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A PERSPECTIVE TO RECONSIDER PARTNERSHIP LAW†

DONALD J. WEIDNER*

The Uniform Partnership Act, unchanged in over seventy years, is being considered for revision by the National Conference of Commissioners on Uniform State Laws. As Reporter to the Drafting Committee, Professor Weidner recommends that the revision process begin with a reconsideration of the fundamentals of partnership law. The drafters of the present act struggled to reconcile the conflicts between the entity and aggregate theories of partnership, conflicts which still permeate partnership law. While theoretical consistency may be desirable, a pragmatic approach to revision requires a structuring of partnership law that will serve the needs of both large and small partnerships. Major factors that must be considered during revision include the current business and investment uses of partnerships, changes in the laws that govern other forms of business organizations, and federal income tax treatment. Several specific provisions of the present Act that require close scrutiny include those relating to the duties of care and loyalty, dissolution, and other remedies available to dissatisfied partners. Professor Weidner concludes that the revision process can move the law of general partnership more toward an entity model without adverse tax consequences.

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I. INTRODUCTION

THE UNIFORM Partnership Act has not been revised in over seventy years. This product of the National Conference of Commissioners on Uniform State Laws has enjoyed widespread adoption and been the object of relatively few state variations. Nevertheless, in 1984, the State of Georgia enacted massive revisions to its partnership statute.¹ In January of 1986, an American Bar Association Committee issued a thoughtful report that recommended an extensive series of revisions to the Uniform Partnership Act, many of them along the lines of the recent Georgia changes.² In the fall of 1986, Congress enacted the Tax Reform Act of 1986.³ The 1986 Act changed the comparative tax advantages of partnerships and corporations by setting corporate income tax rates higher than individual income tax rates while tightening up on the corporate income tax. Because partnerships are conduits for federal income tax purposes such that partnership income is taxed not at the entity level but only at the level of the individual partners, "disincorporation" or "unincorporation" has become a topic of much discussion.⁴ Spurred in part by these developments, the National Conference of Commissioners on Uniform State Laws has formally undertaken a project to consider a revision of the Uniform Partnership Act.

There are two basic ways the Conference of Commissioners might proceed. First, the Commissioners could proceed directly to the Uniform Partnership Act, compare it with the new Georgia statute and the American Bar Association Report, and quickly edit it to incorporate the most obviously appealing features of these recent and credible efforts. Second, the Commissioners could begin their consideration, not with the details of the latest statute and the recently proposed

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². UPA Revision Subcommittee of the Committee on Partnerships and Unincorporated Business Organizations, Should the Uniform Partnership Act Be Revised?, 43 BUS. LAW. 121 (1987) [hereinafter ABA Report]. Professor Harry J. Haynsworth, of the University of South Carolina School of Law, was the Chairman of the ABA Subcommittee.
⁴. One author summarizes the limited utility of the C corporation as follows:
   In particular, the repeal of the so-called General Utilities doctrine, when combined with the revised corporate alternative minimum tax increases, seems to . . . put some real teeth into . . . the corporate income tax. What this means is that one form of conducting a business—the traditional C corporation—will be a taxing entity, but the other three traditional forms—S corporations, partnerships, and proprietorships—will not be. From this simple observation, it is obvious I think, that C corporations are an endangered species.
amendments, but with a broad review of the purposes of partnership law and the conceptual and practical tensions that cause a reconsideration in the first place. The purpose of this article is to explore the latter approach. It asks the basic question: What is the continuing need, if any, for a separate form of business organization called a partnership? In particular, given developments in the law of corporations and limited partnerships, what role remains for a partnership statute?

II. THE ORIGINAL UNIFORM PARTNERSHIP ACT

A. Basic Conceptions of the Original Drafters

The original Uniform Partnership Act (Uniform Act) went through eight tentative drafts over a span of twelve years before approval by the Conference of Commissioners at their 1914 meeting. The first two drafts were submitted to the Committee by Dean James Barr Ames of the Harvard Law School. On the death of Dean Ames, William Draper Lewis, of the University of Pennsylvania Law School, took up the work. Discussing the purposes of the final product, Professor Lewis stated that the merit of the Uniform Act would depend on whether it stated the law in simple, clear language, whether it resolved existing uncertainties, and whether the substantive changes it introduced were beneficial.

In discussing the extent to which the Uniform Act eliminated uncertainties, Professor Lewis emphasized that, “there is one matter connected with partnership which legislation cannot make certain. By no human ingenuity would a Partnership Act which does not abolish common law partnerships enable the person who reads it to tell in every supposable case whether there is or is not a partnership.” This statement reflects far more than a recognition that codification will never eliminate all uncertainty. It reflects his focus on inadvertent and other small partnerships and his basic assumption that partnership is a residual category.

To Lewis, the “fundamental characteristic” of partnership law was that it is a residual body of law that governs all relationships that are not “statutory in origin.” Unfolding the Uniform Act for public view, he stated that the uncertainty about whether given arrangements will constitute partnerships:

6. Id. at 621.
7. Id. at 622.
8. Id.
lies in the fundamental characteristic which distinguishes partnerships from every other business association. All other business associations are statutory in origin. They are formed by the happening of an event designated in a statute as necessary to their formation. . . . Partnership is the residuum, including all forms of co-ownership, of a business except those business associations organized under a specific statute.9

A statute providing that a partnership is not formed until compliance with its formalities occurs, continued Lewis, "would not be a statute regulating common law partnerships, but one abolishing common law partnership and establishing a new form of statutory association."10 If no formal act is necessary to establish a partnership, it will not always be "easy to determine whether the acts proved indicate co-ownership of a business. Ownership . . . involves the idea of control; but the degree of control necessary is incapable of exact definition."11

Uncertainty in the law of partnerships was seen as primarily due to conflicts among the decisions of different states, the absence of legal authority, even on important issues, and confusion on the legal theory of partnerships. Lewis thought that the greatest source of uncertainty was confusion over the basic theory of partnerships, that is, whether the partnership was to be viewed as an entity or an aggregate.

