether a transferee who acquires only a distributional interest will acquire the status of an interest holder is determined by the definition of “interest holder.”

Governors of an entity have the kinds of rights listed in the definition of “governance interest” by reason of their position with the entity. For a governor to have a “governance interest,” however, requires that the governor also have those rights for a reason other than the governor’s status as such. A manager who is not a member in a limited liability company, for example, will not have a governance interest, but a manager who is a member will have a governance interest arising from the ownership of a membership interest.

“Governor” [(15)]—This term has been chosen to provide a way of referring to a person who has the authority under an entity’s organic law to make management decisions regarding the entity that is different from any of the existing terms used in connection with particular types of entities. Depending on the type of entity or its organic rules, the governors of an entity may have the power to act on their own authority, or they may be organized as a board or similar group and have only the power to act collectively, and then only through a designated agent. In other words, a person having only the power to bind the organization pursuant to the instruction of the governors is not a governor. Under the organic rules, particularly those of unincorporated entities, most or all of the management decisions may be reserved to the members or partners. Thus, if a manager of a limited liability company were limited to having authority to execute management decisions made by the members and did not have any authority to make independent management decisions, the manager would not be a governor under this definition.

“Interest” [(16)]—In the usual case, the interest held by an interest holder will include both a governance interest and a distributional interest. Members in nonprofit corporations or unincorporated nonprofit associations generally do not have any distributional interest because they do not receive distributions, but they nonetheless may hold a governance interest in which case they would have the status of interest holders under this article.

“Interest exchange” [(17)]—The term “interest exchange” means a transaction authorized by Part 3 pursuant to which an entity may acquire interests in another entity. The consideration that may be provided to the interest holders whose interests are being acquired in an exchange may consist in whole or part of interests in a third party that is not one of the two parties to the exchange itself. *See* Section 1131(a).

“Interest holder” [(18)]—This article does not refer to “equity” interests or “equity” owners or holders because the term “equity” could be confusing in the case of a nonprofit entity whose members do not have an interest in the assets or results of operations of the entity but have only a right to vote on its internal affairs.

“Interest holder liability” [(19)]—This term is used to describe the vicarious liability of an interest holder, by virtue of being an interest holder, for liabilities of the entity. The term includes only personal liability of an interest holder for a debt of the entity imposed on the interest holder either by statute or by the organic rules to the extent authorized pursuant to the organic law. Liabilities that an interest holder incurs in any other fashion are not interest holder liabilities for purposes of this act. Thus, for example, if a state’s business corporation law makes shareholders personally liable for unpaid wages because of their status as shareholders, that liability would be an “interest holder liability.” If, on the other hand, a shareholder were to guarantee payment of an obligation of a corporation, that liability would not be an “interest holder liability” because it is a direct liability and not based on the status of being a shareholder. Similarly, the liability to return an improper distribution is not an interest holder liability because it is a direct liability of the interest holder based on receipt of the distribution.

“Merger” [(20)]—The term means a transaction in which two or more entities are combined into a single entity pursuant to a filing by the filing office. The term “merger” in this act includes the transaction known as a consolidation in which a new entity results from the combination of two or more pre-existing entities.

“Merging entity” [(21)]—The term “merging entity” refers to each entity that is in existence immediately before a merger and is a party to the merger. It will include the surviving entity if the surviving entity exists before the merger becomes effective. It does not include an entity that provides consideration to be received by interest holders if that entity is not a party to the merger.

“Organic law” [(22)]—Organic law means statutes that govern the internal affairs of an entity. For example, this act is the organic law of a limited liability partnership whose statement of qualification is filed under this act.

Entity laws in a few states purport to require that some of their internal governance rules applicable to a domestic entity also apply to a foreign entity with significant ties to the state. *See, e.g.,* CAL. CORP. CODE § 2115 (Foreign Corporations); N.Y. NOT-FOR-PROFIT-CORP. §§ 1318–21 (Liabilities of Directors and Officers of Foreign Corporations); 15 PA.CONST. STAT. § 6145 (Applicability of Certain Safeguards to Foreign Corporations). Such a “sticky fingers” law is not included within the definition of “organic law” for purposes of this act because those laws are not part of the law of the entity’s jurisdiction of formation.

“Organic rules” [(23)]—The term “organic rules” means an entity’s public organic record and the private organic rules. The organic rules, together with this act, the organic law, and the common law, provide the rules governing the internal affairs of the entity. For example, this act and the partnership agreement comprise the organic rules of a limited liability partnership formed under this act.

“Plan” [(24)]—The term “plan” is a short-hand way of referring to the plan of merger, interest exchange, conversion, or domestication, as the case may be, depending on which form of transaction is taking place. *See* Sections 1122 (plan of merger), 1132 (plan of interest exchange), 1142 (plan of conversion), 1152 (plan of domestication).

“Private organic rules” [(29)]—The term private “organic rules” is intended to include all governing rules of an entity that are binding on all of its interest holders, whether or not in record form, except for the provisions of the entity’s public organic record, if any. The term is intended to include agreements in “record” form such as corporate bylaws, as well as oral partnership agreements and oral operating agreements among LLC members.

“Protected agreement” [(30)]—The term “protected agreement” refers to evidences of indebtedness and agreements binding on the entity or any of its governors or interest holders that are unpaid or executory in whole or in part on the effective date of the act. Thus a revolving line of credit from a bank to a corporation would constitute a protected agreement even if advances were not made until after the effective date of the act. Likewise, a partnership agreement in effect under this act or a predecessor to this act is a “protected agreement.”

If a protected agreement has provisions that apply if an entity merges, those provisions will apply if the entity enters into an interest exchange, conversion, or domestication even though the agreement does not mention those other types of transactions. *See* Sections 1131(c) (interest exchange), 1141(c) (conversion), 1151(c) (domestication).

“Public organic record” [(31)]—A “public organic record” is a record that is filed publicly to form, organize, incorporate, or otherwise create an entity. The term does not include a statement of authority under this act or any of the other statements that may be filed under this act since those statements do not create a new entity. Thus, a statement of qualification filed under Section 1003 is not a “public organic record.” The limited liability partnership that results from the filing is the same entity as the partnership that delivered the statement to the filing office.

Similarly, the term does not include a statement of authority filed under Section 7 of the Revised Uniform Unincorporated Nonprofit Association Act (2008) (Last Amended 2013), a statement appointing a registered agent filed under Section 31 of that act, or any of the various statements filed under the ULLCA (2006) (Last Amended 2013).

In those states where a deed of trust or other instrument is publicly filed to create a business trust, that filing will constitute a public organic record. But in those states where a business trust is not created by a public filing, the deed of trust or similar record will be part of the private organic rules of the business trust.

Where a public organic document has been amended or restated, the term means the public organic document as last amended or restated.

“Registered foreign entity” [(32)]—This term refers to a foreign entity that is registered to transact business in this state pursuant to a public filing.

“Surviving entity” [(37)]—The term “surviving entity” refers to either a merging entity that survives the merger or the new entity created by the merger.

“Type of entity” [(38)]—The term “type of entity” has been developed in an attempt to distinguish different legal forms of entities. It is sometimes difficult to decide whether one is

dealing with a different form of entity or a variation of the same form. For example, a limited partnership, although it has long been characterized or even defined as a partnership, is a different type of entity from a general partnership, while a limited liability partnership is not a different type of entity from a general partnership. In some states cooperatives are categories of business corporations or nonprofit corporations, while in other states cooperatives are a separate type of entity.

SECTION 1102. RELATIONSHIP OF [ARTICLE] TO OTHER LAWS.

(a) This [article] does not authorize an act prohibited by, and does not affect the application or requirements of, law other than this [article].

(b) A transaction effected under this [act] may not create or impair a right, duty, or obligation of a person under the statutory law of this state relating to a change in control, takeover, business combination, control-share acquisition, or similar transaction involving a domestic merging, acquired, converting, or domesticating business corporation unless:

(1) if the corporation does not survive the transaction, the transaction satisfies any requirements of the law; or

(2) if the corporation survives the transaction, the approval of the plan is by a vote of the shareholders or directors which would be sufficient to create or impair the right, duty, or obligation directly under the law.

Comment

This section preserves existing regulatory law in an adopting state in general terms. Adopting states should consider more carefully integrating this act with their various regulatory laws. For example, in some states certain professions are limited in their use of limited liability entities. *See* Section 1103.

Laws other than this act that will apply to transactions under the act include, for example, uniform fraudulent transfer and fraudulent conveyance acts, state insolvency statutes, federal bankruptcy law, and Articles 8 and 9 of the Uniform Commercial Code.

Subsection (b)—Many states have enacted “antitakeover” statutes intended to make it more difficult to acquire control of a publicly traded corporation. Those statutes often provide that their application to a particular corporation cannot be changed unless the corporation obtains certain specified approvals, such as a vote of disinterested directors or a supermajority vote by

the shareholders. The purpose of the special requirements in this subsection on varying the application of an antitakeover statute is to protect against a hostile acquirer or group of shareholders seeking to use the act to avoid the application of the antitakeover statute.

This subsection protects the application of antitakeover statutes from being affected by a transaction under this act by requiring that the transaction be approved in a manner that would be sufficient to approve changing the application of the antitakeover statute. If a transaction is approved in that manner, there is no policy reason to prohibit the application of the antitakeover statute from being varied by a transaction under this act. If the application of an antitakeover statute cannot be varied by action of an entity subject to it, then a transaction under this act will be permissible only if the antitakeover provision continues to apply after the transaction or the transaction itself is permissible under the antitakeover statute.

SECTION 1103. REQUIRED NOTICE OR APPROVAL.

(a) A domestic or foreign entity that is required to give notice to, or obtain the approval of, a governmental agency or officer of this state to be a party to a merger must give the notice or obtain the approval to be a party to an interest exchange, conversion, or domestication.

(b) Property held for a charitable purpose under the law of this state by a domestic or foreign entity immediately before a transaction under this [article] becomes effective may not, as a result of the transaction, be diverted from the objects for which it was donated, granted, devised, or otherwise transferred unless, to the extent required by or pursuant to the law of this state concerning cy pres or other law dealing with nondiversion of charitable assets, the entity obtains an appropriate order of [the appropriate court] [the Attorney General] specifying the disposition of the property.

(c) A bequest, devise, gift, grant, or promise contained in a will or other instrument of donation, subscription, or conveyance which is made to a merging entity that is not the surviving entity and which takes effect or remains payable after the merger inures to the surviving entity.

(d) A trust obligation that would govern property if transferred to a nonsurviving entity applies to property that is transferred to the surviving entity under this section.

Legislative Note: *As an alternative to enacting Subsection (a), a state may identify each of its*

regulatory laws that requires prior approval for a merger of a regulated entity, decide whether regulatory approval should be required for an interest exchange, conversion, or domestication, and make amendments as appropriate to those laws.

