Choice of Entity – General Considerations

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Advanced Partnerships, LLCs And LLPs: *Organization And Operation In California*[1]

I. Choice of Entity – General Considerations

A. Background

When an individual or group of individuals decide to create a business, one important decision that must be made is to select the form of the business entity. For the most part, the potential business owner or owners will chose between one of five entities: sole proprietorship, general partnership, corporation, limited liability company, and limited liability partnership. Each entity has its own advantages and disadvantages and this section is designed to provide basic information about each entity.

B. Sole Proprietorship

A sole proprietorship is the simplest manner in which to organize a business. Any person that wishes to start a business without co-owners and without forming a legal entity is a sole proprietor. A sole proprietorship is not itself a legal entity, rather it is a term that refers to a natural person who directly owns a company and is directly responsible for its debts.

The advantages of establishing a sole proprietorship include the complete control and the ease of formation. The sole proprietor may act through agents or employees. To establish a sole proprietorship, the prospective business owner does not need to file any documents with any government agency. The sole proprietorship must still meet certain legal requirements, including licensing, permits, and insurance.

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[1] Prepared with the assistance of Brian Hom, law clerk, Thelen Reid & Priest LLP. This article is intended to provide general guidelines for practice in California by California business entities. Individual cases may vary and business owners should consult their own counsel for specific advice.

A primary disadvantages of a sole proprietorship is that the sole proprietor is liable for all acts of the business and does not benefit from a liability shield. The business owner faces unlimited personal liability for all business losses and liabilities. Moreover, if the owner is married, the couple's community property is also placed at risk. Furthermore, the sole proprietor is subject to liability for injuries caused by the negligence of employees or agents.

A sole proprietorship is the simplest of all business forms and is often chosen because, for the business owners, the simplicity and lack of expense information.

C. General Partnership

A general partnership is the default business entity that exists when the business owners jointly engage in business for profit do not overtly select a form. Joint business owners may be deemed general partners, even if they have no specific intent to be "general partners" or have agreed how profits and losses will be shared. No special formalities are required to form a general partnership. The partnership agreement does not necessarily have to be written to be enforceable.

The advantages of a general partnership include the ability to act as a separate legal entity. The general partnership can hold and convey legal title to real property in its own name, it can sue and be sued in the partnership name, and it continues in existence notwithstanding the "dissociation" of one or more partners. The distribution of profits and losses of the general partnership are determined by the partnership agreement and may be allocated disproportionately. Without a formal agreement, the profits are shared equally. Also, each general partner is a co-owner of the general partnership and has equal right to participate in the management and control of the business. As a default, disagreements as to matters that arise during the ordinary course of business are decided

by a majority of partners and extraordinary matters and amendments to the partnership agreement must have unanimous consent of the partners.

The disadvantages of a general partnership include unlimited personal liability for losses. As long as a general partner was engaged in behavior that occurred during the ordinary course of the partnership business, that partner is deemed to be an agent for the general partnership. As a result, all other general partners will be bound by a single partner's business decisions. Each general partner is joint and severally liable for the partnership's business obligations, despite how the general partnership agreement may have allocated losses. Additionally, each partner may be held jointly and severally liable for tortious acts committed by a co-partner during the ordinary course of partnership business, including misapplication of another's money or property. Finally, a court can change a general partnership's composition by ordering an individual general partner to sell her share to a third party to satisfy a judgment, as long as the sale will not unduly interfere with the business.

D. Corporation

A corporation is a separate legal entity that is created and exists under specific authority granted by state law. It has its own identity, separate and apart from the persons who created it and from its shareholders.

A major advantage of selecting a corporation is for its shield against personal liability. As long as all the requirements for forming and operating a corporation are met and maintained, shareholders will generally be able to manage and control the day-to-day operation of a corporation without losing their liability protection. Additionally, shareholders are not personally liable for the acts of the corporation simply by reason of their equity ownership in the corporation.

The liability shield can be lost if the corporation is the "alter-ego" of its shareholders, or a "mere corporate shell." A court may allow a third-party claimant to "pierce the corporate veil" to satisfy claims from the shareholders' personal assets. It has been held that an individual shareholder may be liable under these circumstances where the corporation is not "only influenced and governed by that person, but that there is such a unity of interest and ownership that the individuality, or separateness, of such person and corporation has ceased, and that the facts are such that an adherence to the fiction of the separate existence of the corporation would, under the particular circumstances, sanction a fraud or promote injustice." (*Talbot v. Fresno-Pacific Corp.* 181 Cal. App. 2d 425 (1960) 431.)

The case of *Associated Vendors, Inc. v. Oakland Meat Company, Inc., et al.* (1962) 210 Cal.App.2d 825 provides the following list of factors California courts have considered in piercing the corporate veil: (1) commingling of funds; (2) the treatment by an individual of the assets of the corporation as his own; (3) the failure to obtain authority to issue stock; (4) the holding out by an individual that he is personally liable for the debts of the corporation; (5) the failure to maintain minutes of adequate corporate records; (6) the identical equitable ownership in the two entities; (7) the use of the same office or business location; (8) the failure to adequately capitalize a corporation; (9) the use of a corporation as a mere instrumentality for the business of an individual; (10) the concealment and misrepresentation of the identity of the responsible ownership, management, and financial interest or concealment of personal business activities; (11) the disregard of legal formalities; (12) the use of the corporate entity to procure labor, services, or merchandise for another person or entity; (13) the diversion of assets from a

corporation by or to a stockholder, to the detriment of creditors; (14) the contracting with another with intent to avoid performance by use of a corporate entity as a shield against personal liability; (15) the formation and use of a corporation to transfer to it the existing liability of another person.

1. C-Corporations

A "C-Corp" is the default type of corporation. It is named and governed by sub-chapter C of the Internal Revenue Code. The C-corp is subject to double-taxation, since taxes are collected from a corporation's profits and again from shareholders when those profits are distributed as dividends. A corporation can sometimes avoid double taxation through salary payments to employees, provided the amounts are reasonable, because salaries are a deductible expense of the corporation.

2. S-Corporations

An "S-corp" is a corporation named and governed by sub-chapter S of the Internal Revenue Code. Unlike a C-corp, an S-corp is taxed as a partnership and is only subject to one level of taxation. Additionally, like a partnership, the S-corp will not file separate tax returns, rather; the profits and losses by the S-corp will be counted on the individual shareholder's income returns. S-corps are also not subject to the additional annual franchise tax of limited liability companies formed in California. In exchange for the generous tax treatment, S-corps are subject to strict regulations, including: (1) an S-corp is formed when a corporation elects S-corp status by filing with the IRS; (2) an S-corp may have no more than 75 shareholders; (3) S-corp shareholders may only be U.S. citizens or residents, or certain 'electing small business' trusts; and (4) an S-corp may only have one class of stock.

3. Close Corporations

In California the words "close corporation" or "statutory close corporation" are terms of art, referring to a specific type of organization available to some closely held corporations. Ordinarily, close corporations are also S-corps, but the two terms should not be used interchangeably. An S-corp is an entity recognized under the IRS code, while close corporations are recognized under state law. The law allows close corporations to adopt special rules to modify the "default" provision of the Code, such as division of profits, allocation of control over corporate affairs, and corporate procedural formalities. In effect, the shareholders may enjoy much of the flexibility of a partnership with the limited liability of a corporation. In addition to the standard requirements for incorporation, a close corporation must: (1) have a written agreement among all shareholders setting forth the matters upon which the shareholders will exercise control; (2) have no more than 35 shareholders; (3) the articles of incorporation must contain: (i) a provision that all of the corporation's issued shares of all classes shall be held of record by not more than a certain number (not to exceed 35); and (ii) the statement, "This corporation is a close corporation."

E. Limited Partnership

Limited partnerships are permitted by statute in California pursuant to the California Revised Limited Partnership Act (Cal. Corp. Code, §§ 15611-15723) which applies to limited partnerships formed on or after July 2, 1984 or limited partnerships that elect to be governed by the Act. Generally limited partnerships consist of one or more general partners who manage the business and are subject to personal liability for partnership obligations and one or more limited who typical contribute capital for a share of the profit. Absent extraordinary circumstances, each limited partner's liability is

limited to that individual's capital contribution. The general partner as an agent of the partnership may be the partnership to obligations to third parties. The limited partners as investors have various rights to records and information, (but participation in management, may expose a "limited partner" to a general partners liability. A limited partnership may be organized with a corporation as the general partner to further limited liability since under most circumstances the shareholders of a corporation are not personally liable for corporate obligations.

F. Limited Liability Partnership

Limited Liability Partnership (LLP) can be thought of as a general partnership with the added feature of a corporate-style limited liability shield for its partners or a limited liability company (LLC) for those entities statutorily prohibited from being organized as an LLC. By registering as an LLP, the general partners can limit their liability for the partnership's obligations and debts with only certain limited exception.

A LLP is a relatively recent creation that offers the benefit of limited liability for partners in law, accounting, and architectural firms organized as general partners. In California, the LLP is only available to partnerships engaged in the practice of law, public accountancy, or architecture and those providing services or facilities related or complementary to those provided by such firms. Additionally, the partnership must be registered with the state and provide liability insurance, collateral, or have a specified net worth to be allowed limited liability status.

G. Overview of Limited Liability Company

A limited liability company (LLC) is a unique business entity that offers the benefits of a partnership and corporation without the regulation or rigidity of a limited

partnership and S-corps. An LLC is a hybrid entity that combines the pass-through tax treatment of a partnership with the general limited liability protections of a corporation.

