

# HOUSE BILL REPORT

## HB 2386

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### As Reported By House Committee On:

Law & Justice

**Title:** An act relating to the revised uniform partnership act.

**Brief Description:** Creating the revised uniform partnership act.

**Sponsors:** Representatives Sheahan, Appelwick, Constantine, Kenney and Costa.

### Brief History:

#### Committee Activity:

Law & Justice: 1/21/98, 1/23/98 [DPS].

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## HOUSE COMMITTEE ON LAW & JUSTICE

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 13 members: Representatives Sheahan, Chairman; McDonald, Vice Chairman; Sterk, Vice Chairman; Costa, Ranking Minority Member; Constantine, Assistant Ranking Minority Member; Carrell; Cody; Kenney; Lambert; Lantz; Mulliken; Robertson and Sherstad.

**Staff:** Edie Adams (786-7180).

**Background:** The Washington Uniform Partnership Act (WUPA), originally adopted in 1945, provides rules and guidelines for a business organized as a partnership or a limited liability partnership. WUPA is based on the Uniform Partnership Act (UPA) adopted in 1914 by the National Conference of Commissioners on Uniform State Laws (NCCUSL). The UPA has been adopted in every state except Louisiana.

In 1994, the NCCUSL adopted a Revised Uniform Partnership Act (RUPA) and recommended it for adoption in all states. In 1996, the NCCUSL adopted amendments to RUPA relating to limited liability partnerships and recommended adoption of these further amendments in all states. The Partnership Law Committee of the Washington State Bar Association reviewed the Revised Uniform Partnership Act and recommends its adoption, with changes, in Washington.

A partnership, also referred to as a general partnership, is created whenever two or more persons create an association to carry on business and share in profits and ownership control. No legal documentation is required to form a partnership, and the partnership

dissolves upon the death, bankruptcy, or withdrawal of any partner, unless otherwise agreed. Each partner is an agent of all others and can bind the partnership. Ordinary partnership matters are decided by a majority vote of the partners. Partners cannot transfer their interests in the partnership unless all other partners agree. Each partner has unlimited personal liability for the debts and obligations of the partnership.

In 1995, the Legislature adopted the Limited Liability Partnership Act. A limited liability partnership is formed by filing an application with the Secretary of State and paying a \$175 application fee. Limited liability partnerships are governed by many of the same rules and guidelines that apply to partnerships, with several differences. A partner in a limited liability partnership is not liable for debts, obligations, and liabilities of the partnership arising from tortuous conduct committed in the course of the partnership business by another partner or an employee of the partnership. A limited liability partnership that provides professional services must maintain professional liability insurance. Foreign limited liability partnerships organized under the laws of another jurisdiction may do business in this state and are required to register with the Secretary of State. Foreign limited liability partnerships are governed by the laws of the state under which they are formed.

**Summary of Substitute Bill:** The Washington Uniform Partnership Act is repealed and replaced with the Revised Uniform Partnership Act (RUPA) with modifications proposed by the Partnership Law Committee of the Washington Bar Association. The RUPA makes the following significant changes to partnership law: (1) a partnership is treated as a legal entity with the ability to convert into or merge with other entities; (2) a partnership for a specific purpose or term will not automatically dissolve when a partner leaves the partnership; (3) partners are not strict fiduciaries for each other and may pursue their own interests, subject to their duties of loyalty and care; (4) partnerships may merge with other partnerships, limited partnerships, corporations, and limited liability companies, and a provision for dissenters' rights in mergers is provided; (5) partnerships may execute and file statements of authority to help partnerships transfer property and accomplish other partnership business; and (6) the limitation on the personal liability of a partner in a limited liability partnership is extended to include any obligation of the partnership.

GENERAL PROVISIONS: The Revised Uniform Partnership Act provides default rules for the relations among partners and between partners and the partnership, which may be varied or restricted by the partnership agreement. There are several limitations on the ability of a partnership agreement to vary or restrict certain relations, including limitations on the ability to eliminate a partner's duty of loyalty, duty of care, or obligation of good faith and fair dealing.