As with Subsection (a), an adopting state may choose to amend its various laws with respect to the nondiversion of charitable property to cover the various transactions authorized by this act as an alternative to enacting Subsection (b).

Comment

Subsection (a)—Because at least some of the provisions of this act will be new in most states, it is likely that existing state laws that require regulatory approval of transactions by businesses such as banks, insurance companies, or public utilities may not be worded in a fashion that will include at least some of the transactions authorized by this act. The purpose of this subsection is to ensure that transactions under this act will be subject to the same regulatory approval as mergers. This subsection is based on whether a merger by a regulated entity requires prior approval because the transactions authorized by this act may be effectuated indirectly in many cases under existing law by establishing a wholly owned subsidiary of the desired type and then merging into it.

The consequence of violating this subsection should be the same as in the case of a merger consummated without the required approval.

Subsection (b)—This act applies generally to nonprofit corporations and unincorporated nonprofit associations. As in the case of laws regulating particular industries, a state's laws governing the nondiversion of charitable property to other uses may not cover some of the transactions authorized by this act. To prevent the procedures in this act from being used to avoid restrictions on the use of such charitable property, this subsection requires approval of the effect of transactions under this act by the appropriate arm of government having supervision of nonprofit entities.

An approval or order obtained under this section may impose conditions or specify the disposition of assets or liabilities in a manner different than would otherwise be the case. In such an instance, the approval or order will control over the provisions of this act specifying the effects of a transaction. *See* Sections 1126 (effect of merger), 1136 (effect of interest exchange), 1146 (effect of conversion), 1156 (effect of domestication).

Subsection (c)—This subsection clarifies the legal effect of a merger on bequests, etc. that were originally made to an entity that does not survive the merger. This issue does not arise in an interest exchange, conversion, or domestication transaction because the entity to which the bequest, etc. was made survives in some form after the transaction.

SECTION 1104. NONEXCLUSIVITY. The fact that a transaction under this [article] produces a certain result does not preclude the same result from being accomplished in any other

manner permitted by law other than this [article].

Comment

This section allows a transaction that has the same end result as one of the transactions governed by this act, but that is accomplished in a manner not within the scope of this act, to be exempt from this act. For example, a sale of assets and transfer of liabilities by two entities to a third entity followed by the liquidation of the two transferring entities can be accomplished pursuant to statutory provisions pertaining to sale of assets rather than under Part 2 of this article, even though the end result of the transaction is essentially the same as if the two entities had merged into a third entity.

SECTION 1105. REFERENCE TO EXTERNAL FACTS. A plan may refer to facts ascertainable outside the plan if the manner in which the facts will operate upon the plan is specified in the plan. The facts may include the occurrence of an event or a determination or action by a person, whether or not the event, determination, or action is within the control of a party to the transaction.

Comment

This section is based on, but more concise than, section 1.20(k) of the Model Business Corporation Act.

SECTION 1106. APPRAISAL RIGHTS. An interest holder of a domestic merging, acquired, converting, or domesticating partnership is entitled to contractual appraisal rights in connection with a transaction under this [article] to the extent provided in:

- (1) the partnership's organic rules; or
- (2) the plan.

Comment

In corporate law, appraisal rights developed when corporate statutes were amended to permit mergers with less than unanimous consent of the shareholders. This article provides no appraisal rights, because as a default rule transactions under this article require the consent or affirmative vote of all the partners. Where the partnership agreement changes this default rule, parties may wish to consider contractual appraisal rights.

This subsection validates the grant of such contractual appraisal rights. *Cf.* 6 DEL. CODE

ANN. §§ 15-120 (general partnerships), 17-212 (limited partnerships), 18-210 (limited liability companies) (validating “contractual appraisal rights”); MODEL BUS. CORP. ACT § 13.02(5) (permitting the articles of incorporation, bylaws, or a resolution of the board of directors to confer appraisal rights in contexts in which they would otherwise not be available). Legislative authorization in this subsection of the grant of contractual appraisal rights removes any question as to whether a court would have jurisdiction to hear a case in which the parties were attempting to create jurisdiction in the court by private agreement.

In this section, the term “appraisal rights” refers to any arrangement, either in the partnership agreement or the plan, providing for the buy-out of partners that object to a transaction under this article.

[SECTION 1107. EXCLUDED ENTITIES AND TRANSACTIONS.]

(a) The following entities may not participate in a transaction under this [article]:

(1)

(2).

(b) This [article] may not be used to effect a transaction that:

(1)

(2).]

Legislative Note: Subsection (a) may be used by states that have special statutes restricted to the organization of certain types of entities. A common example is banking statutes that prohibit banks from engaging in transactions other than pursuant to those statutes.

Nonprofit entities may participate in transactions under this act with for-profit entities, subject to compliance with Section 1103. If a state desires, however, to exclude entities with a charitable purpose or to exclude other types of entities from the scope of this article, that may be done by referring to those entities in Subsection (a).

Subsection (b) may be used to exclude certain types of transactions governed by more specific statutes. A common example is the conversion of an insurance company from mutual to stock form. There may be other types of transactions that vary greatly among the states.

[PART] 2

MERGER

SECTION 1121. MERGER AUTHORIZED.

(a) By complying with this [part]:

(1) one or more domestic partnerships may merge with one or more domestic or foreign entities into a domestic or foreign surviving entity; and

(2) two or more foreign entities may merge into a domestic partnership.

(b) By complying with the provisions of this [part] applicable to foreign entities, a foreign entity may be a party to a merger under this [part] or may be the surviving entity in such a merger if the merger is authorized by the law of the foreign entity's jurisdiction of formation.

Comment

The merger transaction authorized by this act involves the combination of one or more domestic general partnerships with or into one or more other domestic or foreign entities. It also contemplates the consolidation of two or more foreign entities into a single domestic general partnership. Upon the effective date of the merger, all the assets and liabilities of the constituent entities vest in the surviving entity as a matter of law. As such, mergers require the existence of at least two separate entities before the transaction and only one entity may survive the merger. If independent existence of the constituent entities is desired following the conclusion of the transaction, a restructuring transaction other than a merger must be used to accomplish the transfer of assets and liabilities.

This act authorizes a merger for state entity law purposes. Federal law and other state law will independently determine how a merger transaction will be taxed.

Subsection (a)(1)—This paragraph states the general rule that subject to Subsection (b) one or more domestic general partnerships may merge with or into a domestic or foreign surviving entity.

Subsection (a)(2)—This paragraph provides that two or more foreign entities may merge into a domestic surviving general partnership so long as the requirements of Subsection (b) are met.

Subsection (b)—This subsection provides that a foreign entity may be a party to a merger or may be the surviving entity in a merger only if the merger is authorized by the laws of the foreign entity's jurisdiction of formation.

SECTION 1122. PLAN OF MERGER.

(a) A domestic partnership may become a party to a merger under this [part] by approving a plan of merger. The plan must be in a record and contain:

(1) as to each merging entity, its name, jurisdiction of formation, and type of

entity;

(2) if the surviving entity is to be created in the merger, a statement to that effect and the entity's name, jurisdiction of formation, and type of entity;

(3) the manner of converting the interests in each party to the merger into interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing;

(4) if the surviving entity exists before the merger, any proposed amendments to:

(A) its public organic record, if any; or

(B) its private organic rules that are, or are proposed to be, in a record;

(5) if the surviving entity is to be created in the merger:

(A) its proposed public organic record, if any; and

(B) the full text of its private organic rules that are proposed to be in a record;

(6) the other terms and conditions of the merger; and

(7) any other provision required by the law of a merging entity's jurisdiction of formation or the organic rules of a merging entity.

(b) In addition to the requirements of subsection (a), a plan of merger may contain any other provision not prohibited by law.

Comment

Subsection (a)—This subsection states the requirements for the plan of merger. They are similar to plan of merger provisions in corporation statutes. *See* MODEL BUS. CORP. ACT § 11.02(c). The requirements stated in this subsection are mandatory. *See* Section 105(c)(15).

Subsection (a)(1)—This paragraph requires that the plan of merger identify the parties to the merger. The name of a merging entity as it appears in the plan of merger will be its name in its jurisdiction of formation.

Subsection (a)(3)—The language of this paragraph is similar to Model Business Corporation Act § 11.02(c)(3). What may be done under this paragraph with respect to providing for continuing interests in the surviving entity for some holders of interests of a class or series of a party to the merger while paying some other form of consideration to other holders of the same class or series of interests in that entity will vary depending on the type of entity involved and the extent to which its organic rules provide for non-uniform treatment of interest holders in a manner that is permissible under its organic law. Similarly the ability to use a merger to reorganize the capital structure of the surviving entity will vary depending on the type of entity involved and whether the entity has appropriately adopted relevant provisions in its organic rules.

If the organic law and organic rules of an unincorporated entity permit a non-uniform “equity shuffle” to be accomplished in a merger involving the unincorporated entity, the minority owners of the unincorporated entity will not necessarily be entitled to the statutory appraisal rights currently afforded to minority stockholders in merging corporate entities. Any perceived unfairness in the shuffle would be addressed either: (i) under principles of fiduciary duties and the contractual obligations of good faith and fair dealing, assuming, of course, that such duties and obligations have not been contractually modified or eliminated to the extent permitted by the applicable organic law, or (ii) by the exercise of whatever rights the minority owners may have to veto the transaction or to withdraw or to dissociate and be paid the value of their interests.

The Model Business Corporation Act generally requires that shares of the same class or series be treated in the same manner in a merger unless the corporation has adopted an applicable provision of its articles of incorporation pursuant to section 6.01(e) of that act providing for variations in the treatment of holders of the same class or series of shares. Thus, a determination of what may be done by way of an equity shuffle in the case of a corporation will require reference to its organic law and organic rules.

The consideration paid to the interest holders of the merging parties may be supplied in whole or part by a person who is not a party to the merger.

Subsection (b)—This subsection provides the statutory authority for a merging party to include a provision in a plan of merger that is not specifically listed in Subsection (a). One such possibility is contractual appraisal rights as provided in Section 1106(2).

SECTION 1123. APPROVAL OF MERGER.

(a) A plan of merger is not effective unless it has been approved:

(1) by a domestic merging partnership, by all the partners of the partnership entitled to vote on or consent to any matter; and

(2) in a record, by each partner of a domestic merging partnership which will have interest holder liability for debts, obligations, and other liabilities that are incurred after the

merger becomes effective, unless:

(A) the partnership agreement of the partnership provides in a record for the approval of a merger in which some or all of its partners become subject to interest holder liability by the affirmative vote or consent of fewer than all the partners; and

(B) the partner consented in a record to or voted for that provision of the partnership agreement or became a partner after the adoption of that provision.

(b) A merger involving a domestic merging entity that is not a partnership is not effective unless the merger is approved by that entity in accordance with its organic law.