An LLC is a separate legal entity, capable of suing and being sued, and has the rights, obligations, powers, and privileges accorded by the California Corporations Code. It only takes one person to establish an LLC and owner or owners of an LLC are referred to as "members." Members may manage the LLC themselves or elect a manager or managers to operate the business. The organization and operation of an LLC can be similar to a sole proprietorship, a corporation, a general partnership or a limited partnership.

A California LLC may not engage in businesses required to be licensed, certified, or registered under the Business and Professions Code. An LLC comes into existence with the filing of appropriate Articles of Organization with the Secretary of State unless expressly authorized by statute (Corp. Code § 17375. (Insurance Code §§ 1647 and 1647.5 permit insurance agents and brokers to conduct businesses as LLC subject to certain requirements).

To complete the formation process of an LLC, the members must enter into an Operating Agreement. The Operating Agreement is simply an agreement between the members of the LLC to organize a limited liability company. The operating agreement can be simple and can be an oral agreement. The operating agreement can serve as a vehicle for restricting or enlarging the rights of the members regarding the management and control of the LLC. Limitations of LLC members' rights regarding transferability of interests should be outlined in the operating agreement such as whether transferring of interests require member's or manger's approval. While it is not required, it serves as a

precautionary measure to ensure that later disputes can be resolved efficiently and with certainty.

H. General Considerations Indicating Suitability of LLCs

Generally an LLC is selected as the business entity when potential business owners desire the flexibility of a partnership and the liability shield of a corporation, but do not want certain burdens associated with each. An LLC presents a compromise between all the business entities. Members of an LLC may chose to have the entity taxed as a corporation or as a pass-through entity (like a partnership) that avoids double taxation. Unlike other entities that avoid double taxation and limit liability such as limited partnerships and S-corporation, LLCs do not have the burdensome restriction of either of those entities. Also, each member may be involved in the day-to-day operations and still enjoy limited liability and there is no limit on the number or type of members.

To add to an LLC's flexibility, there are two basic methods to control an LLC, either the members of the LLC can run the daily operations of the entity or they may hire a manager or mangers to run operate the entity.

1. Member Managed

In a member-managed LLC, all members have a right to manage and control the company subject to any limitations or grants in the Article of Organization or the Operating Agreement. The members are also subject to the same duties and obligations as any manager.

2. Manager Managed

For a limited liability company to be managed by managers, the Articles of Organization must have stated that the LLC is to be managed by one or more managers. The Articles, however, do not have to state the names of the managers, only that the LLC

will be managed by managers as opposed to members. Managers may be corporations or other companies, and do not need to be a natural person or members of the LLC. The number of managers does not need to be stated in the Articles of Organization, though it may.

I. Advantages Of Using An LLC

The chief advantage of selecting an LLC is that members are typically protected by a liability shield. Ordinarily, only the limited liability company can be held responsible for the entity's debts. Except for a few narrow exceptions, LLC members are not personally liable for the debts or obligations of the entity and enjoy same limited liability as corporate shareholders. The LLC members may face personal liability under the guarantor liability and "alter ego" liability theories. Under guarantor liability, the LLC members will be personally liable for the entity's obligations if they personally guaranteed the obligation. Additionally, under "alter ego" liability, a member may be found liable for an LLC's obligations under the common law "alter ego" doctrine. A difference in LLC "alter ego" analysis and standard analysis is that for an LLC, failure to hold or observe formalities pertaining to calling or conducting of meetings is not a factor tending to establish that a member or members have alter ego or personal liability for any debt, obligation, or liability of the LLC where if the Articles of Organization or Operating Agreement do not expressly require the holding of meetings of members or managers. This "exception" to corporate style alter ego analysis does not apply to liability for the member's participation in tortious conduct or pursuant to a written guaranty or other contractual obligation entered into by the member, other than an Operating Agreement (Cal. Corp. Code § 17101).

CHOICE OF ENTITY CONSIDERATIONS

Topic	C Corporation	S Corporation	Limited Liability Company	Limited Partnership	General Partnership
Ease or Difficulty of Formation; Transaction Costs	In California, Articles of Incorporation must be filed with the Secretary of State Statement of Domestic Stock Corporation must be filed with the Secretary of State within 90 days after filing the Articles. The parties need not negotiate a detailed agreement governing the structure and operation of the corporation, but can instead, rely on the General Corporation Law. However, if the parties desire to restrict the transferability or	In California, Articles of Incorporation must be filed with the Secretary of State Statement of Domestic Stock Corporation must be filed with the Secretary of State within 90 days after filing the Articles. The parties need not negotiate a detailed agreement governing the structure and operation of the corporation, but can instead, rely on the General Corporation Law. However, if the parties desire to restrict the transferability or	In California, an LLC is formed by filing Articles of Organization (Form LCC-1) with the Secretary of State Within 90 days after filing the Articles, the LLC must file a Statement of Information with the Secretary of State. All members must enter into an Operating Agreement. Although oral agreements are permitted, the agreement should be in writing. The cost and complexity of the agreement will depend on the	In California, a limited partnership is formed by filing with the Secretary of State a Certificate of Limited Partnership (Form LP-1) executed by all the general partners. Although oral agreements are permitted, the Limited Partnership Agreement should be in writing. The cost and complexity of the Partnership Agreement will depend on the structure and business of the partnership. Drafting the Agreement may be more time-	In California, no filing fee is required to form the entity. Partners should, but need not, enter into a General Partnership Agreement. The cost and complexity of the Agreement depends on the structure and business of the partnership. Drafting the General Partnership Agreement may be more time-consuming and costly than drafting simple articles and bylaws for a corporation.

Topic	C Corporation	S Corporation	Limited Liability Company	Limited Partnership	General Partnership
	voting rights of stock, or provide for different classes of stock, a detailed agreement or specially-drafted Articles of Incorporation may be required. After formation, directors must be elected, officers appointed, Bylaws prepared and adopted, and shares of stock issued, all of which (plus other organizational matters) should be reflected in organizational minutes.	voting rights of stock, or provide for different classes of stock, a detailed agreement or specially-drafted Articles of Incorporation may be required. After formation, directors must be elected, officers appointed, Bylaws prepared and adopted, and shares of stock issued, all of which (plus other organizational matters) should be reflected in organizational minutes.	nature of the LLC and its business. Drafting the agreement may be more time-consuming and costly than drafting simple articles and bylaws for a corporation.	consuming and costly than drafting simple articles and bylaws for a corporation.	

Topic	C Corporation	S Corporation	Limited Liability Company	Limited Partnership	General Partnership
Agency Authority of Owners and Management	Officers are agents of the corporation. Neither shareholders nor directors have agency authority to bind the corporation.	Officers are agents of the corporation. Neither shareholders nor directors have agency authority to bind the corporation.	In a member-managed LLC, every member is an agent of the LLC, and the act of any member, for apparently carrying on in the usual way the business of the LLC, binds the LLC. In a manager-managed LLC, (1) every manager is an agent of the LLC, and the act of any manager, for apparently carrying on in the usual way the business of the LLC, binds the LLC, and (2) members are not agents of, and cannot bind, the LLC.	General partners are agents of the limited partnership. Limited partners do not have apparent agency authority to bind the partnership.	Each partner is an agent of the partnership. The act of any partner for apparently carrying on in the usual way the business of the partnership binds the partnership. The Partnership Agreement may restrict the authority of a particular partner to bind the partnership; however, a restriction on authority will not be effective against third parties who have no knowledge of the restriction.

Topic	C Corporation	S Corporation	Limited Liability Company	Limited Partnership	General Partnership
			The Articles of Organization or the Operating Agreement may limit the authority of members (in a member-managed LLC) or managers (in a manager-managed LLC) to bind the LLC. However, such limitations will not be effective against third parties without actual knowledge of the restrictions.		
Liability of Owners for Business Obligations	Shareholders are not liable for the obligations of a corporation. However, shareholders may be liable (1) to the extent they personally guaranty corporate debts; (2)	Shareholders are not liable for the obligations of a corporation. However, shareholders may be liable (1) to the extent they personally guaranty corporate debts; (2)	Members of an LLC are not liable for the obligations of the LLC. However, a member may be liable (1) to the extent he or she personally guaranteed debts of the LLC; (2) for the	The general partner is liable for partnership obligations to the same extent as partners of a general partnership. Limited partners are not liable for partnership	Partners are jointly and severally liable for the wrongful acts or omissions of any partner acting in the ordinary course of partnership business or with authority of the partners, and are

Topic	C Corporation	S Corporation	Limited Liability Company	Limited Partnership	General Partnership
	to the extent they receive improper distributions; (3) if a court "pierces the corporate veil" of a corporation to impose personal liability on the shareholders; or (4) if a controlling shareholder breaches a duty to the other shareholders or the corporation.	to the extent they receive improper distributions; (3) if a court "pierces the corporate veil" of a corporation to impose personal liability on the shareholders; or (4) if a controlling shareholder breaches a duty to the other shareholders or the corporation.	member's participation in tortious conduct; (3) with respect to distributions from an LLC made in violation of the LLC Act; and (4) if a court "pierces the company veil" of an LLC to impose personal liability on the member. The criteria used to determine whether to "pierce the LLC veil" are the same criteria used to determine whether to pierce the corporate veil, except that the failure to hold meetings of members or managers or to observe formalities	obligations and risk only the loss of their agreed capital contribution. Limited partners may become liable as general partners if they participate in the management of the partnership business.	jointly liable for all other obligations of the partnership.