B. The Entity Versus the Aggregate Approach

The law of partnerships has long been characterized by efforts to identify those issues to be resolved in accord with the entity theory of partnerships and those to be resolved in accord with the aggregate theory of partnerships. This dichotomy has long existed under state law, and has more recently come to exist for federal income tax purposes. Traditionally, the common law aggregate approach declined to recognize the partnership as an organization with a separate legal personality. The aggregate approach viewed the partnership as nothing more than a conduit for the collection of individuals it embraced. Each partner was seen as owning a direct stake in the partnership assets and as conducting his pro-rata share of partnership business. The entity theory, on the other hand, treated the partnership as a distinct, almost tangible, entity interposed between partners and partnership assets. The partner's interest was viewed as a separate bundle of rights and liabilities associated with his participation in the organization, analo-
gous to the interest of a corporate stockholder in his shares of stock.

As the state law of partnership developed, the adoption of the entity approach was urged on the ground that it was a feature of the law merchant that reflected business reality more accurately than the aggregate or conduit theory. Ready acceptance of the entity theory was probably impeded by two nineteenth-century common law preconceptions. The first was the notion that the separate legal personality of a business organization was associated with relieving its owners from personal liability. The second was the related notion that organizational personality was a special privilege to be dispensed only by the legislature. Neither of these notions transferred readily to the relations of partners, who were unlimitedly liable and whose relation as partners could be judicially established independent of their intent.

Tension between the two theories continues under state law in part because the Uniform Act is a product of drafters who espoused opposing theories. Dean Ames, who prepared the first two drafts, espoused the entity theory, whereas Professor Lewis, who took over after Ames' death and shepherded the project to completion, strongly supported the aggregate theory. According to Lewis, "[t]he chief source of uncertainty [in the common law] ... as well as the source of several distinctly inequitable rules of our existing law of partnership is the confusion in regard to the nature of a partnership and the legal incidents attached to the partner's right in partnership property." Under his stewardship, the project declared its intent to turn away from the entity theory and emphasize the common law aggregate approach.

Although Lewis denounced the entity theory quite roundly, he did not argue that it had no value. He admitted, for example, that the entity theory ended some of the confusion in the law concerning the rights of a partner's separate creditors:

If the partnership is a legal entity against which the partners have claims for their shares in the profits and in the surplus, after the payments of debts to third persons, then the separate creditor of a partner may garnishee the fictitious legal person or bring a bill in equity against it for the purpose of ascertaining the claims of his debtor, and having these claims paid over to him, in the satisfaction of his judgment.

12. Id. at 623.
13. See id. at 640 (discussion of the pivotal meeting resolving to shift from the entity to the aggregate approach).
14. Id.
More fundamentally, Lewis rejected the notion that the entity theory was an accurate reflection of a business practice that treated partnerships as entities. He believed that those who advocated the entity or "mercantile theory" did so because they assumed as an empirical matter "that business men in partnership transactions, whether inter se or with third persons, proceed on the fundamental premise on which the theory is based." He perceived business reality differently:

When a business man deals with persons carrying on business in partnership, the character of the partners and their total wealth, individual and collective, is all that is important to him. The rule that partners are unlimitedly liable for partnership debts is the only thing approaching a legal theory which he need carry in his mind.

Lewis also claimed that the entity theory made "it impossible to work out in a satisfactory way the rights of a firm creditor against the separate property of a partner." If the partnership is a "separate legal personality," he questioned, what is the relationship of the partners to those who do business with the partnership? Should the partners be regarded as "co-principals," and the partnership contract be treated as a joint contract between partners and their partnership entity? Or should the partners be seen as having no legal relationship with partnership creditors, having "merely contract[ed] with the legal entity to pay partnership debts, if the property of the entity is not sufficient to pay them?"

Lewis would not accept the second solution, which had been favored by Ames. He felt it was "cumbersome" to take a position that "denies all contractual relations between the partners and the person dealing with the partnership..." He argued that theoretical consistency would require a creditor who obtains a judgment against the partnership to "bring a new proceeding against the partner whose separate property he desires to subject to the payment of his debt." Lewis said that such an approach would violate the understanding "of every business man who deals with a partnership, that he is dealing

15. Id. at 639.
16. Id.
17. Id. at 640-41.
18. Id. at 640.
19. Id.
20. Id. at 640-41.
21. Id. at 641.
22. Id.
23. Id.
24. Id.
with a group of persons who are directly and unlimitedly liable for partnership obligations." Given that you are required to join the partners as co-principals, said Lewis, why add the "fictitious legal person?"

Finally, Professor Lewis said that the "most serious practical difficulty" with the entity theory was that it entails a partnership registration system and a provision that a partnership cannot exist until it is registered:

Any system which prevents a partnership from being in existence until it is registered, and which thus introduces into the law of partnerships the difficulties which surround *de facto* corporations, should not be tolerated for a moment unless the necessity for the adoption of the theory is imperative. No such necessity exists.

The extent to which the final product incorporates the entity as opposed to the aggregate theory is very much in the eye of the beholder. The Uniform Act was greeted by the suggestion that it embodied the entity theory much more than its drafters cared to admit. Many still believe that entity notions permeate the Uniform Act, although there is also respected authority that the aggregate theory predominates. Learned Hand, for example, thought it would be a "palpable perversion" to derive an entity approach from the Uniform Act:

The Uniform Partnership Act . . . did not . . . make the firm an independent juristic entity. . . . [T]he essentials of the old model were preserved. Indeed, many of the supposed innovations were not such; for example, the limitation upon a partner's power to assign

25. *Id.*
26. *Id.*
27. *Id.*
28. The term "partnership property" is used in § 8 and throughout the Uniform Act. Section 8(3) permits the partnership to take and convey title in the partnership name. Section 9(1) makes every partner an agent of the partnership. Section 12 discusses a fraud by the partner on the partnership. Section 18(a) imposes on a partner the duty to contribute to the losses of the partnership. Section 40(a)(2) provides that the right to contributions is a partnership asset. Section 18(b) requires the partnership to indemnify the partner in certain cases. Section 21 makes a partner accountable to the partnership, and § 35 discusses the partner's power to bind the partnership after dissolution. One writer comments, "These extracts seem more consistent with the entity than with the aggregate view of the nature of the partnership and illustrate the difficulty, if not impossibility, not only of writing and talking about the partnership, but of formulating its rights and obligations without treating it as a legal person." *Crane, The Uniform Partnership Act: A Criticism*, 28 HARV. L. REV. 762, 771 (1915). See also *Crane, The Uniform Partnership Act and Legal Persons*, 29 HARV. L. REV. 838, 843 (1916).
29. See J. CRANE & A. BROMBERG, LAW OF PARTNERSHIP 16-29 (1968) [hereinafter CRANE & BROMBERG].
firm property, the declaration that his interest in it "is his share of the profit and surplus" and the extent of an assignee's interest acquired by the assignment, had all been law before, at least in some jurisdiction. . . . With this history before us, it would be a palpable perversion to understand the act as creating a new juristic person, which owned the firm property and was obligor of the firm debts, against which the partners had only a chose in action, and to which they were liable as guarantors.\textsuperscript{30}