The law of the jurisdiction where a partnership has its chief executive office governs the partnership, except that Washington law governs relations among partners and the partnership and the liability of partners for an obligation of a limited liability partnership.

NATURE AND FORMATION OF PARTNERSHIP: A partnership is considered a legal entity distinct from its partners, rather than an aggregate of individuals, enabling it to sue and be sued in its own name.

Property of a partnership is owned by the partnership, rather than by the partners individually. Rules that determine when a partnership acquires property and the circumstances under which property is considered partnership property are expanded and clarified.

RELATIONS OF PARTNERS: Various provisions relating to the relations of partners to other persons, to other partners, and to the partnership are clarified and changed.

A partner's fiduciary duties to the partnership and other partners consist of the duty of loyalty and the duty of care. In addition, a partner has an obligation of good faith and fair dealing in discharging the duties to the partnership and exercising any rights under the partnership agreement. The partnership agreement may not unreasonably reduce the duty of care or eliminate the duty of loyalty, but may specify types of activities that do not violate the duty of loyalty if it is not manifestly unreasonable to do so. The partnership agreement may not eliminate the obligation of good faith and fair dealing, but may set the standards by which the obligation is to be measured, if the standards are not manifestly unreasonable.

A statement of partnership authority is created that provides a mechanism for a partnership to designate the authority of a partner to transfer real property or to enter into other transactions on behalf of the partnership. A statement of authority filed with the Secretary of State imparts constructive notice to third parties of the authority or lack of authority of a partner to transfer a partnership's real property.

A statement of denial is created that provides a mechanism for a partner or a person named as a partner to file a denial of the person's authority or status as a partner. The statement of denial must be filed in the office of the Secretary of State.

Provisions concerning the transfer of property are amended to apply to personal property as well as real property. A mechanism is provided for a sole surviving partner to execute and file documents in the name of the partnership to transfer property.

Provisions concerning the liability of a partnership and partners are modified to provide that a partner is jointly and severally liable for all partnership obligations and all actionable conduct of another partner that obligates the partnership, unless otherwise agreed. In an action against a partnership and the partners, a creditor who receives a judgment must first enforce the judgement against the partnership, and then against the partners' individual assets, with some exceptions. In addition, liability rules are changed to allow a partner to sue a partnership that has committed a tort that harms the partner

and to clarify that the partnership is liable for property of a third party that is improperly taken by a partner but not actually received by the partnership.

DISSOCIATION AND DISSOLUTION: Various provisions relating to dissociation of a partner and dissolution of the partnership are amended.

Dissociation of a partner does not automatically cause dissolution and liquidation of the partnership. A partnership that continues in business after the dissociation of a partner is legally the same business that existed prior to the dissociation. The list of events of dissociation and the circumstances under which a dissociation is wrongful are modified.

When a partnership elects to continue the business after an event of dissociation, the partnership must buy out the dissociated partner's interest in the partnership according to a buyout price based on a calculation specified in statute. The good will value of the partnership may be considered in determining the value of a wrongfully dissociated partner's interest. A process is provided for determining the value of a dissociated partner's interest when the partner and the partnership can not agree on a buyout price.

The apparent authority of a dissociated partner to bind the partnership is limited to a maximum of two years following dissociation and may be terminated prior to two years by actual notice or 90 days after filing a notice of dissociation with the Secretary of State.

The list of events that may result in the dissolution and winding up of a partnership are amended to provide an opportunity for a partnership to cure an event causing dissolution, to allow a majority of partners to agree to continue a partnership that is dissolved under certain circumstances, and to allow a retroactive revocation of the dissolution by agreement of all the partners other than a wrongfully dissociating partner.

A partnership is bound by an act of a partner after dissolution that is appropriate for winding up the partnership or, if the other party did not have notice of the dissolution, for an act that would have bound the partnership prior to dissolution. A partner who is liquidating the partnership is authorized to engage in certain activities not ordinarily incident to winding up to preserve the business as a going concern or for other specified reasons.