Topic	C Corporation	S Corporation	Limited Liability Company	Limited Partnership	General Partnership
			pertaining to meetings will not be considered a factor if the LLC is not required to hold meetings of members of managers.		

Fiduciary Obligations, Minority Rights, And Personal Liability

Prepared and Presented by:

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Advanced Partnerships, LLCs And LLPs: ***Organization And Operation In California***[2]

II. Fiduciary Obligations, Minority Rights, and Personal Liability

A. Defacto Partnerships

The California Partnership Act, Corp. Code §§16100-16962, defines a partnership as an association of two or more "persons" to carry on as co-owners a business for profit. (Corp. Code § 16101(8)). A "person" includes individuals, partnerships, corporations, limited liability companies, and other associations. (Corp Code § 15002; *see also*, Corp. Code § 16101(11). The purpose of the partnership must be legal and involve no violation of public policy. Otherwise, subject to a few limited exceptions, a partnership may be formed to engage in any trade, occupation, or profession.

1. Determining the existence of a partnership

a. Intent of the Parties

Whether a particular association is a partnership depends on whether a community of interest arises between the parties, whether the business is undertaken as a common enterprise with a mutual right of control, and whether the business is operated for the parties' joint account with the right in the owner of each interest to share in the profits. *Greene v Brooks* (1965) 235 Cal.App.2d 161. Some cases indicate that whether a particular association is a partnership depends substantially on the intention or understanding of the parties involved. See, e.g., *Solomont v. Polk Development Co.* (1966) 245 Cal.App.2d 488). The intention of the parties need not be expressed, but may be implied. *Estate of Foreman* (1969) 269 Cal.App.2d 180. Additionally, there are

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specific rules that are identified at Corp. Code § 16202 to determine whether a partnership exists.

b. Statutory Authority

In addition to the California Partnership Act, there are many other California statutes which may be relevant to partnerships and relationships among partners include:

a) California Revised Limited Partnership Act (Corp. Code §§ 15611-15723);

b) Statutes relating to mining partnerships (Pub. Res. Code § 3940, et seq.);

c) Statute regarding competition agreements between partners (Bus. & Prof. Code § 16602);

d) Statutes pertaining to agency relationships generally (Civ. Code § 2295, et seq.);

e) Fictitious business name statute (Bus. & Prof. Code § 17900, et seq.);

f) Corporate Securities Law (Corp. Code § 25000, et seq.);

g) Uniform Fraudulent Transfer Act (Civ. Code § 3439, et seq.)

Partnerships are the default business entity that is created when two or more people enter into a business for profit when no other form is selected. The rules governing partnerships are very broad and encompassing. As a result, people outside the partnership may be construed to be part of the partnership, or defacto partners, if they become too involved in the partnership, such as managing daily operations or controlling the business. To be a partner, there need not be a specific intent, intent may be implied through actions, nor does there need to be a written agreement. If a person is deemed a defacto partner he or she will subject be subject to the same obligations and liabilities as any other general partner in the partnership.

B. Codification Of Fiduciary Duties

In the early 1990s, the National Conference of Commissioners of Uniform State Laws (NCCUSL) proposed the Revised Uniform Partnership Act (RUPA) for adoption by the states. RUPA was the first major effort to modernize and codify state partnership law as it had developed since the original Uniform Partnership Act was adopted in 1914. RUPA included a codification of partners' fiduciary duties, partly in reaction to case law. The final version of RUPA may be reviewed on the official NCCUSL website maintained in association with the University of Pennsylvania Law School: http://www.law.upenn.edu/bll/ulc/ulc_frame.htm.

The California state legislature enacted a version of RUPA in 1996 titled the California Uniform Partnership Act of 1994 ("California Partnership Act") (Corp. Code §§ 16100-16962). Initially, the new law governed partnerships formed on or after January 1, 1997 (unless the partnership was continuing the business of a dissolved partnership). As of January 1, 1999, the new law governs all California partnerships, including those formed before January 1, 1997, thus replacing the former Uniform Partnership Act in its entirety. See Corp. Code § 16111.

The State Bar committee that drafted the legislation believed that the codification of partner fiduciary duties did not materially depart from prior case law. See Senate Judiciary Committee Analysis of AB 583 (Aug. 23, 1996) (Drafters' Comments). The legislative history of AB 583 includes the following commentary on Corp. Code § 16404, the statutory section that sets forth the fiduciary duties of partners:

> This section, which is perhaps the most controversial, provides significant changes and additions to the statutory formulation. Due to the sparse statutory law governing fiduciary duties in [the California Uniform

> Partnership Act], the intricacies of fiduciary duty have mainly derived from common law. In comparing and contrasting common law with RUPA, it is difficult to say with certainty if RUPA will have any significant impact on existing law.
>
> The members of the RUPA Subcommittee reviewed a number of California cases that have dealt with the fiduciary duty of partners. Their goal was to determine whether any of the California cases dealing with fiduciary duty of partners would have been decided differently if Article 4 of RUPA had been applied. The subcommittee concluded that none of the California cases would have been decided differently; therefore the new fiduciary duty section makes no substantive change from prior law.

The California Partnership Act permits a careful drafter to define and restrict, although not to eliminate, the fiduciary duties of partners. See Corp. Code § 16103. It also limits the broad implications of prior case law that classified partners as "trustees." For example, unlike a true trustee, a partner under the Partnership Act does not violate his or her fiduciary duty "merely because the partner's conduct furthers the partner's own interest." Corp. Code § 16404(e).

The California Partnership Act also added some certainty to case law by:

- Specifying certain duties as fiduciary duties (see Corp. Code § 16404(b));
- Identifying the obligation of good faith (see Corp. Code § 16404(d); and
- Allowing limited waivers of fiduciary duties (see Corp. Code § 16103).

Fiduciary duties of partners are codified in Corp. Code § 16404 as follows:

> (a) The fiduciary duties a partner owes to the partnership and the other partners are the duty of loyalty and the duty of care set forth in subdivision (b) and (c).
>
> (b) A partner's duty of loyalty to the partnership and the other partners include all of the following:
>
> (1) To account to the partnership and hold as trustee for it any property, profit, or benefit derived by the partner in the conduct and winding up of the partnership business

> or derived from a use by the partner of partnership property or information, including 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 party having an interest adverse to the partnership.
>
> (3) To refrain from competing with the partnership in the conduct of the partnership business before the dissolution of the partnership.
>
> (c) A partner's duty of care to the partnership and the other partners in the conduct and winding up of the partnership business is limited to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law.
>
> (d) A partner shall discharge the duties to the partnership and the other partners under this chapter or under the partnership agreement and exercise any rights consistently with the obligation of good faith and fair dealing.
>
> (e) A partner does not violate a duty or obligation under this chapter or under the partnership agreement merely because the partner's conduct furthers the partner's own interest.
>
> (f) A partner may lend money to and transact other business with the partnership, and as to each loan or transaction, the rights and obligations of the partner regarding performance or enforcement are the same as those of person who is not a partner, subject to other applicable law.
>
> (g) This section applies to a person winding up the partnership business as the personal or legal representative of the last surviving partner as if the person were a partner.

C. Obligation Of Good Faith And Fair Dealing

In addition to fiduciary duties, the California Partnership Act provides that a partner has an obligation of good faith and fair dealing in the discharge of his or her duties – as well as in the exercise of any rights – under the statute and under the partnership agreement. Corp. Code § 16404(d).

The obligation of good faith and fair dealing is theoretically based on the partners' mutual agreement to form the partnership. Prior cases held that the relationship among partners is of a fiduciary nature that imposes on them a duty of good faith and fair dealing and requires that no partner may take unfair advantage of another partner. See, *e.g., Wyler v. Feuer* (1978) 85 Cal.App.3d 392; *Page v. Page* (1961) 55 Cal.2d 192, 10; *Prince v. Harting* (1960) 177 Cal.App.2d.

The drafters of both RUPA and the California Partnership Act did not define the obligation of good faith and fair dealing. Left without a statutory definition, "good faith and fair dealing" is sufficiently flexible to allow one to argue that it includes many perceived unfair practices.

There is no California case law directly explaining the meaning of "good faith and fair dealing" as used in the California Partnership Act. Accordingly, the best guidance is prior case law. The leading case in California is *Page v. Page* (1961) 55 Cal.2d 192. In that case, one of two partners in a linen supply business sued for a declaration that the partnership was a partnership at will. The evidence showed that the partners had entered into an oral agreement without discussing a fixed term. Each partner had contributed $43,000 over the years. The partnership became profitable when an air force base was established nearby. The plaintiff operated the partnership's business and was its major creditor. As such, he was in a unique position to take over profitable business opportunities on the partnership's dissolution. The California Supreme Court held, among other things, there was no showing of bad faith. Despite this, the Court held that the plaintiff owed the defendant fiduciary duties and that the plaintiff could be liable in a

further action if the plaintiff excluded the defendant from a future partnership business opportunity.

California courts have relied on *Page* for the proposition that partners must deal with each other in good faith. See, *e.g., Leff v. Gunter* (1983) 33 Cal.3d 508; *Crouse v. Brobeck, Phleger & Harrison* (1998) 67 Cal.App.4th 1509; *Rosenfield, Meyer & Susman v. Cohen* (1983) 146 Cal.App.3d 200, 194 CR 180. *Page*, however, is arguably distinguishable because in *Page*, the Court specifically relied on the concept of partners as "trustees."

1. Partners Acting in Their Own Self-interest

What is *not* included in the obligation of good faith and fair dealing may be clearer than what *is* included. A partner does not violate his or her obligation under the statue merely because his or her conduct furthers his or her own interests. Corp. Code § 16404(e). Likewise, a partner may lend money and transact other business with the partnership, and should be treated like any other creditor. See Corp. Code § 16404(f).