Most cases can, of course, be decided without resort to the general theory of the partnership as an entity versus an aggregate. On the other hand, it seems clear that the general theory of the organization will be influential in certain cases. \textit{Fairway Development Co. v. Title Insurance Co.}\textsuperscript{31} is a recent example of a case that appears to have been decided by resorting to the general notion that a partnership is an aggregate rather than an entity. A real estate development partnership consisting of three individuals took out a title insurance policy with the defendant. Subsequently, two of the partners "transferred not just their interest in the partnership, i.e., their respective shares of profits and surplus, but their entire respective bundles of partnership rights" to the remaining partner and a third person.\textsuperscript{32} When an undisclosed pipeline easement was discovered and the surviving partnership sued for breach of the title insurance contract, the court held that a new partnership had been formed and that the new partnership had no "standing" to bring the action.\textsuperscript{33} The court was not impressed with the argument that all members of both the old and the new partnerships intended the new partnership to continue with all the assets and business of the old partnership. The court held that the insurance contract was with the first partnership, which had dissolved.\textsuperscript{34} Hence, the court held, the title insurance company "is not in privity with the plaintiff as the named party guaranteed."\textsuperscript{35} To emphasize, the court explained its decision solely as a consequence of the theory that a particular aggregation of individuals had dissolved, and without any discussion of the intent or legitimate expectations of the parties, windfalls, or wipeouts.\textsuperscript{36}

\textsuperscript{30} Helvering v. Smith, 90 F.2d 590, 591-92 (2d Cir. 1937) (citations omitted).
\textsuperscript{31} 621 F. Supp. 120 (N.D. Ohio 1985).
\textsuperscript{32} \textit{Id.} at 124.
\textsuperscript{33} \textit{Id.} at 125.
\textsuperscript{34} \textit{Id.}
\textsuperscript{35} \textit{Id.} at 121.
\textsuperscript{36} In addition to basic partnership provisions based on the Uniform Act, the Ohio statutes also contain a special supplement on fraud in partnership affairs and the use of fictitious names in partnerships. Partnerships transacting business in Ohio under names that are fictitious or do
In short, the Uniform Act was still warm from the oven when the debate started over whether it reflected an aggregate or an entity theory. On the one hand, provisions such as the one that states that “the partnership is liable” for wrongful acts of partners clearly reflect an entity approach. On the other hand, the Uniform Act scrapped the initial definition of a partnership as “a legal person” formed by the association of two or more individuals. In the middle, many of its provisions can be rationalized in terms of either theory. The subsequent experience with the federal income tax law of partnerships suggests that it is not necessary to exalt one theory at the cost of the complete suppression of the other. Each approach has its place, depending on the policies dominant in a particular situation—for example, simplicity versus precision. It nevertheless might be helpful to state the residual theory that will be applied, or tend to be applied, if other analysis fails. Given that the entity theory seems to inhere in the Uniform Act more than its final authors cared to admit, given that the entity theory seems to cut in favor of rather than against simplicity, and given that partnerships of significant size and complexity have become common, including partnerships with corporations and limited not reveal the names of all the partners must record a certificate stating the name and residence of each partner. Ohio Rev. Code Ann. § 1777.02 (Anderson 1985). The court in Fairway Development found significance in the requirement that a new certificate be filed whenever there is a change in membership in a registered partnership. 621 F. Supp. at 123. See Ohio Rev. Code Ann. § 1777.03 (Anderson 1985). Incorrectly assuming that the special supplementary provisions are part of the Uniform Act, the court found in them further support for the aggregate theory:

[Where members of a general partnership change, the partnership must file a new certificate of partnership, unlike a limited partnership, which simply may amend its certificate of partnership. The fact that the Uniform Partnership Law makes this distinction supports a finding that the authors of the Uniform Partnership Act recognized that a change of the members of a general partnership in fact changes the original partnership and creates a new partnership requiring a new certificate, as opposed to an amendment to the original certificate.

Fairway Development, 621 F. Supp. at 123.


38. Lewis, The Uniform Partnership Act—A Reply to Mr. Crane’s Criticism, 29 Harv. L. Rev. 158, 165 (1915).

39. The accounting partnership in Wheeler v. Hurdman, 825 F.2d 257 (10th Cir. 1987), had 3,570 personnel, 502 of whom were partners, in 80 offices. The court stated:

For many purposes evolving law now classifies partnerships as separate entities rather than an aggregate of partners; thus partners can be classed as employees of the partnership entity. Furthermore, ownership in very large partnerships is de minimus on an individual basis (Wheeler as one of 500, for instance). Finally, big partnerships are like corporations: “Wall Street law firms and stock brokerage firms provide significant examples. These are often large, impersonal, highly structured enterprises of essentially perpetual duration.”

partnerships as partners, there is widespread opinion that a revised Uniform Act should more directly adopt an entity model. The ABA Report recommends that the entity theory "be incorporated into any revision of the UPA whenever possible and that the 'aggregate theory' should be retained only where it appears to be essential, e.g., because of tax considerations." Whether and how to directly embrace an entity model will be a central philosophical question for the Commissioners.

III. CONTINUITY, DISSOLUTION AND THE DISSATISFIED PARTNER

A. The Tenancy in Partnership

The basic provision for the stability of the partnership form is the tenancy in partnership. The Uniform Act provides that partnership property is held by the partners in a special form of coownership designated tenancy in partnership. As the incidents of the tenancy in partnership are unfolded, it becomes clear that the partnership is

40. See, e.g., M. Eisenberg, An Introduction to Agency and Partnership 36 (1987): On the whole . . . the use of an aggregate theory in the U.P.A. was unfortunate. Generally speaking, the entity theory of a partnership is much more functional than the aggregate theory. In those cases where the U.P.A. does not treat the partnership as if it were an entity, the result tends to be bad, and in need of correction. In those cases where the U.P.A. does treat the partnership as if it were an entity, the result is good, but the statutory approach is often made needlessly complex by the mechanics of reconciling the entity result with the aggregate theory.