Changes are made in the rules relating to settling of accounts in the liquidation process, including a provision that partners who are creditors are treated the same as other creditors, to the extent permitted by law, rather than placing partner creditors behind other creditors.

CONVERSIONS AND MERGERS: A partnership may convert into a limited partnership upon approval of all partners, or upon approval of fewer than all partners if authorized in the partnership agreement. A limited partnership may convert into a

partnership upon the approval of all partners. A partnership or limited partnership that is converted remains for all purposes the same entity that existed prior to conversion. Rules are provided setting forth a partner's liability after conversion.

A partnership may merge with one or more partnerships, limited partnerships, limited liability companies, or corporations pursuant to a merger plan. The plan must set forth the names of all merging companies and the surviving company, terms and conditions of the merger, and the manner and basis of converting the interests. Approval of the merger plan requires the approval of all the partners. If a limited partnership, limited liability company, or corporation is a party to the merger, the plan of merger must be approved in accordance with merger laws governing those entities. Details concerning the filing and effects of merger are provided. Merger of foreign and domestic partnerships, limited partnerships, limited liability companies, and corporations is allowed.

A partner may dissent from a merger plan and obtain payment of the fair market value of the partner's interest in the partnership. A dissenter may not challenge a merger unless the merger fails to comply with the procedural requirements imposed by law, or with the partnership agreement, or is fraudulent with respect to the partner or partnership. Detailed rules concerning notice requirements and payment demands are provided.

LIMITED LIABILITY PARTNERSHIPS: Various changes are made to the requirements relating to limited liability partnerships and foreign limited liability partnerships.

The limitation on the personal liability of a partner in a limited liability partnership is extended. A partner in a limited liability partnership is not personally liable for any obligation of the partnership, whether arising in contract, tort, or otherwise. The rules relating to rights and duties of partners and obligations and procedures relating to dissociation and dissolution of a partnership apply to limited liability partnerships.

The failure of a foreign limited liability partnership to register with the Secretary of State does not affect the validity of a contract entered into in this state or, by itself, waive the limitation of personal liability of a partner of the foreign limited liability partnership. The Secretary of State is designated the agent for service of process for a foreign limited liability company that transacts business in Washington without registering. Specific activities are listed that are not considered transacting business in the state, such as maintaining or defending an action, holding meetings of partners or carrying on internal affairs activities, or maintaining bank accounts. The Attorney General may maintain an action to restrain a foreign limited liability partnership from transacting business in the state in violation of the law.

**MISCELLANEOUS:** The Secretary of State is authorized to adopt rules to implement the act and must adopt rules establishing fees for filing of statements and for the provision of copies, certified copies, certificates, and other services.

Various provisions of the Business Corporations Act, the Limited Partnership Act, and the Limited Liability Company Act are amended to authorize the merger of these entities with a domestic partnership or with any of the other entities.

The RUPA will apply to all partnerships effective January 1, 1999. Before January 1, 1999, the RUPA applies to any entity formed after the effective date of the act or any entity formed before the effective date of the act that elects to be governed by the act.

**Substitute Bill Compared to Original Bill:** The substitute bill makes various technical amendments to the merger provisions of the Business Corporations Act and the Limited Partnership Act to include references to limited liability companies and partnerships, and to correct an incorrect reference.

**Appropriation:** None.

**Fiscal Note:** Not requested.

**Effective Date of Substitute Bill:** Ninety days after adjournment of session in which bill is passed, except Section 1308, which takes effect January 1, 1999.

**Testimony For:** This bill revises the Uniform Partnership Act, which is a 70-year-old statute. The revisions conform partnership law to modern practice and to the expectations of reasonable people who enter into partnership arrangements concerning what rules should apply. The revisions contain some new, modernizing concepts that treat partnerships as legal entities, allowing them to merge with other legal entities, such as corporations, limited liability companies, and limited partnerships.

**Testimony Against:** None.

**Testified:** Bruce Benson and Brian Todd, Washington State Bar Association (pro).