2. Limiting Fiduciary Duties and the Obligation of Good faith

While partners in a California partnership cannot waive or eliminate entirely the duties of loyalty or care or the obligation of good faith, the partnership agreement may set forth the scope and standards by which fiduciary duties are to be measured. Corp. Code § 16103(b) provides in part:

> (b) The partnership agreement may not do any of the following:
>
> . . .
>
> (3) eliminate the duty of loyalty under subdivision (b) of Section 16404 or paragraph (3) of subdivision (b) of Section 16603, but, if not manifestly unreasonable, may do either of the following:

(A) The partnership agreement may identify specific types of categories of activities that do not violate the duty of loyalty.

(B) Unreasonably reduce the duty of care under subdivision (c) of Section 16404 or paragraph (3) of subdivision (b) of Section 16603.

(4) Unreasonably reduce the duty of care under subdivision (c) of Section 16404, but the partnership agreement may prescribe the standards by which the performance of the obligation is to be measured, if the standards are not manifestly unreasonable.

(5) Eliminate the obligation of good faith and fair dealing under subdivision (d) of Section 16404, but the partnership agreement may prescribe the standards by which the performance of the obligation is to be measured, if the standards are not manifestly unreasonable.

The language of Corp. Code § 16103 parallels the language of RUPA section 103 to the extent that it allows the partners to limit contractually the fiduciary duties and the obligation of good faith, unless the limitation is "manifestly unreasonable" (as to the duty of loyalty and the obligation of good faith) or "unreasonable" (as to the duty of care).

The RUPA drafters, whose guidance the California drafters followed on the waiver limitations, recognized that broad waivers of all fiduciary duties among partners would be contrary to much of the pre-RUPA case law. The Comments to RUPA section 103 explained:

> There has always been a tension regarding the extent to which a partner's fiduciary duty of loyalty can be varied by agreement, as contrasted with the other partners' consent to a particular and known breach of duty. On the one hand, courts have been loathe to enforce agreements broadly "waiving" in advance a partner's fiduciary duty of loyalty, especially where there is unequal bargaining power, information, or sophistication. For this reason, a very broad provision in a partnership agreement in effect negating any duty of loyalty, such as a provision giving a managing partner complete discretion to manage the

> business with no liability except for acts and omissions that constitute willful misconduct, will not likely be enforced.

Consistent with this admonition, Corp. Code § 16103 limits waivers of the duty of loyalty to those which are not "manifestly unreasonable." Moreover, consent must be unanimous unless the agreement provides otherwise. Corp. Code § 16103(b)(3); Selecting and Forming Business Entities section 6.10 (Cal CEB 1996).

Notably, Corp. Code § 16103 does not prohibit waiver of any other potential fiduciary duties. Accordingly, if a practitioner is concerned about the possible expansion of fiduciary duties under California law, Corp. Code § 16103 would not prevent the partners from agreeing to waive any such additional duties.

Like the duties of loyalty and care, the obligation of good faith and fair dealing is not waivable. Corporations Code § 16103(b)(5) provides that a partnership agreement may not:

> Eliminate the obligation of good faith and fair dealing under subdivision (d) of Section 16404, but the partnership agreement may prescribe the standards by which the performance of the obligation is to be measured, if the standards are not manifestly unreasonable.

Section 16103(b)(5) is derived from RUPA section 103(b); accordingly, the RUPA drafters' comments provide guidance on the interpretation that courts may give to the statute. The RUPA drafters noted that:

> Subsection (b)(5) authorizes the partners to determine the standard by which the performance of the obligation of good faith and fair dealing is to be measured. The language of subsection (b)(5) is based on UCC Section 1-102(3). The partners can negotiate and draft specific contract provisions tailored to their particular needs (*e.g,* five days notice of partners' meeting is adequate notice), but blanket waivers of the obligation are unenforceable.

By permitting a partial waiver of fiduciary duties and the obligation of good faith, the California Partnership Act follows the guiding principle of RUPA that allows partners to modify most of their obligations to each other by agreement. Both the California Partnership Act and RUPA appear to reflect a fundamentally "contractarian" approach to fiduciary duties. The contractarian view of partnership relations basically holds that partnership relations are in the nature of contract, under which partners are free to serve their respective self-interests, unless they specially agree otherwise. Contractarians believe that the function of statues such as RUPA in defining obligations of the parties should be limited to default rules for parties who have not prepared highly customized agreements. The alternative view, sometime referred to as the "fiduciarian" view, focuses on the parties' status rather than their contract. It regards partnerships as essentially collective in nature, and take the position that as a fiduciary, a partner can subordinate the collective interest of the partnership entity to his or her own interest only with contemporaneous notice and informed consent of the other partners.

D. California Revised Limited Partnership Act

Under the California Revised Limited Partnership Act (Corp. Code § 15611 et seq.) a general partner has the same rights and powers and is subject to the same restrictions and liabilities as a partner in a general partnership. Additionally limited partnerships are governed in the same manner as general partnerships under the California Partnership Act of 1994.

The California Partnership Act, like RUPA, specifies only two fiduciary duties: a duty of loyalty and a duty of care to the partnership and to the other partners.

1. Duty of Loyalty

The duty of loyalty has three components: (1) the duty to account; (2) the duty to refrain from self-dealing; and (3) the duty not to compete.

a. Duty to Account

Pursuant to the duty to account, a partner in a California partnership owes a duty to account to the partnership and hold as trustee for it any property, profit, or benefit derived by the partner in the conduct and winding up of partnership business or derived from the partner's use of partnership property or information, including the appropriation of a partnership opportunity. Corp. Code § 16404(b)(1). Thus, the partnership may recover from a partner any money or property that can be traced back to the partnership. This represents a codification of existing law that a partner may not appropriate benefits from the partnership without the other partners' consent and may not usurp a partnership opportunity. See *Fraser v Boguki* (1998) 203 Cal.App.3d 604 (overruled on separate grounds); *Ferry v McNeil* (1963) 214 Cal.App.2d 411.

The drafters of RUPA whom California legislators followed in this regard, intended that the duty to account would continue the general rule that partnership property usurped by a partner, including the misappropriation of a partnership opportunity, is held in trust for the partnership. The RUPA drafters explained that (Comment to RUPA section 404):

> Under a constructive trust theory, the partnership can recover any money or property in the partner's hands that can be traced to the partnership. *See, e.g., Yoder v. Hooper,* 695 P.2d 1182 (Colo. App. 1984), *aff'd.* 737 P.2d 852 (Colo. 1987); *Fortugno v. Hudson Manure Co.,* 51 N.J. Super 482, 114 A.2d 207 (1958); *Harestad v. Weitzel,* 242 Or. 199, 536 P.2d 522 (1975). As a result, the partnership's claim is greater than that of an ordinary creditor.

The duty to account is time-limited. A partner need only account for property, profit, or benefit with respect to the time that the partner engaged in the conduct of partnership business or winding up the partnership. When a partner disassociates from the partnership he or she need only account for the personal profits derived from matters arising, or events occurring, *before* the disassociation, unless the partner participates in winding up the partnership. Corp. Code § 16404(b). Once the partner has fully withdrawn, he or she is thereafter free to appropriate any business opportunity regardless of whether the partnership continues in existence. The duty to account does not include the time period before formation.

b. Duty to Refrain From Self-Dealing

The second part element of the duty of loyalty states that a partner owes a duty to the partnership and other partners to refrain from self-dealing. Corp. Code § 16404(b)(2). The prohibition against self-dealing appears to be a codification of existing California law. See *Cagnolatti v. Guinn* (1983) 140 Cal.App.3d 42; *Prince v. Harting* (1960) 177 Cal.App.2d 720. The California drafters indicated that this was the legislative intent. See Drafters' Comments ("common law has long held that a partner may not usurp a partnership opportunity"). When considered together with Corp. Code § 16404(e), which states, "[a] partner does not violate a duty or obligation under this chapter or under the partnership agreement merely because the partner's conduct furthers the partner's own interest," an argument can be made, however, that the law after codification may be different. See Vestal, *Fundamental Contractarian Error in the Revised Uniform California Partnership Act of 1992*, 73 Boston Univ. L. Rev. 523, 554-55 (1993).

A partner's hands are not completely tied by the ban on self-dealing. For example, a partner may lend money and transact other business with the partnership, and

to the extent that the partner does so, he or she is to be treated like any other creditor who is not a partner. Corp. Code § 16404(f). The duty is time limited in the same manner as the duty to account. See Corp. Code § 16404(b)(1), (2). Thus, after withdrawal, a partner is free to deal in a manner adverse to the partnership with respect to new matters and events. See Corp. Code § 16603.

c. Duty Not to Compete

Third, pursuant to the duty of loyalty, a partner also owes a duty not to compete with the partnership in the conduct of its business. Corp. Code § 16404(b)(3).

Unlike the other loyalty duties, the duty not to compete applies only to the "conduct" of partnership business, and does not extend to "winding up" the business. See Corp. Code § 16404(b)(3). Thus, unless the partnership agreement provides otherwise, a partner is free to compete immediately upon the partnership's dissolution.

Similarly the duty not to compete ends immediately upon the partner's disassociation from the partnership—even if the partnership continues to exist. Corp. Code § 16603(2). However, the disassociated partner cannot use confidential information after his or her disassociation and may also be restricted by laws governing trade secrets or an express confidentiality agreement.