41. ABA Report, supra note 2, at 124.

42. The Uniform Partnership Act Revision Subcommittee of the Committee on Partnerships and Unincorporated Business Organizations recommends the following:

(i) Increased emphasis on the entity theory. This is reflected in a number of sections. The two most significant are the proposed revisions to section 25 limiting a partner's rights in specific partnership property to the right to use such property in the conduct of the partnership business and a new short form partnership filing requirement similar to that required for limited partnerships under the 1985 RULPA amendments. . . . A third important recommendation is specific authorization for a partnership agreement to contain a provision that prevents a technical dissolution if the remaining partners agree to buy out the interest of a withdrawing partner. A fourth related change is a recommendation for a new section that will specifically authorize a partnership to sue and be sued in its own name. It is also recommended that language be included which makes it clear that a partner who steals money from a partnership can be guilty of embezzlement, fraud, and related crimes. Finally, the recommendation that a creditor with a judgment against the partnership must exhaust his collection remedies against the partnership before seeking to enforce the judgment against the individual assets of the partners also reflects the increased emphasis on the entity theory.

ABA Report, supra note 2, at 124-25.

43. Many in the legal profession seem unaware of the tenancy in partnership or its significance. At the extreme, see R. Cunningham, W. Stoebuck & D. Whitman, Law of Property 196 (1984) ("The tenancy in partnership—a modified form of tenancy in common—has now been eliminated in all states by the adoption of the Uniform Partnership Act.").

treated as an independent, almost tangible entity, that stands firmly between its assets and the partners. The partner has no right to possess partnership property for nonpartnership purposes. She does have an equal right with other partners to possess partnership property for partnership purposes, but this right "is not assignable except in connection with the assignment of rights of all the partners in the same property." Similarly, "[a] partner's right in specific partnership property is not subject to attachment or execution, except on a claim against the partnership."

In a very real sense, the effect of the tenancy in partnership is to cut off the individual partner from partnership assets. Indeed, the Uniform Act provides that the interest of the partner is not in the underlying partnership assets, but in the partnership entity: "A partner's interest in the partnership is his share of the profits and surplus, and the same is personal property." Just as the property interest of shareholders is viewed as being in their shares, which are their contracts of residual ownership, a partnership interest is seen as a separate asset and one that is classified as personal property.

The drafters of the Uniform Act had several important objectives to be served by the definition of the tenancy in partnership. The first was the general goal of simplification, which also is frequently the goal when an entity model is adopted for federal income tax purposes. The second was to incorporate selected features of the law of joint tenancy into the law of partnership. For example, when a joint tenant dies, the surviving joint tenants succeed to the interest of the deceased tenant in whatever property was held in the joint tenancy.

To summarize joint tenancy:

A second form of concurrent ownership, an ancient part of common-law jurisprudence known as "joint tenancy," is rooted in the concept that the cotenants comprise, for at least one purpose, not a number of individuals, each owning an undivided interest, but a corporate unity—a singular legal entity which owns the property. The consequence of this is that joint tenancy involves what is termed "right of survivorship." This signifies that upon the death of one joint tenant no interest can be transferred from him to any other person by testate or intestate succession. The surviving joint tenants (if two or more survive) continue to comprise the unity or entity which owns the property, and eventually the one who lives longest comprises the unit alone and is therefore sole owner. [T]he concept is that upon the death of a joint tenant he simply ceases to be part of the owning entity—i.e., no interest is "transferred" from him to anyone . . .

ers of the Uniform Act felt that "[t]he incident of survivorship fits in with the necessities of partnership. On the death of a partner, the other partners and not the executors of the deceased partner should have a right to wind up partnership affairs." The third goal was to lay the foundation for a simplified procedure in those cases in which the separate creditor of one partner wished to secure satisfaction out of his debtor's interest in the partnership. The basic policy judgment was that particular pieces of partnership property, and potentially, the very business of the partnership, should not be jeopardized by every claim of separate creditors. Thus, the Uniform Act was drafted so that no partner has any interest in specific partnership assets for her own personal purposes; she has nothing to convey voluntarily, nor can her personal creditors force such a conveyance. Rather, her interest in the partnership is her share of the profits and surplus, and it is against this interest that her separate creditors may seek a charging order.

There seems to be a consensus that the tenancy in partnership reaches the basic right result but does so awkwardly. The statute begins with a broad declaration that the partners are coowners of partnership property. Following that statement, however, is a series of specific provisions that strip the partners of the usual incidents of ownership. As one commentator has put it, "under the U.P.A. individual partners own the partnership property in theory, but all the incidents of ownership are vested in the partnership." The tenancy in partnership is perhaps the most telling example of the statute's adoption of an entity solution with a concurrent insistence that it be stated in aggregate terms. The Commissioners should consider whether the Uniform Act would be clarified and simplified by a direct statement that the partnership, like a corporation, owns its assets, and that individual partners have no more claim to those assets than do shareholders to corporate assets.

B. Dissolution and Delectus Personae

Several important questions remain after the initial decision to give the partnership first claim to the assets of the business. When may the assets be pulled from the partnership? When does the partnership re-

53. *Id.* § 28 at 358. "The practical effect of these interpolations into the common law was to impound firm assets and deprive the individual partners of any control over them except in so far as they were dealing with them on behalf of the firm as a unit." Commissioner v. Lehman, 165 F.2d 383, 385 (2d Cir.), cert. denied, 334 U.S. 819 (1948).
relationship end, voluntarily or not? When the relationship does end, what are the consequences? When may a partner end his continuing exposure to personal liability for the actions and deficiencies of his fellow partners? More narrowly, when may the dissatisfied holder of a partnership interest insist on being cashed out? May the dissatisfied partner demand that the partnership assets be liquidated, the partnership liabilities satisfied and the surplus distributed? Or, may the satisfied partners continue the business if they buy out the interest of the dissatisfied partner for its fair value? Or, may they consider the dissatisfied partner's investment as locked in for as long as he promised or for some other period? Two concepts basic to a discussion of these questions are *delectus personae* and dissolution.