(c) A merger involving a foreign merging entity is not effective unless the merger is approved by the foreign entity in accordance with the law of the foreign entity's jurisdiction of formation.

Comment

Subsection (a)—In the uniform acts pertaining to unincorporated business organizations, unanimity is the default rule for approving a merger. The partnership agreement certainly can change this rule, but care should be taken in doing so. For example, a merger can revise the partnership agreement. Section 1122(a)(4). Thus, if a merger requires less-than-unanimous consent, the partnership agreement is subject to amendment by the same quantum of consent. “Exit rights” also require consideration. This act does not provide appraisal rights, because those rights are inapposite when unanimous consent is required. *See* the comment to Section 1106.

Subsection (a)(2)—This provision is not a default rule, Section 105(c)(14), and deals with the situation in which a partner of a general partnership that is a party to a merger will have “interest holder liability” for the liabilities of the surviving entity which are incurred after the merger becomes effective. This provision applies regardless of whether the partnership is an LLP. The issue is not whether the partners have “interest holder liability” in their current partnership but rather whether they will have that liability in the surviving entity. Thus, for example, if general partnership Alpha merges into general partnership Beta, which is not an LLP, the special approval requirement in Subsection (a)(2) will be applicable to each Alpha partner who will become a Beta partner—regardless of whether Alpha is a limited liability partnership.

The consent of a partner required by Subsection (a)(2)(B) may be given either by: (i) signing or agreeing generally to the terms of a partnership agreement that includes the required provision permitting less than unanimous approval of a merger in which partners become subject to “interest holder liability,” or (ii) voting for or consenting to an amendment to the partnership

agreement to add such a provision.

Subsection (b)—Where a domestic entity other than a general partnership is a party to a merger under this act, this subsection defers to that entity’s organic law for the requirements for approval of the merger by that entity.

Subsection (c)—Where a foreign entity is a party to a merger under this act, this subsection defers to the laws of the foreign jurisdiction for the requirements for approval of the merger by the foreign entity. Those laws will include the organic law of the foreign entity and other applicable laws. The laws of the foreign jurisdiction will also control the application of any special approval requirements found in the organic rules of the foreign entity.

SECTION 1124. AMENDMENT OR ABANDONMENT OF PLAN OF MERGER.

(a) A plan of merger may be amended only with the consent of each party to the plan, except as otherwise provided in the plan.

(b) A domestic merging partnership may approve an amendment of a plan of merger:

(1) in the same manner as the plan was approved, if the plan does not provide for the manner in which it may be amended; or

(2) by its partners in the manner provided in the plan, but a partner that was entitled to vote on or consent to approval of the merger is entitled to vote on or consent to any amendment of the plan that will change:

(A) the amount or kind of interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing, to be received by the interest holders of any party to the plan;

(B) the public organic record, if any, or private organic rules of the surviving entity that will be in effect immediately after the merger be effective, except for changes that do not require approval of the interest holders of the surviving entity under its organic law or organic rules; or

(C) any other terms or conditions of the plan, if the change would

adversely affect the partner in any material respect.

(c) After a plan of merger has been approved and before a statement of merger becomes effective, the plan may be abandoned as provided in the plan. Unless prohibited by the plan, a domestic merging partnership may abandon the plan in the same manner as the plan was approved.

(d) If a plan of merger is abandoned after a statement of merger has been delivered to the [Secretary of State] for filing and before the statement becomes effective, a statement of abandonment, signed by a party to the plan, must be delivered to the [Secretary of State] for filing before the statement of merger becomes effective. The statement of abandonment takes effect on filing, and the merger is abandoned and does not become effective. The statement of abandonment must contain:

- (1) the name of each party to the plan of merger;
- (2) the date on which the statement of merger was filed by the [Secretary of State]; and
- (3) a statement that the merger has been abandoned in accordance with this section.

Comment

This section sets out the requirements for amending or abandoning the plan of merger. They are similar to provisions for amending or abandoning mergers found in existing corporation merger statutes. *See* MODEL BUS.CORP. ACT §§ 11.02(e), 11.08.

SECTION 1125. STATEMENT OF MERGER; EFFECTIVE DATE OF MERGER.

(a) A statement of merger must be signed by each merging entity and delivered to the [Secretary of State] for filing.

(b) A statement of merger must contain:

(1) the name, jurisdiction of formation, and type of entity of each merging entity that is not the surviving entity;

(2) the name, jurisdiction of formation, and type of entity of the surviving entity;

(3) a statement that the merger was approved by each domestic merging entity, if any, in accordance with this [part] and by each foreign merging entity, if any, in accordance with the law of its jurisdiction of formation;

(4) if the surviving entity exists before the merger and is a domestic filing entity, any amendment to its public organic record approved as part of the plan of merger;

(5) if the surviving entity is created by the merger and is a domestic filing entity, its public organic record, as an attachment; and

(6) if the surviving entity is created by the merger and is a domestic limited liability partnership, its statement of qualification, as an attachment.

(c) In addition to the requirements of subsection (b), a statement of merger may contain any other provision not prohibited by law.

(d) If the surviving entity is a domestic entity, its public organic record, if any, must satisfy the requirements of the law of this state, except that the public organic record does not need to be signed.

(e) A plan of merger that is signed by all the merging entities and meets all the requirements of subsection (b) may be delivered to the [Secretary of State] for filing instead of a statement of merger and on filing has the same effect. If a plan of merger is filed as provided in this subsection, references in this [article] to a statement of merger refer to the plan of merger filed under this subsection.

(f) If the surviving entity is a domestic partnership, the merger becomes effective when

the statement of merger is effective. In all other cases, the merger becomes effective on the later of:

- (1) the date and time provided by the organic law of the surviving entity; and
- (2) when the statement is effective.

Comment

The filing of a statement of merger makes the transaction a matter of public record.

Subsection (a)—This subsection pertains to all merging entities involved in a merger, not merely any merging domestic general partnership. Other filings may be required by the organic law of other entities participating in the merger.

Subsection (b)(1) and (2)—The names of foreign entities set forth in the statement of merger will generally be their names in their jurisdiction of formation, except that if a foreign entity has been required to adopt a different name in order to register to do business in this state, the foreign qualification statute will likely require that, when the entity does business in this state, the entity must use the name adopted for the purposes of registering to do business. Engaging in a merger under this act will be part of the business done by the entity in this state and the name of the entity set forth in the statement of merger will thus need to be the name under which the entity has registered to do business. Use of the name under which the entity has registered to do business will allow the records in the filing office to associate the registration of the entity to do business with the statement of merger.

Subsection (b)(3)—For more information on the statement of merger, see Subsection (f), comment.

Subsection (b)(4)—The statement in this paragraph that the plan of merger was approved by each entity in accordance with this article necessarily presupposes that the plan was approved in accordance with any valid, special requirements in the organic rules of each merging entity.

Subsection (b)(5) and (6)—The public organic record of a domestic surviving entity created by the merger that is attached to the statement of merger becomes the original, officially filed text of the public organic record of the surviving entity when the statement of merger takes effect. It is not necessary, or appropriate, to make any other filing to create the surviving entity.

Similarly, a statement of qualification for a domestic limited liability partnership created by the merger that is attached to the statement of merger does not need to be filed separately.

Subsection (d)—Organic laws typically require that an initial filing that creates an entity be signed by the person serving as the incorporator or other organizer. This subsection, however, provides that the public organic record of the surviving entity does not need to be signed since the record is attached to a signed record.

This subsection also permits the public organic record of the surviving entity to omit any provision that is not required to be included in a restatement of the public organic record. Pursuant to this provision, for example, the public organic record of a business corporation created as the surviving entity in the merger would not need to state the name and address of each incorporator even though that information would be required by section 2.02(a)(4) of the Model Business Corporation Act if the corporation were being incorporated outside the context of the merger.

Subsection (e)—A plan of merger that contains all the information required in the statement of merger may be filed instead of the statement of merger. The plan must be in a record and signed by each merging party.

Subsection (f)—A merger in which the surviving entity is a domestic general partnership takes effect when the statement of merger takes effect. A merger in which the surviving entity is a foreign entity will usually also take effect when the statement of merger takes effect because the practice is to coordinate the filings that need to be made when a merger involves both a domestic entity and also a foreign entity so that the filings in each jurisdiction take effect at the same time.

However, when the surviving general partnership is a foreign general partnership, it is possible that the filing in the foreign jurisdiction will take effect at a different time. For that reason, this subsection provides that the merger will take effect at the later of: (i) when the statement of merger takes effect; and (ii) when the merger takes effect under the law of the foreign jurisdiction. This rule avoids the possibility that the merger will take effect in this state before it takes effect in the foreign jurisdiction, which would produce the undesirable result that the merging domestic general partnership would cease to appear as an active entity on the records of this state before the records of the foreign jurisdiction reflect a completed merger.

It is necessary for the filing office to record only the effective date of the statement of merger, and the filing office does not need to be concerned with the effective date of the merger itself. Persons wishing to determine the effective date of a merger involving both a domestic and a foreign entity will be able to do so by consulting the records of the filing offices in each jurisdiction.

SECTION 1126. EFFECT OF MERGER.

(a) When a merger becomes effective:

- (1) the surviving entity continues or comes into existence;
- (2) each merging entity that is not the surviving entity ceases to exist;
- (3) all property of each merging entity vests in the surviving entity without transfer, reversion, or impairment;

(4) all debts, obligations, and other liabilities of each merging entity are debts, obligations, and other liabilities of the surviving entity;

(5) except as otherwise provided by law or the plan of merger, all the rights, privileges, immunities, powers, and purposes of each merging entity vest in the surviving entity;

(6) if the surviving entity exists before the merger:

(A) all its property continues to be vested in it without transfer, reversion, or impairment;

(B) it remains subject to all its debts, obligations, and other liabilities; and

(C) all its rights, privileges, immunities, powers, and purposes continue to be vested in it;

(7) the name of the surviving entity may be substituted for the name of any merging entity that is a party to any pending action or proceeding;

(8) if the surviving entity exists before the merger:

(A) its public organic record, if any, is amended as provided in the statement of merger; and

(B) its private organic rules that are to be in a record, if any, are amended to the extent provided in the plan of merger;

(9) if the surviving entity is created by the merger, its private organic rules become effective and:

(A) if it is a filing entity, its public organic record becomes effective; and

(B) if it is a limited liability partnership, its statement of qualification becomes effective; and

(10) the interests in each merging entity which are to be converted in the merger

are converted, and the interest holders of those interests are entitled only to the rights provided to them under the plan of merger and to any appraisal rights they have under Section 1106 and the merging entity's organic law.

(b) Except as otherwise provided in the organic law or organic rules of a merging entity, the merger does not give rise to any rights that an interest holder, governor, or third party would have upon a dissolution, liquidation, or winding up of the merging entity.