Prior case law in California also recognized a partner's duty not to compete. See, *e.g., Olivet v. Frischling* (1980) 104 Cal.App.3d 831. The new statute, however, appears to have changed the time when that duty ends. Before adoption of the California Partnership Act, it had been held that a partner's duty not to compete survives his or her withdrawal from the partnership unless the parties agree otherwise. *Leff v. Gunter*, (1983) 33 Cal.3d 508.

In *Leff*, the California Supreme Court held that a partner's duty not to compete with the partnership with respect to a partnership opportunity which the partnership is actively pursuing survives the partner's withdrawal from the partnership. In that case, plaintiff and defendants had formed a joint venture in order to bid on a government project. After submitting their final bid, defendants advised plaintiff that they were withdrawing from the joint venture because they had become overextended on another project. Unbeknownst to plaintiff, however, defendants had already formed a different joint venture under which they submitted a separate bid for the same project less than a month after their withdrawal. The project was awarded to defendants because their bid was significantly lower than the bid proposed by the joint venture.

Plaintiff sued defendants for unfair competition and breach of fiduciary duty. Ruling for plaintiff, the California Supreme Court held that defendants breached their duty not to compete when they submitted the separate bid by the new joint venture. In so holding, the Court found "an obvious and essential unfairness in one partner's attempted exploitation of a partnership opportunity for his own personal benefit and to the resulting detriment of his copartners." 33 Cal.3d at 514. The Court also found that defendants could not relieve themselves of this duty simply by withdrawing from the joint venture. Noting that California law had long recognized a continuing fiduciary duty between former partners, the Court cited to the rule that "[a former partner] cannot make any profit to himself from a secret transaction *initiated* while the relation of trustee … exists, no matter when it springs into actual operation." 33 Cal.3d at 515, quoting *Donleavey v. Johnston* (1914) 24 Cal.App. 319, 328.

2. Duty of Care

The second fiduciary duty codified by the California Partnership Act is the duty of care. Under this duty, a partner must refrain from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of the law. Corp. Code § 16404(c). Although other states had recognized this duty prior to RUPA, California courts had not. See Drafters' Comments ("California courts do not recognize a duty of care, but the duty has been established by other state courts."). The duty of care may be analogized to a business judgment rule. The duty of care standards is a default position. The duty of care may not be unreasonably reduced by a partnership agreement, the agreement. Corp. Code § 16103(b)(4).

E. Limited Liabilities Companies Act

Limited liability companies ("LLCs") combine corporate and non-corporate elements.

To many practitioners the LLC has become the business vehicle of choice for non-public enterprises. The various state statutes vary in their description of the duties owed by members of LLCs.

In 1994, NCCUSL approved a Uniform Limited Liability Company Act (ULLCA). The ULLCA was revised in 1996 and consideration is being given to further revisions. A preliminary draft of A Revision of the Uniform Limited Partnership Act was circulated for consideration at NCCUSL's August 2003 annual conference. The American Bar Association has also drafted its own LLC model act known as the "Prototype Limited Liability Company Act ."

California LLCs are governed by the Beverly-Killea Limited Liability Company Act (Corp. Code §§ 17000 et seq.) ("LLC Act"). The LLC Act was enacted in 1994, two

years before the California Partnership Act of 1994 took effect. Nonetheless, the fiduciary duties of managers and members of limited liability companies appear to be governed by the standards set forth for partners under the Partnership Act. Both case and statutory law is extremely limited in California with respect to explaining the fiduciary duties of members of LLCs to each other and to the LLC. Thus, a leading treatise has noted:

> The scope of fiduciary duties owed by LLC members and managers to the LLC and its members is an area of significant uncertainty, particularly in cases where the LLC Agreement purports to reduce fiduciary duties below the level established by the default rules. (Marsh's California Corporation Law (Aspen 2003) § 3.05[E])

The LLC Act differentiates between member-managed limited liability companies from manager-managed limited liability companies.

1. Member Managed LLCs

The LLC Act provides that, "Unless the articles of organization include the statement referred to in subdivision (b) of Section 1751 vesting management of the limited liability company in a manager or managers, the business and affairs of a limited liability company shall be managed by the members subject to any provisions of the articles of organization or operating agreement restricting or enlarging the management rights and duties of any member or class of members. If management is vested in the members, each of the members shall have the same rights and be subject to all duties and obligations of managers as set forth in this title." Cal. Corp. Code section 17150.

The duties of loyalty and care should be incorporated by the provision that the members shall be subject to all "duties" as set forth in the LLC Act because section 17153 provides, "The fiduciary duties a manager owes to the limited liability company

and to its members are those of a partner to a partnership and to the partners of the partnership." Since both the duty of loyalty and the duty of care are specific fiduciary duties of partners under the Partnership Act, these duties apply to all members in a California member managed LLC.

While the issue has not been decided, it may be reasoned that good faith is also encompassed either as an "obligation" incorporated by Corp. Code § 17153 or as a concomitant of contracts generally.

2. Manager Managed LLCs

In a manager managed LLC, managers owe the same fiduciary duties of care and loyalty to the LLC and all its members as are owed by a partner to a partnership and its partners. Corp. Code § 17153. These duties may be modified, although the extent of permissible modification is uncertain, in a written operating agreement with the members' informed consent. Corp. Code § 17005(d). A written agreement may also provide for the appointment of officers of an LLC unless otherwise provided are appointed by the manager(s) of the LLC. Corp. Code § 17154(b).

The LLC Act does not address the fiduciary duties of a non-managing member of a manager managed LLC. It does, however, specifically provide that a member may lend money to and transact other business with the LLC and, "subject to other applicable law, has the same rights and obligations with respect thereto as a person who is not a member." Corp. Code § 17004(a).

3. Waiver

It is uncertain to what extent, members can by agreement waive the fiduciary duties in a LLC.

Corp. Code § 17005 appears to permit members to waive their fiduciary duties, except to the extent that the members are managers. Thus section 17005 provides broad (but not unlimited) authority for members to contract concerning their relationships with each other, even to the extent of varying the provisions of Corp. Code § 17153 which otherwise incorporates the duties and obligations of partners.

Corp. Code § 17005(d) however provides that with respect to managers that, "The fiduciary duties of a manager to the limited liability company and to the members of the [LLC] may only be modified in a written operating agreement with the informed consent of the members." However, section 17153 incorporates the duties of a general partnership ("The fiduciary duties a manager owes to the limited liability company and to its members are those of a partner to a partnership and to the partners of the partnership.") The interplay between those two sections and Corp. Code § 16103(b) (which generally limits the ability to waive certain duties in a partnership agreement) is unclear. Arguably section 17005(d) which basically provides that you one can waive the duties by agreement, should be applied to the LLC context because section 17005(d) is part of the LLC Act. An additional rationale may be offered based on the rule of interpretation that the more specific provision should govern. At present, the matter remains unresolved.

Ethical Considerations

Prepared and Presented by:

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Advanced Partnerships, LLCs And LLPs: *Organization And Operation In California*[3]

III. Ethical Considerations

A. Role Of Attorney As Advisor In LLC And LLP

An initial issue for the attorney is whether or not the prospective client's needs fall within his or her areas of professional expertise. Before representing a prospective client who wants advice on organizing and selecting a business entity, the attorney must have enough preliminary information to determine whether he or she can adequately represent the client. Information should be collected regarding the identities, biographies, and business affiliations of the principals and people that will have material relationships with the potential organization, a summary of the business plan, and trade names that will be used. With this information, the attorney will know, from the beginning. Additionally, counsel will need to use the information to identify any potential conflicts of interest before discussing any significant confidential information or giving any substantive legal advice.

In determining competence, the attorney must have the skill and expertise to handle the matter or associate in co-counsel with the necessary expertise. Advising the client on forming a business entity requires more than understanding the various business entities, but also may include knowledge of other areas of law (*e.g.*, intellectual property, taxation, and securities regulation). Additionally, the attorney may be need to know about the areas of law that will apply to the potential client's organization. If it is

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[3] Prepared with the assistance of Brian Hom, law clerk, Thelen Reid & Priest LLP
This article is intended to provide general guidelines for practice in California by California business entities. Individual cases may vary and business owners should consult their own counsel for specific advice.

determined that the attorney cannot competently represent the potential client or the attorney faces a conflict of interest, the attorney has a duty to protect any confidential information acquired from the potential client.

It is also important that the attorney make sure that all parties involved is to identify the client. The client may be the person who approached the attorney, his or her business partner, the entity, or any combination. Identifying the client is important for the attorney because the parties involved may have conflicting interests and the attorney must represent and protect the interests of the client even if adverse to the interests of another party involved who may have introduced the client.

1. Conflicts of Interest

a. Representing Multiple Clients

Attorneys that are hired to assist with the formation of a business entity are often requested to represent the parties involved as well as the newly formed entity. Commonly the parties will have different interests in the entity with respect to control, liquidity, and capital investments. Pursuant to California Rules of Professional Conduct an attorney should not represent parties with conflicting interests without the informed written consent and waiver from the parties.

An attorney that is representing more than one client should always be aware that potential conflicts may arise throughout the representation. If a conflict should arise, the attorney should inform the parties in writing of the conflict and its consequences. The attorney should then obtain the parties' informed and written consent to continue representation.

A problem may arise if an attorney is representing multiple parties and those parties have a disagreement over the business. While an attorney may with appropriate

disclosures and consent from the parties act as a mediator to attempt to resolve the dispute, if that fails, the attorney will most likely be barred from representing any party if the dispute is brought to mediation, arbitration, or trial.