The term *delectus personae*, meaning choice of the person, has long been used to refer to the rule that each of the parties involved must intend to enter into a partnership relationship. This notion is embodied in the Uniform Act's rule that one cannot "become a member of a partnership without the consent of all the partners."\(^\text{55}\)

*Delectus personae* operates mainly to keep out of an existing partnership someone who receives an interest in the firm by assignment or inheritance. However, the necessary consent of the other persons may be given or waived by conduct. Or they may give it in advance by their agreement, say by providing for freely transferable interests. Or they may delegate to some of their number (say a managing partner) the authority to consent for all.\(^\text{56}\)

Given the personal liability of partners for each other's conduct, it makes sense that new partners cannot be "forced" on the membership. On the other hand, a partner's interest is assignable even though an assignee does not become a partner without the consent of the other partners.\(^\text{57}\) The assignment of a partner's interest does not of itself cause a dissolution of the firm or entitle the assignee to participate in management, but it does entitle him "to receive in accordance with his contract the profits to which the assigning partner would otherwise be entitled."\(^\text{58}\)

Dissolution is probably the most confusing concept and area in all of partnership law. In this respect, little has changed since the Uniform Act was drafted. Lewis felt the confusion of his day came about because the term dissolution had no agreed-upon meaning in the part-

\(^{55}\) *Unif. Partnership Act* § 18(g), 6 U.L.A. 213 (1914).

\(^{56}\) *Crane & Bromberg*, supra note 29, at 44.


\(^{58}\) *Id.*
nership context, once stating, "[t]he subject of the dissolution and winding up of a partnership is involved in considerable confusion principally because of the various ways in which the word 'dissolution' is employed." 59

Because of the assumption that a lack of uniform terminology was the problem, the solution adopted in the Uniform Act is to define more precisely what is meant by dissolution. The Uniform Act's definition of dissolution has two basic parts: the first states what dissolution is; the second states what dissolution is not. Dissolution is defined to be "the change in the relation of the partners caused by any partner ceasing to be associated in the carrying on as distinguished from the winding up of the business." 60 On the other hand, dissolution is distinguished from winding up and termination: "On dissolution the partnership is not terminated, but continues until the winding up of partnership affairs is completed." 61 The Official Comment explains that "dissolution designates the point in time when the partners cease to carry on the business together; termination is the point in time when all the partnership affairs are wound up; winding up, the process of settling partnership affairs after dissolution." 62 The Uniform Act definition reflects an aggregate conception that a partnership consists not of a business that continues despite occasional or even frequent changes in membership, but of a very specific cast of characters. The basic conception is that whenever one of the cast of characters leaves, the partnership dissolves. This aggregate concept of dissolution, coupled with the notion that no person can be forced to remain a partner, led to the basic rule that any partner has the power to dissolve the partnership at any time, even if to do so would violate the partnership agreement. 63

Dissolution and its consequences remains an extremely troublesome area despite the new definitions. The ABA Report recommends sixty-six changes to the dissolution provisions of the Uniform Act. 64 One

59. Lewis, supra note 5, at 626-27.
60. UNIF. PARTNERSHIP ACT § 29, 6 U.L.A. 364 (1914).
61. Id. § 30 at 367.
62. Id. § 29 comment at 365.
63. Id. § 31(2) at 376.
64. The summary of those 66 recommendations is as follows: In addition to specific authorization for a partnership agreement to prevent a technical dissolution by authorizing a buyout of a withdrawing partner's interest, the most significant recommendations are:
   (a) delete bankruptcy of a partner as a cause of dissolution or, alternatively, clarify whether there should be a distinction for dissolution purposes between a liquidation proceeding and a rehabilitation or reorganization proceeding;
   (b) specifically state that the admission of an additional partner (as opposed to the
basic problem is that the Uniform Act leaves uncertainty both about when dissolution takes place and about its consequences. As the leading text on partnership puts it:

The statute is imprecise, not in the relative meaning of the three phrases, but in the incomplete coordination between the general definition of dissolution (in terms of a partner ceasing to be associated) and the specific causes of dissolution. Thus there are dissolutions not covered by specific causes and disassociations of partners which are not dissolutions. Moreover, the definition [sic] confuses cause and effect.\footnote{65}

Retirement is an example of a cause for dissolution that is not specifically mentioned in the sections listing the causes of dissolution, although it can be inferred as a cause from those that are listed.\footnote{66}

admission of a replacement partner) does not cause a dissolution;
(c) eliminate losses as an independent ground for court ordered dissolution (A court would still have discretionary authority to dissolve a partnership on this basis, however);
(d) eliminate any right of an assignee of a partner to obtain a court ordered dissolution;
(e) specifically authorize a court in a dissolution suit to order remedies other than dissolution (e.g., damages, attorneys’ fees, etc.);
(f) authorize the non-withdrawing partners to continue the partnership after dissolution and, if they agree to do so within ninety days of a partner’s withdrawal, limit the withdrawing partner’s rights to receiving the fair value of his capital and his share of undistributed profits less any provable damages;
(g) specifically authorize a cause of action for breach of fiduciary duty by the remaining partners against a wrongfully dissolving or expelled partner;
(h) eliminate the mandatory exclusion of goodwill from the value to be paid to a wrongfully dissolving partner; and
(i) specifically authorize for the liquidating partners to take appropriate action to preserve the going concern value of the partnership for a reasonable time.

\textit{ABA Report, supra} note 2, at 125-26.

\footnote{65.} \textsc{Crane \& Bromberg, supra} note 29, at 416-17 (footnotes omitted). The authors note that failure to furnish additional funds is a dissolution not covered by specific causes. In addition, “Retirement is an obvious cause of dissolution not specified, although it may fall within one of the specific causes. Admission of a new partner is not specified as a cause although it is often said to be. The better view is that it is not.” \textit{Id.} at 417 n.3.

\footnote{66.}

\textbf{§ 31. Causes of Dissolution}

Dissolution is caused:

(i) Without violation of the agreement between the partners,
(a) By the termination of the definite term or particular undertaking specified in the agreement,
(b) By the express will of any partner when no definite term or particular undertaking is specified,
(c) By the express will of all the partners who have not assigned their interests or suffered them to be charged for their separate debts, either before or after the termi-
Death, on the other hand, is a dissociation from the partnership that may not result in dissolution.67 Most basically, the causes and effects of dissolution are confused.68

The Uniform Act contains several provisions that attempt to define the consequences of dissolution. Section 33 concerns the effect of dissolution on the authority of a partner to act for the partnership. It establishes the basic proposition that, "[e]xcept so far as may be necessary to wind up partnership affairs or to complete transactions begun but not then finished, dissolution terminates all authority of any partner to act for the partnership."69 The section then acts as a switchboard to direct the reader to additional rules contained in section 34, dealing with the rights of partners to contribution from their fellows after dissolution,70 and section 35, dealing with the power of a partner to bind the partnership to third persons after dissolution.71 Section 36 addresses the effect of dissolution on the existing liability of a partner, including the general rule that dissolution "does not of itself discharge the existing liability of any partner."72 Section 37 provides the general rule that the partners who have not wrongfully dissolved have the

nation of any specified term or particular undertaking,

(d) By the expulsion of any partner from the business bona fide in accordance with such a power conferred by the agreement between the partners;

(2) In contravention of the agreement between the partners, where the circumstances do not permit a dissolution under any other provision of this section, by the express will of any partner at any time;

(3) By any event which makes it unlawful for the business of the partnership to be carried on or for the members to carry it on in partnership;

(4) By the death of any partner;

(5) By the bankruptcy of any partner or the partnership;

(6) By decree of court under section 32.