(c) When a merger becomes effective, a person that did not have interest holder liability with respect to any of the merging entities and becomes subject to interest holder liability with respect to a domestic entity as a result of the merger has interest holder liability only to the extent provided by the organic law of that entity and only for those debts, obligations, and other liabilities that are incurred after the merger becomes effective.

(d) When a merger becomes effective, the interest holder liability of a person that ceases to hold an interest in a domestic merging partnership with respect to which the person had interest holder liability is subject to the following rules:

(1) The merger does not discharge any interest holder liability under this [act] to the extent the interest holder liability was incurred before the merger became effective.

(2) The person does not have interest holder liability under this [act] for any debt, obligation, or other liability that is incurred after the merger becomes effective.

(3) This [act] continues to apply to the release, collection, or discharge of any interest holder liability preserved under paragraph (1) as if the merger had not occurred and the surviving entity were the domestic merging entity.

(4) The person has whatever rights of contribution from any other person as are provided by this [act], law other than this [act], or the partnership agreement of the domestic

merging partnership with respect to any interest holder liability preserved under paragraph (1) as if the merger had not occurred.

(e) When a merger has become effective, a foreign entity that is the surviving entity may be served with process in this state for the collection and enforcement of any debts, obligations, or other liabilities of a domestic merging partnership as provided in Section 119.

(f) When a merger has become effective, the registration to do business in this state of any foreign merging entity that is not the surviving entity is canceled.

Comment

With the exception of Subsections (c) and (d), this section is similar to statutory provisions on the effect of a merger of a corporation with a corporation. *See* MODEL BUS. CORP. ACT § 11.07.

Subsection (a)—This subsection states the general understanding that in a merger the assets and liabilities of the merging entities automatically vest in the surviving entity. The surviving entity becomes the owner of all real and personal property of the merged entities and is subject to all debts, obligations, and liabilities of the merging entities. A merger does not constitute a transfer, assignment, or conveyance of any property held by the merging entities before the merger. A merger also does not give rise to a claim that a contract with a merging entity is no longer in effect on the ground of nonassignability, unless the contract specifically provides that it does not survive a merger. The contract rights that are vested in the surviving entity include the right to enforce subscription agreements for interests and obligations to make capital contributions entered into or incurred before the merger. *See* Section 1103(c) (dealing with the surviving entity's rights in trust obligations of a nonsurviving party in a merger and transactions such as bequests made to a nonsurviving party to a merger that take effect after the merger).

After a merger has become effective, the law of the surviving entity's jurisdiction of formation governs the surviving entity. *See* Sections 1103(a) and (b) (modifying the provisions of this section with respect to the effects of a merger to the extent a regulatory law provides otherwise or any of the parties holds property committed to charitable purposes).

Subsection (a)(2)—A merger cannot have the effect of making an interest holder of a domestic merging general partnership subject to interest holder liability for the debts, obligations, or other liabilities of any other person or entity unless the interest holder has signed a separate written consent to become subject to such liability or previously agreed to the effectuation of a transaction having that effect without the interest holder's consent. The partnership agreement cannot change this provision. Section 105(c)(14).

Subsection (a)(7)—All pending proceedings involving either the survivor or a party whose separate existence ceased as a result of the merger are continued. Under this paragraph, the name of the survivor may be, but need not be, substituted in any pending proceeding for the name of a party to the merger whose separate existence ceased as a result of the merger. The substitution may be made whether the survivor is a complainant or a respondent, and may be made at the instance of either the survivor or an opposing party. That substitution has no substantive effect because, whether or not the survivor’s name is substituted, the survivor succeeds to the claims, and is subject to the liabilities, of any party to the merger whose separate existence ceased as a result of the merger.

Subsection (a)(8)(B)—The private organic rules of an unincorporated entity typically may be either oral or written. The plan of merger is not required to set forth amendments to oral provisions of the private organic rules of the surviving entity, and thus this provision is limited in scope to amendments to the private organic rules that are to be in a record, if any.

Subsection (a)(10)—For more information on appraisal rights, see Section 1106, comment.

Subsections (c) and (d)—These subsections set forth rules for two circumstances that typically do not exist in a merger where all the entities involved are corporations. Subsection (c) deals with the situation where an interest holder that does not have vicarious liability for the obligations of a merging entity before the merger has interest holder liability after the merger. An example would be a corporate shareholder who agrees to be the general partner in a limited partnership that is the surviving entity in a merger between a corporation and a limited partnership that is not a limited liability limited partnership. Subsection (d) deals with the situation where an interest holder has vicarious liability for the obligations of one of the merging parties before the merger but ceases to have any interest holder liability for the obligations of the surviving entity after the merger becomes effective. An example would be a general partner in a general partnership that merges into a corporation.

The effects of Subsections (c) and (d) will depend on when a liability is incurred, which is determined by other law. For a discussion of the issue, see the comment to Section 404(c) (The Temporal Nexus – When Claim Incurred).

These subsections apply not only to merging domestic general partnerships but also to any other domestic entity involved in the merger.

Subsection (c)—This subsection sets forth the general rule that an interest holder that was not liable for the liabilities of a merging entity before the merger but will have personal liability for the obligations of the surviving entity after the merger will be personally liable only for the liabilities of a domestic surviving entity that are incurred after the effective date of a merger.

Subsection (d)—This subsection uses “arose” as its term of art, while Section 306(b) and (c) use “incur.” The difference is historical, and no difference in meaning is intended. For a discussion of case law interpreting “incurred,” see Section 306(b), comment.

This subsection provides four rules with respect to an interest holder who ceases to have interest holder liability after the effective date of the merger:

- (1) the interest holder remains personally liable for any obligations that were incurred before the effective date of the merger;
- (2) the interest holder does not have any personal liability for obligations of the surviving entity;
- (3) the pre-existing personal liability of the interest holder is enforced against the interest holder on the same basis as if the merger had not taken place; and
- (4) the interest holder has the same rights of contribution from other interest holders of the merging entity as the interest holder would have had if the merger had not occurred.

See the comment to Section 1146(d).

Subsection (e)—When a merger has become effective, this subsection provides that a foreign entity that is the surviving entity may be served with process in this state. The proceedings covered by this subsection include a proceeding to enforce the rights of any interest holders of each domestic merging entity who are entitled to and exercise appraisal rights. One of the liabilities that a foreign surviving entity succeeds to is the obligation of a merging entity to pay the amount, if any, to which its interest holders who assert appraisal rights are entitled.

[PART] 3

INTEREST EXCHANGE

SECTION 1131. INTEREST EXCHANGE AUTHORIZED.

(a) By complying with this [part]:

(1) a domestic partnership may acquire all of one or more classes or series of interests of another domestic entity or a foreign entity in exchange for interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing; or

(2) all of one or more classes or series of interests of a domestic partnership may be acquired by another domestic entity or a foreign entity in exchange for interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of

the foregoing.

(b) By complying with the provisions of this [part] applicable to foreign entities, a foreign entity may be the acquiring or acquired entity in an interest exchange under this [part] if the interest exchange is authorized by the law of the foreign entity's jurisdiction of formation.

(c) If a protected agreement contains a provision that applies to a merger of a domestic partnership but does not refer to an interest exchange, the provision applies to an interest exchange in which the domestic partnership is the acquired entity as if the interest exchange were a merger until the provision is amended after [the effective date of this [act]].

Comment

An interest exchange is the same type of transaction as the share exchange provided for in section 11.03 of the Model Business Corporation Act. The effect of an interest exchange is that: (i) the separate existence of the acquired entity is not affected; and (ii) the acquiring entity acquires all of the interests of one or more classes of the acquired entity. An interest exchange also allows an indirect acquisition through the use of consideration in the exchange that is not provided by the acquiring entity (*e.g.*, consideration from another or related entity).

Neither share exchanges nor interest exchanges are universally recognized in either corporation or unincorporated entity laws. The effect of an interest exchange can be achieved through a triangular merger in which the acquiring entity forms a new subsidiary and the acquired entity is then merged into the new subsidiary. Part 3 allows the interest exchange to be accomplished directly in a single step, rather than indirectly through the triangular merger route.

The “series” referenced in Subsection (a) are not the series contemplated by the Uniform Statutory Entity Trust Act §§ 401-405 and some LLC statutes. *See, e.g.*, DEL. CODE ANN. tit. 6, § 18-215 (2012); 805 ILL. COMP. STAT. 180/37-40 (2012). Instead, in this context “series” refers to a subset of a class, which is a meaning commonly found in corporation law. *See, e.g.*, MODEL BUS. CORP. ACT § 6.02. Specific provisions authorizing classes and series are less common in unincorporated entity law but do exist. *See, e.g.*, MINN. STAT. § 322B.155 (2012). In any event, a partnership agreement certainly has the power to create classes and series as contemplated by this section.

Subsection (a)—For this section to apply, a domestic limited liability partnership must be either the acquiring or acquired entity.

The acquiring entity is not required to acquire all of the interests in the acquired entity. For example, assume that a general partnership with three classes of partnership interests enters into an interest exchange with an acquiring entity. The acquiring entity need acquire only all of

the partnership interests of one or more classes of the partnership interests.

Subsection (b)—This subsection allows a foreign entity to effectuate an interest exchange with a domestic general partnership if the interest exchange is authorized by the organic law of the foreign entity.

Subsection (c)—This subsection deals with rights of parties to protected agreements, Section 1101(30), when an interest exchange takes place. Because the concept of an interest exchange is relatively new, a person contracting with a domestic general partnership or loaning it money who drafted and negotiated special rights relating to the transaction before the enactment of this article should not be charged with the consequences of not having dealt with the concept of an interest exchange in the context of those special rights. Similarly, when the governance structure of an entity has been negotiated before the enactment of this act, the concept of an interest exchange may not have been reflected in any special governance arrangements; for example, special approval rights may have been provided for fundamental transactions, but those rights fail to include language that would make them applicable to an interest exchange.

Accordingly, this subsection provides a transitional rule that is intended to protect those special rights. If, for example, a general partnership is a party to a contract that provides that the partnership cannot participate in a merger without the consent of the other party to the contract, the requirement to obtain the consent of the other party will apply also to an interest exchange in which the partnership is the acquired entity. If the partnership fails to obtain the consent, the result will be that the other party will have the same rights it would have had if the entity were to participate in a merger without the required consent.

The transitional rule in this subsection ceases to make sense at the time the provisions of the agreement giving rise to the special rights are first amended after the effective date of this article because at that time the provision may be amended to address expressly an interest exchange. The transitional rule will continue to apply, however, if a provision other than the specific provisions giving rise to the special rights is amended.

SECTION 1132. PLAN OF INTEREST EXCHANGE.