Professional Rules of Conduct:

Rule 3-310(B) - (F). Avoiding the Representation of Adverse Interests

(B) A member shall not accept or continue representation of a client without providing written disclosure to the client where:

(1) The member has a legal, business, financial, professional, or personal relationship with a party or witness in the same matter; or

(2) The member knows or reasonably should know that:

(a) the member previously had a legal business, financial, professional, or personal relationship with a party or witness in the same matter; and

(b) the previous relationship would substantially affect the member's representation; or

(3) The member has or had a legal, business, financial, professional, or personal relationship with another person or entity the member knows or reasonably should know would be affected substantially by resolution of the matter; or

(4) The member has or had a legal, business, financial, or professional interest in the subject matter of the representation.

(C) A member shall not, without the informed written consent of each client:

(1) Accept representation of more than one client in a matter in which the interests of the clients potentially conflict; or

(2) Accept or continue representation of more than one client in a matter in which the interests of the clients actually conflict; or

(3) Represent a client in a matter and at the same time in a separate matter accept as a client a person or entity whose interest in the first matter is adverse to the client in the first matter.

(D) A member who represents two or more clients shall not enter into an aggregate settlement of the claims of or against the clients without the informed written consent of each client.

(E) A member shall not, without the informed written consent of the client or former client, accept employment adverse to the client or former client where, by reason of the representation of the client or former client, the member has obtained confidential information material to the employment.

(F) A member shall not accept compensation for representing a client from one other than the client unless:

(1) There is no interference with the member's independence of professional judgment or with the client-lawyer relationship; and

(2) Information relating to representation of the client is protected as required by California Business & Professions Code section 6068, subdivision (e); and

(3) The member obtains the client's informed written consent, provided that no disclosure or consent is required if:

(a) *such nondisclosure is otherwise authorized by law; or*

(b) *the member is rendering legal services on behalf of any public agency which provides legal services to other public agencies or the public.*

b. Organization as Client

The Professional Rules of Conduct also state that when an attorney has an organization as a client, in a situation where the organization's management, investors, employees, members, or other constituents have interests that are or may become adverse to the organization, the attorney should explain the client's identity to the adverse party and limit his or her representation to the client's best interests. If it becomes clear that the client's interests and individual director's or manager's interests are adverse and illegal, the attorney may not disclose the information, but must resign from representation.

The Rules provide guidance in this area as follows:

Rule 3-600. Organization as Client

(A) *In representing an organization, a member shall conform his or her representation to the concept that the client is the organization itself, acting through its highest authorized officer, employee, body, or constituent overseeing the particular engagement.*

(B) *If a member acting on behalf of an organization knows that an actual or apparent agent of the organization acts or intends or refuses to act in a manner that is or may be a violation of law reasonably imputable to the organization, or in a manner which is likely to result in substantial injury to the organization, the member shall not violate his or her duty of protecting all confidential information*

as provided in California Business & Professions Code section 6068, subdivision (e). Subject to California Business & Professions Code section 6068, subdivision (e), the member may take such actions as appear to the member to be in the best lawful interest of the organization. Such actions may include among others:

(1) Urging reconsideration of the matter while explaining its likely consequences to the organization; or

(2) Referring the matter to the next higher authority in the organization, including, if warranted by the seriousness of the matter, referral to the highest internal authority that can act on behalf of the organization.

(C) If, despite the member's actions in accordance with paragraph (B), the highest authority that can act on behalf of the organization insists upon action or a refusal to act that is a violation of law and is likely to result in substantial injury to the organization, the member's response is limited to the member's right, and, where appropriate, duty to resign in accordance with rule 3-700.

(D) In dealing with an organization's directors, officers, employees, members, shareholders, or other constituents, a member shall explain the identity of the client for whom the member acts, whenever it is or becomes apparent that the organization's interests are or may become adverse to those of the constituent(s) with whom the member is dealing. The member shall not mislead such a constituent into believing that the constituent may communicate confidential information to the member in a way that will not be used in the organization's interest if that is or becomes adverse to the constituent.

(E) *A member representing an organization may also represent any of its directors, officers, employees, members, shareholders, or other constituents, subject to the provisions of rule 3-310. If the organization's consent to the dual representation is required by rule 3-310, the consent shall be given by an appropriate constituent of the organization other than the individual or constituent who is to be represented, or by the shareholder(s) or organization members.*

c. Obtaining an interest in the client (options or direct ownership)

When an attorney considers accepting an ownership interest in a client or client's business as payment for services, ethical and conflict of interest considerations arise. When an attorney has a financial interest in a client, the attorney may develop interests in the client that are adverse to the proper attorney – client relationship. In some cases the attorney may have to disgorge part or all of the property if there is a dispute that the attorney's fees were unreasonable or unconscionable. Additionally, the attorney may become a "business partner" of the client, thus creating new conflicts.

At a minimum, when an attorney gains a financial interest in a client, the attorney must: (1) fully disclose the transaction in writing to the client; (2) ascertain the fairness of its terms; (3) advise the client in writing that the client may seek independent legal advice; (4) provide the client with a reasonable opportunity to seek such advice; and (5) obtain the client's informed written consent to the transaction. Also, the attorney may need to disclose the transaction to other parties with a material interest in the business and obtain their informed written consent.

The Rules provide:

Rule 3-300 Avoiding Interests Adverse to a Client

A member shall not enter into a business transaction with a client; or knowingly acquire an ownership, possessory, security, or other pecuniary interest adverse to a client, unless each of the following requirements has been satisfied:

(A) The transaction or acquisition and its terms are fair and reasonable to the client and are fully disclosed and transmitted in writing to the client in a manner which should reasonably have been understood by the client;

(B) The client is advised in writing that the client may seek the advice of an independent lawyer of the client's choice and is given a reasonable opportunity to seek that advice; and

(C) The client thereafter consents in writing to the terms of the transaction or the terms of the acquisition.

B. Role of Attorney As An Intermediary In Negotiating And Drafting Papers

After selecting a business entity, it is important that all the terms of the organization are agreed to and if not, an attorney often serves as an intermediary to assist the parties in reaching an agreement and drafting the operating or partnership agreement. If parties have adverse interests, it is common for each party interested in forming the organization to hire independent counsel. If one party is represented by an attorney, then the other parties should obtain separate counsel to protect their interests.

For the most part, the issues and concerns regarding drafting an LLC's operating agreement are similar to drafting a partnership agreements. There are many resources for attorneys charged with drafting agreements to find sample forms and example

agreements. The forms offer guidance on the issues that are common to partnerships and LLCs, but may need to be modified to accommodate specific client's needs.

C. Scope of Engagement In Securities Law And Implications

1. Engagement Letters

As with most legal representation, a written fee agreement should be used for legal services in the formation and counseling of business entities. Given the nature of the legal services rendered in business formation, contingent fee arrangements are rarely used. In certain limited situations an unwritten fee agreement will be enforceable. The situations are: (1) the total expenses to the client will not exceed $1000.00; (2) a client's rights or interests will be prejudiced in an emergency legal situation and a written fee arrangement is impractical; (3) an agreement regarding fees can be implied by the facts; (4) the client waives a written fee agreement; or (5) the client is a corporation.

Attorneys should also be aware that it is a violation of the Rules to charge or collect an unconscionable fee.

2. Securities Law Implications

Among the matters that the attorney must be familiar with in counseling clients with respect to forming a partnership, LLC, or LLP are state and federal securities laws. General partnership interests are not considered to be securities, but limited partnership interest are securities, and membership interest in manager-managed LLC may be securities. Generally, under federal law, the sale of securities is prohibited unless the securities have been registered under the Securities Act of 1933, or an exemption from registration is available. Similar restrictions exist under California's Corporate Securities Law.

D. Other Ethical Considerations

1. Competency

In addition to the issues already discussed, there are two additional rules that every attorney should be aware of in order to avoid any negative ethical issues. Touched on briefly above, before an attorney accepts a client and agrees to assist with the formation and organization of a business entity, it is imperative that he or she is competent in that field of law. The attorney's professional expertise must not only be in the narrow area of law that the client has requested assistance in, but broad enough to be aware of any intersecting areas of law that may arise in the future for the client.

The Rules do not narrow an attorney's practice areas to those that he or she has knowledge, but will a lawyer to become competent on an issue after accepting a client. An attorney may become competent through affiliating with another attorney who is knowledgeable about that area of law. It must be noted that mere independent study on the part of an attorney will not equate to competence. If a reasonable attorney would have affiliated with another attorney specializing in that field of law or hired an outside expert, the attorney that attempts to learn that area of law though independent study will be treated as if he or she is an expert and will be held to the same level of competence.

The Rules provide guidance in this area as follows:

Rule 3-110 Failing to Act Competently

(A) A member shall not intentionally, recklessly, or repeatedly fail to perform legal services with competence.

(B) For purposes of this rule, "competence" in any legal service shall mean to apply the 1) diligence, 2) learning and skill, and 3) mental, emotional, and physical ability reasonably necessary for the performance of such service.

(C) If a member does not have sufficient learning and skill when the legal service is undertaken, the member may nonetheless perform such services competently by 1) associating with or, where appropriate, professionally consulting another lawyer reasonably believed to be competent, or 2) by acquiring sufficient learning and skill before performance is required.

2. Communication

The second ethical area that an attorney must be aware of is communication. An attorney must keep the client informed about the progress of the matter being represented and be responsive to the client's needs. While the Rules envision an attorney to keep in constant communication with their client, the attorney must only relay significant developments in the matter and not every insignificant or irrelevant detail. As a practical matter, proper and frequent communication is a prime way to avoid dissatisfied clients.