Unif. Partnership Act § 31, 6 U.L.A. 376 (1914). Section 32 provides for dissolution by decree of court, distinguishing between applications for dissolution by a partner and those made by a purchaser of a partnership interest. Id. § 32, at 394.

67. See Crane & Bromberg, supra note 29, at 417 n.4. The authors cite the death of a partner when the agreement specifies no dissolution, as an example of a disassociation that is not a dissolution. In some places this result has been reached by case law and in others it is statutory:

Apparently this result is reached in cases of death and all other disassociations by Ark. Stats. § 65-129 which appends to U.P.A. § 29 "provided that this change in the relation of the partners shall not effect a dissolution of the partnership in contravention or violation of the agreement between the partners."

Id.

68. The ABA Report recommends that, rather than being eliminated, the general definition of dissolution be tied more closely to the specific causes of dissolution. It recommends that § 29 be amended to provide as follows: "Dissolution is caused in accordance with sections 31 and 32." ABA Report, supra note 2, at 161.

70. Id. § 33(1)(b) at 424.
71. Id. § 33(2).
72. Id. § 36(1) at 436.
right to wind up,73 and section 38 discusses the rights of partners to the application of partnership property on dissolution.74 Section 39 concerns the rights of the parties when the partnership is dissolved for fraud or misrepresentation,75 and section 40 provides the rules for settling the accounts among partners after dissolution.76 Of all these provisions, the most controversial is section 38, which governs the rights of a partner to be cashed out on dissolution. The rights of the dissatisfied partner under section 38 are significantly different from the rights of the dissatisfied corporate shareholder.

C. Rights of the Dissatisfied Partner

Section 38 is said to create a distinction between wrongful and non-wrongful dissolution. The basic rule on non-wrongful dissolution is contained in section 38(1):

When dissolution is caused in any way, except in contravention of the partnership agreement, each partner, as against his co-partners and all persons claiming through them in respect of their interests in the partnership, unless otherwise agreed, may have the partnership property applied to discharge its liabilities, and the surplus applied to pay in cash the net amount owing to the respective partners.77

This provision states the consequences of the rule that, when no definite term or particular undertaking is "specified" in the partnership agreement, any partner may dissolve at will without violating the agreement.78 This right to force a liquidation of all partnership assets in discharge of all partnership liabilities may be referred to as the "full liquidation" right.

The Uniform Act sets out a different set of rules in the case of a wrongful dissolution, and distinguishes the rights of the wrongful dissolver from those of the "innocent" partners. Section 38(2) provides for the rights of the innocent partners as follows:

When dissolution is caused in contravention of the partnership agreement the rights of the partners shall be as follows:

73. Id. § 37 at 444.
74. Id. § 38 at 456.
75. Id. § 39 at 467.
76. Id. § 40 at 468.
77. Id. § 38(1) at 456. Section 38(1) also makes specific provision for the bona fide expulsion of a partner: "But if dissolution is caused by expulsion of a partner, bona fide under the partnership agreement and if the expelled partner is discharged from all partnership liabilities, either by payment or agreement under section 36(2), he shall receive in cash only the net amount due him from the partnership." Id.
78. Id. § 31(1)(b) at 376.
(a) Each partner who has not caused dissolution wrongfully shall have,

I. All the rights specified in paragraph (1) of this section [full liquidation rights], and

II. The rights, as against each partner who has caused dissolution wrongfully, to damages for breach of the agreement.

(b) The partners who have not caused the dissolution wrongfully, if they all desire to continue the business in the same name, either by themselves or jointly with others, may do so, during the agreed term for the partnership and for that purpose may possess the partnership property, provided they secure the payment by bond approved by the court, or pay to any partner who has caused the dissolution wrongfully, the value of his interest in the partnership at the dissolution, less any damages recoverable under clause (2a II) of this section, and in like manner indemnify him against all present or future partnership liabilities.79

The corollary rights of a wrongful dissolver are separately stated.80 If the “innocent” partners do not continue the business, the wrongful dissolver has a right to a full liquidation and distribution of his share of surplus, minus any damages he owes for his breach of the partnership agreement. If the innocent partners do continue the business, the wrongful dissolver has the right to have the value of his interest, less damages caused by the dissolution, “ascertained and paid to him in cash, or the payment secured by bond approved by the court, and to be released from all existing liabilities of the partnership; but in ascertaining the value of the partner’s interest the value of the good-will of the business shall not be considered.”81

Although courts, almost without exception, hold that any partner has the power to dissolve at any time,82 at least one recent case has

79. Id. § 38(2) at 456.
80. Id. § 38(2)(c).
81. Id. § 38(2)(c)II at 457.
82. Many decisions reached this result even prior to the Uniform Act:

No partnership can efficiently or beneficially carry on its business without the mutual confidence and cooperation of all the partners. Even when, by the partnership articles, they have covenanted with each other that the partnership shall continue for a certain period, the partnership may be dissolved at any time, at the will of any partner, so far as to put an end to the partnership relation and to the authority of each partner to act for all; but rendering the partner who breaks his covenant liable to an action at law for damages, as in other cases of breaches of contract.


[E]ach partner has a power to dissolve the connection at any time, notwithstanding any convention to the contrary. . . . [T]he power results from the nature of the association. . . . [I]t is for the public interest that no partner should be obliged to continue in such a partnership against his will, inasmuch as the community of goods in such a
suggested that certain partnerships may indeed be made indissoluble. In *Infusaid Corp. v. Intermedics Infusaid, Inc.*, the First Circuit noted the "wealth of precedent to the effect that a court cannot enjoin the dissolution per se of a partnership." Nevertheless, the court stated that the cases cited all had a strong personal services flavor, and refused to assume that personal services were an important ingredient in the case at hand. After noting what it characterized as a "strong presumption against specific performance of a joint venture or partnership agreement," the court nevertheless suggested an exception was appropriate:

> Where all parties to the agreement are corporations and there has been a dissolution per se of the relationship, however, and legal remedies have explicitly been found inadequate, a court may order specific performance of the agreement if the relationship is found to be without a significant personal service component. That is, if the joint venture or partnership can be maintained as an ongoing, profit-making concern without obliging any officer or director of the corporation that per se dissolved the relationship "to continue in such a partnership against his will," then specific performance may be ordered, again assuming the inadequacy of a legal remedy. By "specific performance" in this context we mean that the district court may order the corporate co-venturers to continue the business together according to the terms of the joint venture agreement.