(a) A domestic partnership may be the acquired entity in an interest exchange under this [part] by approving a plan of interest exchange. The plan must be in a record and contain:

- (1) the name of the acquired entity;
- (2) the name, jurisdiction of formation, and type of entity of the acquiring entity;
- (3) the manner of converting the interests in the acquired entity into interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing;

(4) any proposed amendments to the partnership agreement that are, or are proposed to be, in a record of the acquired entity;

(5) the other terms and conditions of the interest exchange; and

(6) any other provision required by the law of this state or the partnership agreement of the acquired entity.

(b) In addition to the requirements of subsection (a), a plan of interest exchange may contain any other provision not prohibited by law.

Comment

This section sets forth the requirements for the plan of interest exchange, which must be approved by the acquired entity in accordance with Section 1131. The content of the plan of interest exchange is similar to the content of a plan of merger. *See* Section 1122.

The plan of interest exchange may, but need not, be filed instead of the statement of interest exchange, Section 1135, so long as the plan contains all the information required to be in the statement and is delivered to the filing office for filing after the plan has been adopted and approved. *See* Section 1135(d).

Subsection (a)—The requirements stated in this subsection are mandatory. *See* Section 105(c)(15).

Subsection (a)(3)—Under this paragraph, interest holders in the acquired entity may receive interests or securities of the acquiring entity or of a party other than the acquiring entity, obligations, rights to acquire interests or securities, cash, or other property. *See* the comment to Section 1122(a)(3).

Subsection (b)—This subsection authorizes the plan to contain any other provision the parties wish to include, unless the provision is prohibited by law.

SECTION 1133. APPROVAL OF INTEREST EXCHANGE.

(a) A plan of interest exchange is not effective unless it has been approved:

(1) by all the partners of a domestic acquired partnership entitled to vote on or consent to any matter; and

(2) in a record, by each partner of the domestic acquired partnership that will have interest holder liability for debts, obligations, and other liabilities that are incurred after the

interest exchange becomes effective, unless:

(A) the partnership agreement of the partnership provides in a record for the approval of an interest exchange or a merger in which some or all its partners become subject to interest holder liability by the affirmative vote or consent of fewer than all the partners; and

(B) the partner consented in a record to or voted for that provision of the partnership agreement or became a partner after the adoption of that provision.

(b) An interest exchange involving a domestic acquired entity that is not a partnership is not effective unless it is approved by the domestic entity in accordance with its organic law.

(c) An interest exchange involving a foreign acquired entity is not effective unless it is approved by the foreign entity in accordance with the law of the foreign entity's jurisdiction of formation.

(d) Except as otherwise provided in its organic law or organic rules, the interest holders of the acquiring entity are not required to approve the interest exchange.

Comment

This section sets forth the required approval of an interest exchange. An interest exchange transaction governed by this article requires approval only by the acquired entity, unless the applicable organic law or the organic rules of the acquiring entity otherwise provide, Subsection (d), a condition that rarely exists.

Subsection (a)(2)—For an explanation of this interest holder liability provision, see Section 1123(a)(2), comment.

SECTION 1134. AMENDMENT OR ABANDONMENT OF PLAN OF INTEREST EXCHANGE.

(a) A plan of interest exchange may be amended only with the consent of each party to the plan, except as otherwise provided in the plan.

(b) A domestic acquired partnership may approve an amendment of a plan of interest

exchange:

(1) in the same manner as the plan was approved, if the plan does not provide for the manner in which it may be amended; or

(2) by its partners in the manner provided in the plan, but a partner that was entitled to vote on or consent to approval of the interest exchange is entitled to vote on or consent to any amendment of the plan that will change:

(A) the amount or kind of interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing, to be received by any of the partners of the acquired partnership under the plan;

(B) the partnership agreement of the acquired partnership that will be in effect immediately after the interest exchange becomes effective, except for changes that do not require approval of the partners of the acquired partnership under this [act] or the partnership agreement; or

(C) any other terms or conditions of the plan, if the change would adversely affect the partner in any material respect.

(c) After a plan of interest exchange has been approved and before a statement of interest exchange becomes effective, the plan may be abandoned as provided in the plan. Unless prohibited by the plan, a domestic acquired partnership may abandon the plan in the same manner as the plan was approved.

(d) If a plan of interest exchange is abandoned after a statement of interest exchange has been delivered to the [Secretary of State] for filing and before the statement becomes effective, a statement of abandonment, signed by the acquired partnership, must be delivered to the [Secretary of State] for filing before the statement of interest exchange becomes effective. The

statement of abandonment takes effect on filing, and the interest exchange is abandoned and does not become effective. The statement of abandonment must contain:

- (1) the name of the acquired partnership;
- (2) the date on which the statement of interest exchange was filed by the [Secretary of State]; and
- (3) a statement that the interest exchange has been abandoned in accordance with this section.

Comment

This section parallels provisions in Parts 2 (mergers), 4 (conversions), and 5 (domestications). *See* Sections 1124, 1144, 1154.

SECTION 1135. STATEMENT OF INTEREST EXCHANGE; EFFECTIVE DATE OF INTEREST EXCHANGE.

(a) A statement of interest exchange must be signed by a domestic acquired partnership and delivered to the [Secretary of State] for filing.

(b) A statement of interest exchange must contain:

- (1) the name of the acquired partnership;
 - (2) the name, jurisdiction of formation, and type of entity of the acquiring entity;
- and

(3) a statement that the plan of interest exchange was approved by the acquired partnership in accordance with this [part].

(c) In addition to the requirements of subsection (b), a statement of interest exchange may contain any other provision not prohibited by law.

(d) A plan of interest exchange that is signed by a domestic acquired partnership and meets all the requirements of subsection (b) may be delivered to the [Secretary of State] for filing

instead of a statement of interest exchange and on filing has the same effect. If a plan of interest exchange is filed as provided in this subsection, references in this [article] to a statement of interest exchange refer to the plan of interest exchange filed under this subsection.

(e) An interest exchange becomes effective when the statement of interest exchange is effective.

Comment

This section applies only when the acquired entity is a domestic general partnership. The filing makes the transaction a matter of public record.

This act has no filing requirement when the only domestic general partnership involved is the acquiring entity.

Subsection (b)—This subsection states the requirements for a statement of interest exchange, which are essentially the same as the requirements for a statement of merger under Section 1125(b).

Subsection (d)—A plan of interest exchange can be used as a substitute for the statement of interest exchange so long as the plan satisfies the requirements in Subsection (b).

Subsection (e)—This subsection applies when the acquiring entity is a domestic general partnership, and Section 114 determines when a record delivered for filing under this act becomes effective. A statement of interest exchange may specify a delayed effective time and date, subject to the ninety-day limit stated in Section 114(3) and (4).

If the acquiring entity is not a domestic general partnership, the effectiveness of the interest exchange will occur when provided by the law of the jurisdiction of formation of the acquiring entity.

SECTION 1136. EFFECT OF INTEREST EXCHANGE.

(a) When an interest exchange in which the acquired entity is a domestic partnership becomes effective:

(1) the interests in the acquired partnership which are the subject of the interest exchange are converted, and the partners holding those interests are entitled only to the rights provided to them under the plan of interest exchange and to any appraisal rights they have under

Section 1106;

(2) the acquiring entity becomes the interest holder of the interests in the acquired partnership stated in the plan of interest exchange to be acquired by the acquiring entity; and

(3) the provisions of the partnership agreement of the acquired partnership that are to be in a record, if any, are amended to the extent provided in the plan of interest exchange.

(b) Except as otherwise provided in the partnership agreement of a domestic acquired partnership, the interest exchange does not give rise to any rights that a partner or third party would have upon a dissolution, liquidation, or winding up of the acquired partnership.

(c) When an interest exchange becomes effective, a person that did not have interest holder liability with respect to a domestic acquired partnership and becomes subject to interest holder liability with respect to a domestic entity as a result of the interest exchange has interest holder liability only to the extent provided by the organic law of the entity and only for those debts, obligations, and other liabilities that are incurred after the interest exchange becomes effective.

(d) When an interest exchange becomes effective, the interest holder liability of a person that ceases to hold an interest in a domestic acquired partnership with respect to which the person had interest holder liability is subject to the following rules:

(1) The interest exchange does not discharge any interest holder liability under this [act] to the extent the interest holder liability was incurred before the interest exchange became effective.

(2) The person does not have interest holder liability under this [act] for any debt, obligation, or other liability that is incurred after the interest exchange becomes effective.

(3) This [act] continues to apply to the release, collection, or discharge of any

interest holder liability preserved under paragraph (1) as if the interest exchange had not occurred.

(4) The person has whatever rights of contribution from any other person as are provided by this [act], law other than this [act], or the partnership agreement of the domestic acquired partnership with respect to any interest holder liability preserved under paragraph (1) as if the interest exchange had not occurred.

Comment

This section applies only when the *acquired* entity is a domestic general partnership, and this part states no rule for the effect of an interest exchange when the only domestic general partnership involved is the *acquiring* entity. For that situation, other provisions of this act must be consulted, because this act is the organic law of the acquiring entity.

Subsection (a)—In contrast to a merger, an interest exchange does not in and of itself affect the separate existence of the parties, vest in the acquiring entity the assets of the acquired entity, or render the acquiring entity liable for the liabilities of the acquired entity. Thus, Subsection (a) is significantly simpler than Section 1126(a) with respect to the effects of a merger.

When an interest exchange becomes effective: (i) the interests of the acquired domestic general partnership are exchanged, converted, or canceled as provided in the plan; (ii) the only rights of the former partners and transferees of the acquired partnership whose interests are affected by the interest exchange are those rights related to the exchange, conversion, or cancellation; (iii) the acquiring entity becomes the owner of the acquired partnership's interests as provided in the plan; and (iv) the provisions of the partnership agreement of the acquired partnership that are to be in a record, if any, are amended to the extent provided in the plan of interest exchange.

Subsection (c)—This subsection provides the rule for future interest holder liability pertaining to domestic entities and parallels analogous provisions in Parts 2 (mergers), 4 (conversions), and 5 (domestications). *See* the comment to Section 1126.

Subsection (d)—This subsection provides the rule for past interest holder liability and parallels analogous provisions in Parts 2 (mergers), 4 (conversions), and 5 (domestications). *See* the comments to Sections 1126(d) and 1146(d).

[PART] 4

CONVERSION

SECTION 1141. CONVERSION AUTHORIZED.

(a) By complying with this [part], a domestic partnership may become:

(1) a domestic entity that is a different type of entity; or

(2) a foreign entity that is a different type of entity, if the conversion is authorized

by the law of the foreign entity's jurisdiction of formation.

(b) By complying with the provisions of this [part] applicable to foreign entities, a foreign entity that is not a foreign partnership may become a domestic partnership if the conversion is authorized by the law of the foreign entity's jurisdiction of formation.

(c) If a protected agreement contains a provision that applies to a merger of a domestic partnership but does not refer to a conversion, the provision applies to a conversion of the partnership as if the conversion were a merger until the provision is amended after [the effective date of this [act]].