The Rules provide guidance in this area as follows:

Rule 3-500. Communication

A member shall keep a client reasonably informed about significant developments relating to the employment or representation, including promptly complying with reasonable requests for information and copies of significant documents when necessary to keep the client so informed.

3. Continued Representation of Suspended Corporation

You should advise those for whom you establish a corporation of the importance of continued payment of the California corporate franchise tax. Not only does a corporation that fails to do so lacks the capacity to sue in this state and if sued, cannot defend in court. (Rev. & Tax. Code § 23301).

Anyone who purports to exercise the rights and powers of a suspended corporation--possibly including a lawyer who appears on its behalf--is guilty of a misdemeanor. (Rev. & Tax. Code . § 19719).

In addition, a lawyer who *knowingly* represents a suspended corporation and conceals this fact from the court may be subject to *sanctions*. (*Palm Valley Homeowners Ass'n., Inc. v. Design MTC* (2000) 85 Cal.App.4th 5553, 563.

4. Attorney's Duty Not to Misrepresent to Investors.

In the Enron litigation the federal district court in Texas held:

> This Court concludes that professionals, including lawyers and accountants, when they take the affirmative step of speaking out, whether individually or as essentially an author or co-author in a statement or report, whether identified or not, about their client's financial condition, do have a duty to third parties not in privity not to knowingly or with severe recklessness issue materially misleading statements on which they intend or have reason to expect that those third parties will rely. Such a duty has been established in cases including *Klein v. Boyd, Caiola v. Citibank, Rubin v. Schottenstein, Ackerman v. Schwartz, Trust Company of Louisiana v. N.N.P.,* and *Ernst & Young v. Pacific Mutual Life Ins.* Moreover, with respect to the element of reliance, for purposes of § 10(b) as well as the tort of fraudulent misrepresentation, the Court is concerned about avoiding the danger of opening the professional liability floodgates to any and every potential investor or foreseeable user of the allegedly misleading information who might obtain and rely on the statement. Therefore this Court finds that a restrictive approach with respect to the group to which the attorney or accountant owes the duty and which thus should have standing to sue, such as that taken by Texas, is appropriate and necessary. In this suit, Lead Plaintiff has alleged as a crucial part of the Ponzi scheme that at least some fraudulent misrepresentations were made by Vinson & Elkins and Arthur Andersen and were aimed at investors to attract funds into Enron, as well as at credit rating agencies to keep Enron's credit rating high and bank loans flowing. Therefore the "limited group" that the attorneys or accountants allegedly intended,

> or might reasonably have expected, to rely on their material misrepresentations, and who allegedly did rely and suffered pecuniary loss, included Plaintiffs in this suit.

In re Enron Corp. Securities, Derivative & ERISA Litigation, 235 F. Supp. 549, 610-611 (S.D. Tex. 2000)

Recent Developments And The Future – RE-RULPA

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Advanced Partnerships, LLCs And LLPs:
Organization And Operation In California[4]

IV. Recent Developments And The Future

A. RE-RULPA

1. HISTORY, DIGEST AND PURPOSE

The Uniform Limited Partnership Act (2001) was "approved and recommended for enactment in all the States" in August 2001 by the National Conference of Commissioners on Uniform State Laws ("NCCUSL").

Currently, formation of limited partnerships under California law and the operation of such limited partnerships are governed by the California Revised Limited Partnership Act, Sections 15611 through 15800 of the Corporations Code ("CRLPA"), which was modeled on the Uniform Limited Partnership Act (1976).

As originally enacted, Section 15722 of CRLPA provided that "[i]n any case not provided for in this chapter, the provisions of the Uniform Partnership Act, Chapter 1 (commencing with Section 15001) govern." When the Uniform Partnership Act of 1994 (Chapter 5 of Title 2 of the Corporations Code) was enacted in 1996, Section 15722 was amended to read:

> In any case not provided for in this chapter, limited partnerships shall be governed in the same manner as general partnerships would be governed pursuant to Section 16111, by the Uniform Partnership Act (Chapter 1 (commencing with Section 15001)), or the Uniform Partnership Act of 1994 (Chapter 5 (commencing with Section 16100)).

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[4] Substantial portions reprinted with the permission of David Marion, Hoge, Fenton, Jones & Appel. Prepared with the assistance of Brian Hom, law clerk, Thelen Reid & Priest LLP. This article is intended to provide general guidelines for practice in California by California business entities. Individual cases may vary and business owners should consult their own counsel for specific advice.

Thus, CRLPA, like the uniform act on which it was modeled, was drafted to rest on and link to the Uniform Partnership Act. As noted by NCCUSL, "This arrangement has not been completely satisfactory, because the consequences of linkage are not always clear."

In August 2001, NCCUSLA approved and recommended for enactment in all states the Uniform Limited Partnership Act (2001) commonly known as RE-RULPA as a standalone statute, de-linked from the general partnership law. NCCUSL's conclusions were that a standalone statute would:

- "be more convenient, providing a single, self-contained source of statutory authority for issues pertaining to limited partnerships;
- eliminate confusion as to which issues were solely subject to the limited partnership act and which required reference (i.e., linkage) to the general partnership act; and
- rationalize future case law, by ending the automatic link between the cases concerning partners in a general partnership and issues pertaining to general partners in a limited partnership.

Thus, a stand alone act seemed likely to promote efficiency, clarity, and coherence in the law of limited partnerships."

The new law also would promote greater certainty with respect to entities formed prior to its effective date. CRLPA, which became effective July 1, 1984, even today may or may not apply to limited partnerships formed prior to that date.

2. CURRENT STATUS

The Partnership and Limited Liability Companies Committee of the Business Section of the California State Bar ("PLLC Committee") has recently completed a two-year review of RE-RULPA. Following that review, RE-RULPA, with certain changes recommended by the PLLC Committee, RE-RULPA, with certain changes recommended

by the PLLC Committee has been approved as an affirmative legislative proposal by the Business Law Section of the Business Law Section of State Bar of California, and it anticipated that it will be introduced as legislation in the 2004-2005 legislative session. If passed in one year, it will likely have an effective date of January 1, 2006. If it turns out to be a two year bill, then the effective date will be delayed by one year and will be effective on January 1, 2007.

3. Key Changes Proposed Under RE-RULPA

a. Liability of Limited Partners

Under the limited partnership law that existed prior to the enactment of CRLPA, a limited partner could become liable as a general partner if he took part in the control of the business of the partnership. CRLPA restricted that exposure by providing that a limited partner can become liable as a general partner if he participates in the control of the business, but "only to persons who transact business with the limited partnership with actual knowledge of that partner's participation in control and with a reasonable belief, based upon the limited partner's conduct, that the partner is a general partner at the time of the transaction." In addition, CRLPA set forth certain activities which do not constitute participation in control of the partnership's business.

Sections 303 of the proposed new law would eliminate the control rule and provide a full, status-based shield against limited partner liability for obligations of a limited partnership.

b. Limited Liability Limited Partnerships

The new law would also provide that a limited partnership can elect to be a limited liability limited partnership ("LLLP"). In an LLLP no partner — whether general or limited — is liable on account of partner status for the limited partnership's

obligations. Both general and limited partners benefit from a full, status-based liability shield that is equivalent to the shield applicable to shareholders of a corporation or members of an LLC. The PLLC Committee believes this is desirable to encourage investment and participation in such entities. Because under current law the general partner of a limited partnership is often itself a limited liability entity such as a corporation or limited liability company, the existence of LLLPs will not significantly increase the risk to persons who deal with limited partnerships.

4. WHAT CHANGES FROM THE MODEL ACT DRAFTED BY NCCUSL ARE PROPOSED?

The Partnership and Limited Liabilities Committee ("PLLC Committee") of the Business Law Section of the California State Bar Association over the last two years reviewed all sections of RE-RULPA and following review and debate among all of its members, drafted changes as deemed appropriate. Changes from the model act are in the chart provided below which also sets forth highlights of RE-RULPA:

SUMMARY OF HIGHLIGHTS AND* DIFFERENCES *BETWEEN NCCUSL MODEL ACT AND RE-RULPA AS PROPOSED BY THE PLLC COMMITTEE

SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW OR REASON FOR CHANGE FROM MODEL ACT
ARTICLE I	**GENERAL PROVISIONS**			
102(9), 201(1)(4) AND 404 (c)	Makes LLLP status available through simple statement in the Certificate of LP	same		Note: Limited liability limited partnership (LLLP) concept is new
104(c)	Duration is perpetual	same		
108	Use of LP name in entity okay	same		
119	no similar provision	Service of process; production of books and records	Ca. Corp. Code ("CCC") §15627	Consistent with existing law
120	no similar provision	Jurisdiction, Arbitration, service of process	CCC § 15627.5	Consistent with existing law
ARTICLE II	**FORMATION; CERTIFICATE OF LIMITED PARTNERSHIP AND OTHER FILINGS**			
201	Certificate of LP to be "delivered" to SOS	Certificate must be filed by SOS and partners to enter into LP agreement to effect formation LP	CCC § 15621	Consistent with existing law
205	no similar provision	Provides for reimbursement of expenses and atty. fees if action to compel filing or signing record for SOS required	CCC § 15625	Consistent with existing law