In light of the long history of the free dissolvability of partnerships, *Infusaid* is a striking development that has already excited scholarly comment suggesting that partners should be permitted to contract away the power to dissolve.

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3 J. Kent, *Commentaries on American Law* 56 (O. Holmes, Jr. 12th ed. 1873) (citations omitted).

83. 739 F.2d 661 (1st Cir. 1984).
84. Id. at 668.
85. Id. at 669.
86. Id. (citations omitted).
87. One commentator writes:
Because an agreement concerning duration is normally reached as a method of stabilizing a partnership, it should be given just that effect. If permitted to bargain effectively on this issue, partners most concerned with the adverse consequences of an early dissolution could pay the price for, and enjoy the benefits of, stability. Partnership law can facilitate this objective by denying a partner the unilateral power to dissolve a partnership by express will prior to the expiration of the term previously accepted by that partner. An agreement concerning duration, in short, should effectively deny a partner the power to unilaterally cause a premature dissolution through an expression of will. If cause exists, the dissatisfied partner may seek a decree of dissolution.

The Commissioners should consider whether the dissolution provisions of the Uniform Act should be changed to give at least some partnerships greater stability.\textsuperscript{88} Consider first the full liquidation right that exists unless there is an agreement to the contrary. It is an extremely powerful remedy. Some have suggested that it is too powerful a remedy and that, to avoid its consequences, courts struggle mightily to "find" oral or implicit agreements to continue for a definite term or until the expiration of a particular undertaking.\textsuperscript{89} The Commissioners should consider whether this remedy ought be continued or how it should be modified. Consider next the rules that should apply when there is an agreement to continue for a stated period or the accomplishment of a stated purpose—the \textit{Infusaid} situation. Why should a dissatisfied partner be entitled to a buyout of his partnership interest at any time? Is his protection too great when compared with that offered his fellow partners? Should the rights of the dissatisfied partner vary depending on whether the source of his dissatisfaction is inside the partnership or from pressures external to the partnership?

If the dissolution power is to be confined, the question becomes what lesser remedies are available to the dissatisfied participant. Subchapter E of the Model Statutory Close Corporation Supplement to the Model Business Corporation Act\textsuperscript{90} is particularly instructive. Section 40\textsuperscript{91} lists situations in which the shareholder of a statutory close corporation may petition a court for relief. Section 41,\textsuperscript{92} entitled "Ordinary Relief," provides that a court may award any one or more of a number of types of relief, including the performance or set aside of any corporate action, the change of corporate articles or bylaws, the removal or appointment of any director or custodian, an accounting, and the payment of dividends or damages. If the court finds that the ordinary relief described in section 41(a) is or would be inadequate or inappropriate, it may order the corporation dissolved under section 43\textsuperscript{93} unless the corporation or one or more of its shareholders purchases all the shares of the dissatisfied shareholder for their fair value and on terms described under section 42(b).\textsuperscript{94} Although the merits of

\begin{footnotesize}


\textsuperscript{90.} \textit{MODEL STATUTORY CLOSE CORP. SUPP.} §§ 40-43 (1983).

\textsuperscript{91.} \textit{Id.} § 40.

\textsuperscript{92.} \textit{Id.} § 41.

\textsuperscript{93.} \textit{Id.} § 43. \textit{See id.} § 41(a).

\textsuperscript{94.} \textit{Id.} § 42(b).
\end{footnotesize}
these particular provisions are of course debatable, the Uniform Act might be substantially improved by similar provisions describing a range of remedies short of full liquidation or buyout.

IV. DUTIES OF LOYALTY AND CARE

The Uniform Act provides that "[e]very partner must account to the partnership for any benefit, and hold as trustee for it any profits derived by him without the consent of the other partners from any transaction connected with the formation, conduct, or liquidation of the partnership or from any use by him of its property." 95 Although a basic purpose of this provision was to give excluded partners priority over the personal creditors of the disloyal partner as to traceable usurped assets, 96 it is also generally seen as the basic statutory embodiment of the fiduciary role of partners as among themselves. The fiduciary duties begin when the parties first become partners and continue even after dissolution through the process of winding up. 97

At the heart of the fiduciary duties among partners is each partner's duty to refrain from appropriating a "partnership opportunity." One leading text has described partnership opportunity to include "an activity necessary or clearly related to the partnership's operations, one offered to or learned about through the partnership, and one developed with partnership funds and facilities." 98 The duty to refrain from diverting a partnership opportunity continues even after the partnership is dissolved. If it did not, a falling out could be staged to effect a diversion of a partnership opportunity. 99

Case law indicates that the duty of loyalty is both vague and powerfully stated. It apparently varies with the circumstances, and is partic-

96. An explanation of this situation is offered by the Official Comment:
A, B and C are partners; A, as a result of a transaction connected with the conduct of the partnership, has in his hands, so that it may be traced, a specific sum of money or other property. A is insolvent. Is the claim of the partnership against A a claim against him as an ordinary creditor, or is it a claim to the specific property or money in his hands? The words "and to hold as trustee for the partnership any profits" indicate clearly that the partnership can claim as their own any property or money that can be traced.
Id. § 21 comment.
97. See generally Crane & Bromberg, supra note 29, at 389-97.
98. Id. at 391 (citations omitted).
99. "Fiduciary duties are among the most important aspects of partnership. . . . Without the protection of fiduciary duties, each [partner] is at the others' mercy." Id. at 389. "Partners are not relieved of fiduciary duties by strained relations. . . . If this were true, 'a designing fiduciary could easily bring about such relations to set the stage for a sharp bargain.'" Id. at 394 (footnotes omitted).
ularly strict in the case of a managing partner. *Meinhard v. Salmon* 100 is generally considered the classic statement of the fiduciary duties of a managing partner, even though the case itself is not based on an explicit finding that a partnership existed. Salmon was a "real estate operator" who acquired a twenty-year lease of the Hotel Bristol. The lease required Salmon to spend a large sum on improvements necessary to adapt the structure to use for offices and retail outlets. These improvements were to be treated as accretions to the land. One month later, Salmon entered into a written "joint venture" agreement with Meinhard, a "woolen merchant," which provided that Meinhard was to pay Salmon half of the monies required "to reconstruct, alter, manage and operate the property." 101 In return, Salmon was to pay Meinhard forty-percent of the net profits for the first five years and fifty-percent for the years thereafter. Any losses were to be borne by them equally. Salmon, however, was to have sole power to manage and operate the building. Indeed, it appears that the lessor was not even aware of Meinhard's existence. 102 The venture between Salmon and Meinhard ultimately proved profitable, "with the result that for each of the investors there came a rich return." 103

