

Is your limited partnership agreement out of date?

By Melissa Sayer

On January 1, 2008, California enacted the Uniform Limited Partnership Act of 2008. Any limited partnership formed after 2007 is subject to the New Act. With some limited exceptions, any limited partnership formed before 2008 is not subject to the New Act until January 1, 2010. Some of the major differences between the old law and the New Act are greater protections for general and limited partners, changes in default rules regarding allocation of profits and losses and changes in default rules regarding transfers of limited partnership interests.

If you have an existing limited partnership agreement that does NOT specifically address allocation of profits and losses or transfers of limited partnership interests, you should consult your legal advisor to review the partnership agreement.

The old law and the New Act provide that the limited partnership agreement can designate how profits and losses are shared among the partners. However, if no provision for profits and losses is made, the old law and the New Act have different "default" rules as to how profits and losses are allocated. Under the old law, profits and losses were allocated in proportion to the contributions made by each partner. The New Act allocates profits and losses in the same manner that distributions are made to each partner (which may or may not be in proportion to the contributions of each partner). This is particularly troublesome because a partner's rights to statutory distributions are now more limited under the New Act. If your partnership agreement does not specifically provide for how profits and losses are to be allocated to the partners, you should strongly consider revising the agreement to specifically address this issue.

Limited partnerships are often used in family businesses or closely held businesses and transfers of partnership interests are an integral part of the planning process. Under both the



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old and the New Act, a partnership agreement can set forth how partnership interests are transferred. However, if the partnership agreement does not specifically address transfers of partnership interests, the default rules under the New Act apply. The default rules under the New Act are significantly different than under previous law. The New Act divides a partnership interest into economic and non-economic rights. Under the New Act, only the right to receive distributions can be transferred and a transferee is not considered a partner. Any "non-economic" rights (such as voting rights) are not transferred unless specifically provided for in the partnership agreement. If the partners want to transfer more than the right to receive distributions, this should be carefully set forth in the partnership agreement.

An older limited partnership may voluntarily elect to be subject to the New Act now rather than wait until 2010. Because of the greater protections to limited partners and general partners, you may want to opt to have the New Act apply to your limited partnership before January 1, 2010. A limited partnership may have one or more general partners and one or more limited partners. Except in a few circumstances, the general partner has exclusive management and control over the partnership whereas the limited partner's participation in management is very limited. Limited control is important in that a limited partner is insulated from personal liability unless he or she is deemed to participate in management and control. The New Act contains an extensive list of specific actions that do not

constitute participating in management and control. Therefore, a limited partner may potentially increase the powers and rights that he or she can exercise and remain insulated from liability.

General partners in the partnership owe certain fiduciary duties to their partners. Breach of a fiduciary duty by a general partner is a serious offense with significant consequences. The New Act provides greater protection to general partners by limiting the fiduciary duties of general partners to three distinct areas. No fiduciary duties are specified for limited partners under the New Act, although they must act consistent with their obligation of good faith and fair dealing.

Even after 2009, some of the provisions of the New Act will not apply to limited partnerships formed before 2008, unless the partnership affirmatively elects to be governed by the New Act. These provisions deal with duration of the partnership, disassociation rights of partners and dissolution under certain circumstances.

The decision whether to elect to be subject to the New Act and the need to update your limited partnership agreement is dependent on a variety of factors and should be considered carefully in consultation with your legal adviser.

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Cece Alemania (left) and Priscilla Becker discuss a project.

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