Comment

This part of Article 11 permits an entity to change to a different type of entity. A transaction in which an entity changes its jurisdiction of organization but does not change its type is a domestication and is the subject of Part 5.

Subsection (a)(2)—For this provision to apply, this type of conversion must be authorized by the law of the foreign jurisdiction. If this is not the case, it may be possible to achieve the same result by forming an entity of the type desired in the foreign jurisdiction and then merging the domestic entity into the new foreign entity under Part 2 of Article 11.

Subsection (b)—This subsection allows a foreign entity to effectuate a conversion into a domestic general partnership, but only if the conversion is permitted by the laws of the foreign entity's jurisdiction of formation. When a foreign entity becomes a domestic general partnership pursuant to this part of Article 11, the effect of the conversion will be as provided in Section 1146. The procedures by which the conversion is approved, however, will be determined by the laws of the foreign entity's jurisdiction of formation. See Section 102(8) for the definition of "jurisdiction of formation."

Subsection (c)—For more information on an authorized interest exchange, see Section 1131(c), comment.

SECTION 1142. PLAN OF CONVERSION.

(a) A domestic partnership may convert to a different type of entity under this [part] by approving a plan of conversion. The plan must be in a record and contain:

- (1) the name of the converting partnership;
- (2) the name, jurisdiction of formation, and type of entity of the converted entity;
- (3) the manner of converting the interests in the converting partnership into interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing;
- (4) the proposed public organic record of the converted entity if it will be a filing entity;
- (5) the full text of the private organic rules of the converted entity which are proposed to be in a record;
- (6) the other terms and conditions of the conversion; and
- (7) any other provision required by the law of this state or the partnership agreement of the converting partnership.

(b) In addition to the requirements of subsection (a), a plan of conversion may contain any other provision not prohibited by law.

Comment

This section sets forth the requirements for the plan of conversion, which must be approved by the converting entity in accordance with Section 1143. The content of a plan of conversion is similar to the content of a plan of merger. *See* Section 1122.

Subsection (a)—The requirements stated in this subsection are mandatory. *See* Section 105(c)(15).

Subsection (a)(3)—Interest holders in the converting entity may receive interests or other securities of the converted entity or of any other person, obligations, rights to acquire interests or other securities, cash, or other property. *See* Sections 1122(a)(3) (mergers), 1132(a)(3) (interest exchanges), 1152(a)(3) (domestications).

Subsection (b)—This subsection authorizes the plan to contain any other provision the parties wish to include, unless the provision is prohibited by law.

SECTION 1143. APPROVAL OF CONVERSION.

(a) A plan of conversion is not effective unless it has been approved:

(1) by a domestic converting partnership, by all the partners of the partnership entitled to vote on or consent to any matter; and

(2) in a record, by each partner of a domestic converting partnership which will have interest holder liability for debts, obligations, and other liabilities that are incurred after the conversion becomes effective, unless:

(A) the partnership agreement of the partnership provides in a record for the approval of a conversion or a merger in which some or all of its partners become subject to interest holder liability by the affirmative vote or consent of fewer than all the partners; and

(B) the partner voted for or consented in a record to that provision of the partnership agreement or became a partner after the adoption of that provision.

(b) A conversion involving a domestic converting entity that is not a partnership is not effective unless it is approved by the domestic converting entity in accordance with its organic law.

(c) A conversion of a foreign converting entity is not effective unless it is approved by the foreign entity in accordance with the law of the foreign entity's jurisdiction of formation.

Comment

Subsection (a)(1)—This provision is a default rule, subject to change in the partnership agreement.

Subsection (a)(2)—This provision is not a default rule. Section 105(c)(14). For an explanation of this interest holder liability provision, see Section 1123(a)(2), comment.

SECTION 1144. AMENDMENT OR ABANDONMENT OF PLAN OF CONVERSION.

(a) A plan of conversion of a domestic converting partnership may be amended:

(1) in the same manner as the plan was approved, if the plan does not provide for the manner in which it may be amended; or

(2) by its partners in the manner provided in the plan, but a partner that was entitled to vote on or consent to approval of the conversion is entitled to vote on or consent to any amendment of the plan that will change:

(A) the amount or kind of interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing, to be received by any of the partners of the converting partnership under the plan;

(B) the public organic record, if any, or private organic rules of the converted entity which will be in effect immediately after the conversion becomes effective, except for changes that do not require approval of the interest holders of the converted entity under its organic law or organic rules; or

(C) any other terms or conditions of the plan, if the change would adversely affect the partner in any material respect.

(b) After a plan of conversion has been approved by a domestic converting partnership and before a statement of conversion becomes effective, the plan may be abandoned as provided in the plan. Unless prohibited by the plan, a domestic converting partnership may abandon the plan in the same manner as the plan was approved.

(c) If a plan of conversion is abandoned after a statement of conversion has been

delivered to the [Secretary of State] for filing and before the statement becomes effective, a statement of abandonment, signed by the converting entity, must be delivered to the [Secretary of State] for filing before the statement of conversion becomes effective. The statement of abandonment takes effect on filing, and the conversion is abandoned and does not become effective. The statement of abandonment must contain:

- (1) the name of the converting partnership;
- (2) the date on which the statement of conversion was filed by the [Secretary of State]; and
- (3) a statement that the conversion has been abandoned in accordance with this section.

Comment

This section parallels analogous provisions in Parts 2 (mergers), 3 (interest exchanges), and 5 (domestications). *See* Sections 1124, 1134, 1154.

SECTION 1145. STATEMENT OF CONVERSION; EFFECTIVE DATE OF CONVERSION.

(a) A statement of conversion must be signed by the converting entity and delivered to the [Secretary of State] for filing.

(b) A statement of conversion must contain:

- (1) the name, jurisdiction of formation, and type of entity of the converting entity;
- (2) the name, jurisdiction of formation, and type of entity of the converted entity;
- (3) if the converting entity is a domestic partnership, a statement that the plan of conversion was approved in accordance with this [part] or, if the converting entity is a foreign entity, a statement that the conversion was approved by the foreign entity in accordance with the law of its jurisdiction of formation;

(4) if the converted entity is a domestic filing entity, its public organic record, as an attachment; and

(5) if the converted entity is a domestic limited liability partnership, its statement of qualification, as an attachment.

(c) In addition to the requirements of subsection (b), a statement of conversion may contain any other provision not prohibited by law.

(d) If the converted entity is a domestic entity, its public organic record, if any, must satisfy the requirements of the law of this state, except that the public organic record does not need to be signed.

(e) A plan of conversion that is signed by a domestic converting partnership and meets all the requirements of subsection (b) may be delivered to the [Secretary of State] for filing instead of a statement of conversion and on filing has the same effect. If a plan of conversion is filed as provided in this subsection, references in this [article] to a statement of conversion refer to the plan of conversion filed under this subsection.

(f) If the converted entity is a domestic partnership, the conversion becomes effective when the statement of conversion is effective. In all other cases, the conversion becomes effective on the later of:

- (1) the date and time provided by the organic law of the converted entity; and
- (2) when the statement is effective.

Comment

This section applies regardless of whether a domestic general partnership is the converting or converted entity. A foreign entity seeking to convert to a domestic general partnership must therefore comply with this section.

If either the converting or converted entity is a foreign entity, the organic law of the foreign entity's jurisdiction must also be consulted.

The filing of a statement of conversion makes the transaction a matter of public record.

Subsection (b)—This subsection sets forth the requirements for a statement of conversion. They are essentially the same as the requirements for a statement of merger in Section 1125.

Subsection (e)—A plan of conversion can be used as a substitute for the statement of conversion so long as the plan satisfies the requirements in Subsection (b).

Subsection (f)—Section 114 determines when a record delivered for filing under this act becomes effective. A statement of conversion may specify a delayed effective time and date, subject to the ninety-day limit stated in Section 114(3) and (4).

When the statement of conversion has become effective under this subsection, the conversion transaction occurs if the converted entity is a domestic general partnership. A conversion in which the converted entity is a foreign entity will usually also take effect when the statement of conversion takes effect because the best practice will be to coordinate the filings that need to be made when a conversion involves both a domestic entity and also a foreign entity so that the filings in each jurisdiction take effect at the same time.

However, when the converting general partnership is a foreign general partnership, it is possible that the filing in the foreign jurisdiction will take effect at a different time. For that reason, this subsection provides that the conversion will take effect at the later of: (i) when the statement of conversion takes effect; and (ii) when the conversion takes effect under the law of the foreign jurisdiction. This rule avoids the possibility that the conversion will take effect in this state before it takes effect in the foreign jurisdiction, which would produce the undesirable result that the converting domestic general partnership would cease to appear as an active entity on the records of this state before appearing as its active, converted self on the records of the foreign jurisdiction.

It is necessary for the filing office to record only the effective date of the statement of conversion, and the filing office does not need to be concerned with the effective date of the conversion itself. Persons wishing to determine the effective date of a conversion involving both a domestic general partnership and a foreign entity will be able to do so by consulting the records of the filing offices in each jurisdiction.

SECTION 1146. EFFECT OF CONVERSION.

(a) When a conversion becomes effective:

(1) the converted entity is:

(A) organized under and subject to the organic law of the converted entity;

and

(B) the same entity without interruption as the converting entity;

(2) all property of the converting entity continues to be vested in the converted entity without transfer, reversion, or impairment;

(3) all debts, obligations, and other liabilities of the converting entity continue as debts, obligations, and other liabilities of the converted entity;

(4) except as otherwise provided by law or the plan of conversion, all the rights, privileges, immunities, powers, and purposes of the converting entity remain in the converted entity;

(5) the name of the converted entity may be substituted for the name of the converting entity in any pending action or proceeding;

(6) if the converted entity is a limited liability partnership, its statement of qualification becomes effective;

(7) the provisions of the partnership agreement of the converted entity which are to be in a record, if any, approved as part of the plan of conversion become effective; and

(8) the interests in the converting entity are converted, and the interest holders of the converting entity are entitled only to the rights provided to them under the plan of conversion and to any appraisal rights they have under Section 1106.

(b) Except as otherwise provided in the partnership agreement of a domestic converting partnership, the conversion does not give rise to any rights that a partner or third party would have upon a dissolution, liquidation, or winding up of the converting entity.

(c) When a conversion becomes effective, a person that did not have interest holder liability with respect to the converting entity and becomes subject to interest holder liability with respect to a domestic entity as a result of the conversion has interest holder liability only to the

extent provided by the organic law of the entity and only for those debts, obligations, and other liabilities that are incurred after the conversion becomes effective.

(d) When a conversion becomes effective, the interest holder liability of a person that ceases to hold an interest in a domestic converting partnership with respect to which the person had interest holder liability is subject to the following rules:

(1) The conversion does not discharge any interest holder liability under this [act] to the extent the interest holder liability was incurred before the conversion became effective.