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SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW <u>OR</u> REASON FOR CHANGE FROM MODEL ACT
210	Filing of annual report with SOS required	None required		Consistent with current CA Law, no annual filing requirement
ARTICLE 3	**BECOMING A LIMITED PARTNER**			
301	Admission of new Limited partner requires <u>consent</u> of all partners	same	CCC § 15631	Current law requires written consent
302	Limited partner cannot bind LP	same		New; provision equates limited partner status with that of corporate shareholder
303	No Limited Partner liability for LP liabilities, whether or not LP is an LLLP, and even if Limited Partner participates in the management and control of the LP	same	CCC § 15632	Changes existing law "control" rules, see (i.e. liable if participates in management or control of business)
305	No fiduciary duties solely by reason of being Limited Partner	same		
307	None	Permits creation classes of LP interests	CCC § 15631.5	Consistent with current law
ARTICLE 4	**GENERAL PARTNERS**			
401	Status as general partner not dependent on being so designated in certificate of LP	same	CCC § 15641	Note: written consent not required under 401(4), contrary to current law (although partnership agreement can specify otherwise)

SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW **OR** REASON FOR CHANGE FROM MODEL ACT
402	General partner is agent of LP	same	CCC § 15509	Current law requires that GP have written consent to do many acts. Under RE-RULPA the fact that person is not listed in certificate of LP is not notice that the person is not a GP (and therefore lacks authority to act for the LP)
403	LP is liable for GP's actionable conduct	same		Note: Does not diminish GP direct liability for own misconduct
404	An obligation of a LP incurred while the LP is a LLLP is solely the obligation of the LP (404(c))	same	CCC § 5509	LLLP status available by designating LP as LLLP in the certificate, providing full liability shield to all GPs. If LLLP status not elected, then GP remains liable as with former law
405	GP may be joined in action against LP if not inconsistent with 404	same		If LP is LLLP throughout its existence, this will bar action against GP, unless GP has liability independent of the LP

SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW OR REASON FOR CHANGE FROM MODEL ACT
406	GP can decide all matters relating to activities of the GP excepts those specified; also provides for no right to compensation for services performed for the partnership	same	CCC § 164501 right to compensation for services in winding up	Consistent with theme of strong, centralized management by GP, with limited partners excluded from ordinary management. No right to compensation for services to LP by GP (eliminating former statutory right to compensation for services in winding up)
408	Fiduciary duties that GP has to LP include duties of loyalty and care	Statutory fiduciary duties not exclusive	CCC § 16404	Consistent with current GP law
409	no similar provision	Permits classes of GP interests	CCC § 15645	Consistent with current GP law
ARTICLE 5	**CONTRIBUTIONS AND DISTRIBUTIONS**			
501	Contribution of partner may consist of tangible or intangible property, money, etc	same	CCC § 15651	Under CC 15651, no contribution of money, property or services required
503	Distributions based on value of contributions	No requirement of valuation of contributions	CCC § 15654	Consistent with current LP law, distributions made as provided in agreement or in proportion to capital contributions (not based on "value" of such contributions)

SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW <u>OR</u> REASON FOR CHANGE FROM MODEL ACT
503.5	Distributions on basis of value of cap. Contributions	Profits and losses will be allocated per agreement or if none, then same as distribution of profits	CCC § 15653	Consistent with current LP law
507	LP may offset amounts owed by partner to LP against claim of LP, who has status of creditor	Same	CCC § 15665	Partner with claim against LP has all rights of a creditor
508	Partnership may not make distribution in violation of partnership agreement, including those that would render the LP insolvent	Distribution will not include amounts constituting reasonable compensation for present or past services, or in ordinary course of business to a retirement or other benefits plan		Payments to partners and employees should not be subject to claims of LP's creditors
509	Statute of limitations on improper distributions is 2 years	Statute of limitations on improper distributions is 4 years	CCC § 15666	Consistent with existing CA LP law
ARTICLE 6	**DISSOCIATION**			
601	Dissociation cannot occur until termination of LP or other events, such as breach of the obligation of good faith and fair dealing (601)(b)(5)(B)	same	CCC § 16404 (b), (c)	Concept of withdrawal replaced with dissociation; provided that fiduciary duties included duty of loyalty and duty of care.

SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW OR REASON FOR CHANGE FROM MODEL ACT
602	Upon dissociation, limited partner becomes mere transferee but unless otherwise agreed has not right to receive a distribution on account of dissociation	same	CCC § 15664	Under existing law, unless otherwise agreed, upon withdrawal, any withdrawing partner is entitled to receive, within reasonable time after withdrawal, the fair value of the limited partner's interest in the LP as of the date of withdrawal based upon right to share in distributions from the LP
605	GP can give notice of dissociation by filing statement with SOS	same	CCC §§ 15643, 15722	consistent with existing law
606	Dissociated GP cannot bind LP if actual notice or more than 2 years after dissociation	same	CCC §§ 15722, 16702	consistent with existing law
ARTICLE 7	**TRANSFERABLE INTERESTS AND RIGHTS OF TRANSFEREES AND CREDITORS**			
703	Judgment creditor of partner may obtain charging order on partnership interest, appoint receiver and order foreclosure	same	CCC § 15673	More detailed procedure and remedies than provided under existing law

SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW <u>**OR**</u> REASON FOR CHANGE FROM MODEL ACT
ARTICLE 8	**DISSOLUTION**			
801	Except as otherwise provided in Section 802, a limited partnership is dissolved, and its activities must be wound up, only upon the happening of an event specified in the partnership agreement; the consent of all general partners and of limited partners owning a majority of the rights to receive distributions as limited partners at the time the consent is to be effective, or after the dissociation of a person as a general partner	same	CCC § 15681	Former law required consent of "majority in interest" of limited partners, rather that of limited partners owning a majority of the rights to receive distributions. Note that RE-RULPA *does not* require that consents to dissolution be given in form of a *signed record,* although the partnership agreement has the right to impose that requirement (per Section 110).
809	Secretary of State can dissolve LP for failure to pay taxes or deliver annual report (and see changes to 801 eliminating reference to SOS power to dissolve)	No dissolution permitted	none	Consistent with existing CA law, no procedure for administrative dissolution
810	Secretary of State can reinstate LP after administrative dissolution	No reinstatement because no dissolution	none	Consistent with existing CA law, no procedure for administrative dissolution or reinstatement

SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW **OR** REASON FOR CHANGE FROM MODEL ACT
811	Administrative appeal from denial of reinstatement	No appeal because no denial of reinstatement, not applicable	none	Consistent with existing CA law
ARTICLE 9	**FOREIGN LIMITED PARTNERSHIPS**			
902	Permits Foreign LP to apply for Certificate of Registration to transact business in this state, listing agent for service of process, general partners and other information	same	No similar provision	This will be a new procedure under RE-RULPA
903	Activities Not Constituting Transacting Business	LP engaged in isolated transaction, completed within 180 days, is exempt from registration	CCC § 15681	Under RE-RULPA, registration of LP completing transaction within 30 days is not required (expanded to 180 days, consistent with current CA law)
906	Revocation of Certificate of Authority	No revocation provided for	No similar provision	Since SOS does not issue certificate of authority, revocation unnecessary
907	Cancellation of Certificate of Authority, sets forth consequences for failure to register, such as inability to defend an action, and appointing SOS as agent for service upon failure to register	Provide for cancellation Certificate of Registration		Similar to consequences failure to register as foreign corporation
ARTICLE 10	**ACTIONS BY PARTNERS**			
1001	Direct actions by partners permitted	same	none	Codifying existing law

SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW <u>OR</u> REASON FOR CHANGE FROM MODEL ACT
1002	Derivative Actions permitted	same		
1005	Proceeds and Expenses	same	None	Provides for award of attorney's fees and costs to successful plaintiff
1006	No similar provision	Posting of bond required in derivative action	CCC § 17501	Consistent with current law
ARTICLE 11	**CONVERSIONS AND MERGER**			
1105.5	No similar provision	Recording certificate of conversion perfects ownership of real property in LP	CCC § 15678.8	Consistent with current law
1107	Merger must be approved by all partners	Merger must be approved by all GP and majority of Limited Partners	CCC § 15678.2	Consistent with current CA law, including grant of dissenter's rights to non- consenting partners
1109.5	No similar provision	Recording of agreement of merger perfects title to real property in surviving entity	CCC § 15677.7	Consistent with current CA law
1110	Unanimous consent of all partners required for conversions or mergers	Eliminates statement that required consent cannot be included in limited partnership agreement which permits amendment with fewer than all of the partners		Permits partnership agreement to control

SECTION NO.	NCCUSL VERSION (MODEL ACT)	PLLC COMMITTEE VERSION	EXISTING CA LAW	COMMENTS RE CHANGE FROM EXISTING LAW OR REASON FOR CHANGE FROM MODEL ACT
ARTICLE 13	**DISSENTING LIMITED PARTNER'S RIGHTS**			
1301-1314	No similar provision	Retains statutory dissenter's rights of non-consenting partners to mergers and conversions	CCC §§ 15679.1 - 15679.14	

* Written comparative analyses of each article RE-RULPA were made by members and associates of the Partnerships and LLCs Committee, Business Law Section, State Bar of California. Each article was analyzed and compared to current California law, which materials were drawn upon in preparation of this outline. Accordingly, thanks for their contributions to the materials included in this outline, is hereby made to the following persons: Article 1, 12 and 13, David Marion; Article 2, Christopher Toews (with Greg Vignos); Article 3, Robert Cornell; Article 4, Edward Gartenberg; Article 5, Philip Jelsma; Article 6, Lemoine Skinner; Article 7, Robert J. Brown; Article 7.6, Arthur Yoon, Article 8, Denise Olrich; Article 9, John J. Camozzi; Article 10, Robert Weiss; Article 11, David Greenberg.