(2) The person does not have interest holder liability under this [act] for any debt, obligation, or other liability that is incurred after the conversion becomes effective.

(3) This [act] continues to apply to the release, collection, or discharge of any interest holder liability preserved under paragraph (1) as if the conversion had not occurred.

(4) The person has whatever rights of contribution from any other person as are provided by this [act], law other than this [act], or the organic rules of the converting entity with respect to any interest holder liability preserved under paragraph (1) as if the conversion had not occurred.

(e) When a conversion has become effective, a foreign entity that is the converted entity may be served with process in this state for the collection and enforcement of any of its debts, obligations, and other liabilities as provided in Section 119.

(f) If the converting entity is a registered foreign entity, its registration to do business in this state is canceled when the conversion becomes effective.

(g) A conversion does not require the entity to wind up its affairs and does not constitute or cause the dissolution of the entity.

Comment

A converted entity is the same entity as it was before the conversion; the entity just has a different legal form.

Subsection (a)—This subsection states the principal legal effects of a conversion. The converted entity remains the owner of all real and personal property and remains subject to all the liabilities, actual or contingent, of the converted entity. A conversion is not a conveyance, transfer, or assignment. A conversion does not give rise to: (i) claims of reverter or impairment of title based on a prohibited conveyance or transfer; or (ii) to a claim that a contract with the converting entity is no longer in effect on the ground of nonassignability, unless the contract specifically provides that it does not survive a conversion. The contract rights that remain in the converted entity include, without limitation, the right to enforce subscription agreements for interests and obligations to make capital contributions entered into or incurred before the conversion.

When a conversion becomes effective, the internal affairs of the converting entity are no longer governed by its former organic law but instead by the organic law of the converted entity. As a result, filings that may have been made under the organic law of the converting entity, such as the following, will no longer be effective: a statement of qualification as a limited liability partnership under UPA (1997) (Last Amended 2013) § 901, a statement of partnership authority under Section 303 of that act, a statement of authority under Section of the ULLCA (2006) (Last Amended 2013) § 302, or under Uniform Unincorporated Nonprofit Association Act (2008) (Last Amended 2013) § 7.

Subsection (a)(5)—All pending proceedings involving the converting entity are continued. The name of the converted entity may be, but need not be, substituted in any pending proceeding for the name of the converting entity.

Subsection (c)—This subsection provides the rule for future interest holder liability and parallels provisions in Parts 2 (mergers), 3 (interest exchanges), and 5 (domestications). *See* the comment to Section 1126(c).

Subsection (d)—Subsection (d) provides the rule for past interest holder liability and parallels analogous provisions in Parts 2 (mergers), 3 (interest exchanges), and 5 (domestications). *See* the comment to Section 1126(d).

Subsection (e)—For this provision to apply, the converting entity must have been a domestic general partnership. When a domestic general partnership becomes a foreign entity as a result of a conversion, some mechanism is needed to facilitate the enforcement of claims by the creditors and interest holders of the converting partnership. This subsection, which parallels analogous provisions in Parts 2 (mergers) and 5 (domestications), authorizes service of process for all such claims in this state.

Subsection (g)—When a conversion takes effect, the entity continues to exist—simply in a different form. This subsection thus makes clear that the conversion does not require the entity

to wind up its affairs and does not constitute or cause the dissolution of the entity.

[PART] 5

DOMESTICATION

SECTION 1151. DOMESTICATION AUTHORIZED.

(a) By complying with this [part], a domestic limited liability partnership may become a foreign limited liability partnership if the domestication is authorized by the law of the foreign jurisdiction.

(b) By complying with the provisions of this [part] applicable to foreign limited liability partnerships, a foreign limited liability partnership may become a domestic limited liability partnership if the domestication is authorized by the law of the foreign limited liability partnership's jurisdiction of formation.

(c) If a protected agreement contains a provision that applies to a merger of a domestic limited liability partnership but does not refer to a domestication, the provision applies to a domestication of the limited liability partnership as if the domestication were a merger until the provision is amended after [the effective date of this [act]].

Comment

A domestication authorized by Part 5 of Article 11 differs from a conversion in that a domestication requires that the domesticating entity be the same type of entity as the domesticated entity. In a conversion, by contrast, the converting entity changes its type.

As with a conversion, all rights and privileges, debts, obligations and other liabilities, and actions or proceedings of a domesticating entity remain vested in the domesticated entity. A domestication is not a sale, transfer, assignment, or conveyance and does not give rise to a claim of reverter or impairment of title. *See* the comment to Section 1146(a).

Part 5 of Article 11 governs the legal effect of a foreign limited liability partnership domesticating in this state. On the other hand, the organic laws of the foreign jurisdiction, and not Part 5, will govern the legal effect of most aspects of a domestication of a domestic limited liability partnership in another jurisdiction. In the latter scenario, Part 5 authorizes the domestication of the domestic entity in the foreign jurisdiction, but Part 5 does not create a right

in the domestic entity to be received in the foreign jurisdiction. Similarly, this section does not provide a right on the part of a foreign limited liability partnership to become a domestic limited liability partnership if the domestication is not authorized by the laws of the foreign jurisdiction. If the foreign jurisdiction does not authorize a domestication transaction, the same results can be accomplished by forming a new limited liability partnership in this state and merging the existing foreign limited liability partnership into the new domestic limited liability partnership.

Subsection (a)—Unlike the Parts 2 (merger), 3 (interest exchange), and 4 (conversion), Part 5 applies only to limited liability partnerships. However, a non-LLP general partnership that seeks to change its governing law may:

- amend its partnership agreement to specify the governing law of the desired jurisdiction, if the partnership intends to remain non-LLP; or
- deliver to the filing office in the desired jurisdiction a statement of qualification, if the partnership intends not only to change its governing law but also to become an LLP.

Subsection (c)—For the parallel provision pertaining to mergers, see Section 1131(c).

SECTION 1152. PLAN OF DOMESTICATION.

(a) A domestic limited liability partnership may become a foreign limited liability partnership in a domestication by approving a plan of domestication. The plan must be in a record and contain:

- (1) the name of the domesticating limited liability partnership;
- (2) the name and jurisdiction of formation of the domesticated limited liability partnership;
- (3) the manner of converting the interests in the domesticating limited liability partnership into interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing;
- (4) the proposed statement of qualification of the domesticated limited liability partnership;
- (5) the full text of the provisions of the partnership agreement of the domesticated limited liability partnership that are proposed to be in a record;
- (6) the other terms and conditions of the domestication; and

(7) any other provision required by the law of this state or the partnership agreement of the domesticating limited liability partnership.

(b) In addition to the requirements of subsection (a), a plan of domestication may contain any other provision not prohibited by law.

Comment

This section sets forth the requirements for the plan of domestication for a domestic limited liability partnership seeking to become a limited liability partnership existing under the law of another jurisdiction. For a foreign limited liability partnership seeking to become a domestic limited liability partnership, the organic law of the foreign limited liability partnership governs the requirements for a plan of domestication. The content of a plan of domestication is similar to the content of a plan of merger. *See* Section 1122.

Subsection (a)—The requirements stated in this subsection are mandatory. *See* Section 105(c)(15).

Subsection (a)(3)—Interest holders in the domesticating limited liability partnership may receive interests or other securities of the domesticated limited liability partnership or any other entity, obligations, rights to acquire interests or other securities, cash, or other property. *See* the comment to Section 1122(a)(3).

Subsection (b)—This subsection authorizes the plan to contain any other provision the parties wish to include, unless the provision is prohibited by law.

SECTION 1153. APPROVAL OF DOMESTICATION.

(a) A plan of domestication of a domestic domesticating limited liability partnership is not effective unless it has been approved:

(1) by all the partners entitled to vote on or consent to any matter; and

(2) in a record, by each partner that will have interest holder liability for debts, obligations, and other liabilities that are incurred after the domestication becomes effective, unless:

(A) the partnership agreement of the domesticating partnership in a record provides for the approval of a domestication or merger in which some or all of its partners

become subject to interest holder liability by the affirmative vote or consent of fewer than all the partners; and

(B) the partner voted for or consented in a record to that provision of the partnership agreement or became a partner after the adoption of that provision.

(b) A domestication of a foreign domesticating limited liability partnership is not effective unless it is approved in accordance with the law of the foreign limited liability partnership's jurisdiction of formation.

Comment

Subsection (a)(1)—This provision is a default rule, subject to change in the partnership agreement.

Subsection (a)(2)—This provision is mandatory. Section 105(c)(14). For an explanation of the provision, see Section 1123(a)(2), comment.

Subsection (b)—In the case of a foreign limited liability partnership that is domesticating in this state, this subsection provides that the required approval is determined by the laws of the foreign limited liability partnership's jurisdiction of formation (which in this context means the jurisdiction in which the foreign LLP's statement of qualification is filed).

SECTION 1154. AMENDMENT OR ABANDONMENT OF PLAN OF DOMESTICATION.

(a) A plan of domestication of a domestic domesticating limited liability partnership may be amended:

(1) in the same manner as the plan was approved, if the plan does not provide for the manner in which it may be amended; or

(2) by its partners in the manner provided in the plan, but a partner that was entitled to vote on or consent to approval of the domestication is entitled to vote on or consent to any amendment of the plan that will change:

(A) the amount or kind of interests, securities, obligations, money, other

property, rights to acquire interests or securities, or any combination of the foregoing, to be received by any of the partners of the domesticating limited liability partnership under the plan;

(B) the partnership agreement of the domesticated limited liability partnership that will be in effect immediately after the domestication becomes effective, except for changes that do not require approval of the partners of the domesticated limited liability partnership under its organic law or partnership agreement; or

(C) any other terms or conditions of the plan, if the change would adversely affect the partner in any material respect.

(b) After a plan of domestication has been approved by a domestic domesticating limited liability partnership and before a statement of domestication becomes effective, the plan may be abandoned as provided in the plan. Unless prohibited by the plan, a domestic domesticating limited liability partnership may abandon the plan in the same manner as the plan was approved.

(c) If a plan of domestication is abandoned after a statement of domestication has been delivered to the [Secretary of State] for filing and before the statement becomes effective, a statement of abandonment, signed by the domesticating limited liability partnership, must be delivered to the [Secretary of State] for filing before the statement of domestication becomes effective. The statement of abandonment takes effect on filing, and the domestication is abandoned and does not become effective. The statement of abandonment must contain:

(1) the name of the domesticating limited liability partnership;

(2) the date on which the statement of domestication was filed by the [Secretary of State]; and

(3) a statement that the domestication has been abandoned in accordance with this section.

Comment

This section parallels provisions in Parts 2 (mergers), 3 (interest exchanges), and 4 (conversions). *See* Sections 1124 (mergers), 1134 (interest exchanges), 1144 (conversions).

SECTION 1155. STATEMENT OF DOMESTICATION; EFFECTIVE DATE OF DOMESTICATION.

(a) A statement of domestication must be signed by the domesticating limited liability partnership and delivered to the [Secretary of State] for filing.

(b) A statement of domestication must contain:

(1) the name and jurisdiction of formation of the domesticating limited liability partnership;

(2) the name and jurisdiction of formation of the domesticated limited liability partnership;

(3) if the domesticating limited liability partnership is a domestic limited liability partnership, a statement that the plan of domestication was approved in accordance with this [part] or, if the domesticating limited liability partnership is a foreign limited liability partnership, a statement that the domestication was approved in accordance with the law of its jurisdiction of formation; and

(4) the statement of qualification of the domesticated limited liability partnership, as an attachment.

(c) In addition to the requirements of subsection (b), a statement of domestication may contain any other provision not prohibited by law.

(d) The statement of qualification of a domesticated domestic limited liability partnership must satisfy the requirements of this [act], but the statement does not need to be signed.

(e) A plan of domestication that is signed by a domesticating domestic limited liability

partnership and meets all the requirements of subsection (b) may be delivered to the [Secretary of State] for filing instead of a statement of domestication and on filing has the same effect. If a plan of domestication is filed as provided in this subsection, references in this [article] to a statement of domestication refer to the plan of domestication filed under this subsection.

(f) If the domesticated entity is a domestic partnership, the domestication becomes effective when the statement of domestication is effective. If the domesticated entity is a foreign partnership, the domestication becomes effective on the later of:

- (1) the date and time provided in the organic law of the domesticated entity; and
- (2) when the statement is effective.

Comment

Regardless of whether a domestic limited liability partnership is the domesticating or domesticated entity:

- This section applies and, therefore, a foreign limited liability partnership seeking to domesticate and thereby become a domestic LLP must comply with this section.
 - The organic law of the foreign LLP's jurisdiction must also be consulted.
- The filing of a statement of domestication makes the transaction a matter of public record.

Subsection (b)—This subsection sets forth the requirements for a statement of domestication. They are essentially the same as the requirements for a statement of merger in Section 1125.

Subsection (e)—A plan of domestication can be used as a substitute for the statement of domestication so long as the plan satisfies the requirements in Subsection (b).

Subsection (f)—Section 114 determines when a record delivered for filing under this act becomes effective. A statement of domestication may specify a delayed effective time and date, subject to the ninety-day limit stated in Section 114(3) and (4).

When the statement of domestication becomes effective under this subsection, the domestication transaction occurs if the domesticated entity is a domestic limited liability partnership. A domestication in which the domesticated entity is a foreign limited liability partnership will usually also take effect when the statement of domestication takes effect because the best practice will be to coordinate the filings that need to be made in each jurisdiction so that they take effect at the same time.

However, when the domesticated general partnership is a foreign general partnership, it is possible that the filing in the foreign jurisdiction will take effect at a different time. For that reason, this subsection provides that the domestication will take effect at the later of: (i) when the statement of domestication takes effect; and (ii) when the domestication takes effect under the law of the foreign jurisdiction. This rule avoids the possibility that the domestication will take effect in this state before it takes effect in the foreign jurisdiction, which would produce the undesirable result that the domesticating domestic general partnership would cease to appear as an active entity on the records of this state before appearing as its active, domesticated self on the records of the foreign jurisdiction.

It is necessary for the filing office to record only the effective date of the statement of domestication, and the filing office does not need to be concerned with the effective date of the domestication itself. Persons wishing to determine the effective date of a domestication will be able to do so by consulting the records of the filing offices in each jurisdiction.

SECTION 1156. EFFECT OF DOMESTICATION.

(a) When a domestication becomes effective:

(1) the domesticated entity is:

(A) organized under and subject to the organic law of the domesticated entity; and

(B) the same entity without interruption as the domesticating entity;

(2) all property of the domesticating entity continues to be vested in the domesticated entity without transfer, reversion, or impairment;

(3) all debts, obligations, and other liabilities of the domesticating entity continue as debts, obligations, and other liabilities of the domesticated entity;

(4) except as otherwise provided by law or the plan of domestication, all the rights, privileges, immunities, powers, and purposes of the domesticating entity remain in the domesticated entity;

(5) the name of the domesticated entity may be substituted for the name of the domesticating entity in any pending action or proceeding;

(6) the statement of qualification of the domesticated entity becomes effective;

(7) the provisions of the partnership agreement of the domesticated entity that are to be in a record, if any, approved as part of the plan of domestication become effective; and

(8) the interests in the domesticating entity are converted to the extent and as approved in connection with the domestication, and the partners of the domesticating entity are entitled only to the rights provided to them under the plan of domestication and to any appraisal rights they have under Section 1106.

(b) Except as otherwise provided in the organic law or partnership agreement of the domesticating limited liability partnership, the domestication does not give rise to any rights that a partner or third party would otherwise have upon a dissolution, liquidation, or winding up of the domesticating partnership.

(c) When a domestication becomes effective, a person that did not have interest holder liability with respect to the domesticating limited liability partnership and becomes subject to interest holder liability with respect to a domestic limited liability partnership as a result of the domestication has interest holder liability only to the extent provided by this [act] and only for those debts, obligations, and other liabilities that are incurred after the domestication becomes effective.

(d) When a domestication becomes effective, the interest holder liability of a person that ceases to hold an interest in a domestic domesticating limited liability partnership with respect to which the person had interest holder liability is subject to the following rules:

(1) The domestication does not discharge any interest holder liability under this [act] to the extent the interest holder liability was incurred before the domestication became effective.

(2) A person does not have interest holder liability under this [act] for any debt,

obligation, or other liability that is incurred after the domestication becomes effective.

(3) This [act] continues to apply to the release, collection, or discharge of any interest holder liability preserved under paragraph (1) as if the domestication had not occurred.

(4) A person has whatever rights of contribution from any other person as are provided by this [act], law other than this [act], or the partnership agreement of the domestic domesticating limited liability partnership with respect to any interest holder liability preserved under paragraph (1) as if the domestication had not occurred.

(e) When a domestication becomes effective, a foreign limited liability partnership that is the domesticated partnership may be served with process in this state for the collection and enforcement of any of its debts, obligations, and other liabilities as provided in Section 119.

(f) If the domesticating limited liability partnership is a registered foreign entity, the registration of the partnership is canceled when the domestication becomes effective.

(g) A domestication does not require a domestic domesticating limited liability partnership to wind up its business and does not constitute or cause the dissolution of the partnership.

Comment

Subsection (a)(1)—The domesticated entity is the same entity as the domesticating entity; it has merely changed its jurisdiction of formation.

Subsection (a)(2)—A domestication is not a sale, conveyance, transfer, or assignment and does not give rise to claims of reverter or impairment of title that may be based on a prohibition on transfer, assignment, or conveyance.

Subsection (a)(4)—All pending proceedings involving the domesticating entity are continued. The name of the domesticated entity may be, but need not be, substituted in any pending proceeding for the name of the domesticating entity.

Subsection (a)(8)—The interests of the domesticating limited liability partnership are reclassified into whatever rights were negotiated in the domestication and the partners and transferees of the domesticating LLP are entitled only to those rights. Paragraph 8, on its face,

allows for certain partners of the domesticating LLP to be entitled to a continuing equity interest in the domesticated LLP whereas other partners of the domesticating LLP may be cashed out as a result of the transaction.

Subsection (c)—This subsection provides the rule for future interest holder liability and parallels analogous provisions in Parts 2 (mergers), 3 (interest exchanges), and 4 (conversions). *See* the comment to Section 1126(c).

Subsection (d)—This subsection provides the rule for past interest holder liability and parallels analogous provisions in Parts 2 (mergers), 3 (interest exchanges), and 4 (conversions). *See* the comments to Sections 1126(d) and 1146(d).

Subsection (e)—When a domestic domesticating limited liability partnership becomes a foreign LLP as a result of a domestication, some mechanism is needed to facilitate the enforcement of claims by the creditors and interest holders of the domesticating LLP. This subsection, which parallels analogous provisions in Parts 2 (mergers) and 4 (conversions), authorizes service of process for all such claims in this state.

Subsection (g)—When a domestication takes effect, the entity continues to exist—simply as a domestic entity under the laws of a different state. This subsection thus makes clear that the domestication does not require the limited liability partnership to wind up its affairs and does not constitute or cause the dissolution of the limited liability partnership.

[ARTICLE] 12

MISCELLANEOUS PROVISIONS

SECTION 1201. UNIFORMITY OF APPLICATION AND CONSTRUCTION. In applying and construing this uniform act, consideration must be given to the need to promote uniformity of the law with respect to its subject matter among states that enact it.

SECTION 1202. RELATION TO ELECTRONIC SIGNATURES IN GLOBAL AND NATIONAL COMMERCE ACT. This [act] modifies, limits, and supersedes the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001 et seq., but does not modify, limit, or supersede Section 101(c) of that act, 15 U.S.C. Section 7001(c), or authorize electronic delivery of any of the notices described in Section 103(b) of that act, 15 U.S.C. Section 7003(b).

Comment

This section responds to specific language of the Electronic Signatures in Global and National Commerce Act and is designed to avoid preemption of state law under that federal legislation.

SECTION 1203. SAVINGS CLAUSE. This [act] does not affect an action commenced, proceeding brought, or right accrued before [the effective date of this [act]].

Comment

This section continues prior law after the effective date of this act with respect to rights accrued and proceedings. But for this section, the new law of this act would displace the old laws in some circumstances. The power of a new act to displace the old statute with respect to conduct occurring before the new act's enactment is substantial. Millard H. Ruud, *The Savings Clause—Some Problems in Construction and Drafting*, 33 TEX. L. REV. 285, 286–93 (1955). A court generally applies the law that exists at the time it acts.

Eventually, this act will apply all to pre-existing general partnerships—whether by choice under Section 110(a)(2) (permitting an early opt-in), or without choice on the “all-inclusive date.” Section 110(b). In this context, the phrase “before [the effective date of this [act]]” should be understood as referring to the date upon which this act becomes applicable to the particular general partnership at issue.

[SECTION 1204. SEVERABILITY CLAUSE. If any provision of this [act] or its application to any person or circumstance is held invalid, the invalidity does not affect other provisions or applications of this [act] which can be given effect without the invalid provision or application, and to this end the provisions of this [act] are severable.]

Legislative Note: *Include this section only if this state lacks a general severability statute or decision by the highest court of this state stating a general rule of severability.*

SECTION 1205. REPEALS. The following are repealed:

(1) [the state partnership act as [amended, and as] in effect immediately before [the effective date of this [act]]].

(2)

(3)

SECTION 1206. EFFECTIVE DATE. This [act] takes effect

Comment

For the effect of the act's effective date on pre-existing partnerships, see Section 110.