By the end of the lease, one Elbridge T. Gerry had become the owner of the reversion and was engaged in the process of site assembly. He owned other property in the neighborhood, including lots adjoining the Hotel Bristol. He planned to lease the entire tract for a long term to someone who would destroy the existing buildings and construct another in their place. After unsuccessfully seeking financing from several other sources, Gerry finally approached Salmon. As a result of the ensuing negotiations, with only four months to run on the lease of the Hotel Bristol to Salmon, Gerry entered into a new lease with a corporation owned and controlled by Salmon. This new lease covered the entire assembled site and required the tenant to construct a three million dollar building. After learning of the new lease, Meinhard made demand that it be held in trust as an asset of his venture with Salmon, and Salmon refused. A referee held that Meinhard did have a right to share in the new lease, and a divided intermediate court of appeals affirmed.

Chief Judge Cardozo exceeded even his own extraordinary abilities at phrasemaking in writing the opinion upholding the decision in favor of Meinhard. He began by stating that Meinhard and Salmon

100. 249 N.Y. 458, 164 N.E. 545 (1928).
101. Id. at 462, 164 N.E. at 546.
102. Id. at 477, 164 N.E. at 552 (Andrews, J., dissenting).
103. Id. at 462, 164 N.E. at 546.
"were coadventurers, subject to fiduciary duties akin to those of partners," but that the "heavier weight of duty" rested on Salmon.\textsuperscript{104} "He was a coadventurer with Meinhard, but he was a manager as well."\textsuperscript{105} He continued with language that has become among the most quoted in partnership law: \textit{ }

Joint adventurers, like copartners, owe to one another, while the enterprise continues, the duty of the finest loyalty. Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the marketplace. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty. . . . Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd.\textsuperscript{106}

Judge Cardozo stated it was inappropriate for Salmon to silently exclude his coadventurer from an opportunity that was an incident of their enterprise. "No answer is it to say that the chance would have been of little value even if seasonably offered. Such a calculus of probabilities is beyond the science of the chancery."\textsuperscript{107} He stated that a constructive trust was to be applied to subordinate "preference of self" to loyalty to others. Finally, he explained that the decision was based neither on a finding of bad faith by Salmon nor on a finding of the ineluctability of Meinhard's claim:

We have no thought to hold that Salmon was guilty of a conscious purpose to defraud. Very likely he assumed in all good faith that with the approaching end of the venture he might ignore his coadventurer and take the extension for himself. He had given to the enterprise time and labor as well as money. He had made it a success. Meinhard, who had given money, but neither time nor labor, had already been richly paid. There might seem to be something grasping in his insistence upon more. Such recriminations are not . . . without their force if conduct is to be judged by the common standards of competitors. That is not to say that they have pertinency here. Salmon . . . was much more than a coadventurer.

\textsuperscript{104} Id.
\textsuperscript{105} Id.
\textsuperscript{106} Id. at 463-64, 164 N.E. at 546 (citations omitted).
\textsuperscript{107} Id. at 466-67, 164 N.E. at 547-48.
He was a managing coadventurer. For him and for those like him the rule of undivided loyalty is relentless and supreme.\textsuperscript{108} 

At one level, it seems hard to argue with the broad proposition that a managing partner must not take advantage of his superior knowledge and control to divert a partnership opportunity.\textsuperscript{109} At another, the correctness of the result is less than obvious if a "grasping" inactive partner has been victorious at the expense of an active partner who has acquitted himself "in all good faith." Judge Andrews, in whose dissent two other judges joined, felt that Salmon’s fiduciary duty should be confined to opportunities "within the scope" of the original joint venture. To the three dissenters, that original venture was designed "to exploit a particular lease," and was never intended to be expanded "into a far greater undertaking lasting for many years."\textsuperscript{110} The Uniform Act would be improved if it clarified the basic relationship between fiduciary duties and the parties’ intent and offered greater guidance on the rules that apply in duty of loyalty situations.\textsuperscript{112}

A related series of questions concerns the extent to which the fiduciary duties of managing or other partners can be drafted away. If the basic purpose of the fiduciary duties is to protect the presumed legitimate expectations of the parties, the parties should have great latitude to define those expectations by agreement. On the other hand, waivers with respect to specific contemporaneous transactions may present

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\item[108.] Id. at 467-68, 164 N.E. at 548 (citations omitted).
\item[109.] Many cases are equally strict in resolving all doubt against managing partners. For example, one court wrote:

[They stand] in a higher fiduciary relationship with the other partners than partners usually occupy. The burden is upon the managing partner to dispel all doubts concerning his conduct toward the partnership or the other partners, and if he is unable to carry this burden all doubts will ordinarily be resolved against him.


\item[110.] A higher authority may have decided that Meinhard was awarded too much. The new building was not completed until after the stock market crashed and the depression was underway. Meinhard died, and left his heirs a share of losses, not profits:

The old building had been profitable but by the time the new one was ready in 1931 the fall in the value of real estate made its operation impossible except at a loss, and Salmon and Meinhard were either compelled to pay the deficits, or to suffer the property to become unoccupied and perhaps to pass out of their hands. Meinhard had died and his estate paid to Salmon his part of the deficits . . . .

Salmon v. Commissioner, 126 F.2d 203, 204 (2d Cir. 1942).

\item[111.] Meinhard, 249 N.Y. at 478, 164 N.E. at 552.

\item[112.] See the more specific statements of the duty of loyalty in Restatement (Second) of Agency §§ 387-394 (1958).
\end{enumerate}
\end{footnotesize}
fewer problems than do waivers of unidentified future transactions.\textsuperscript{113} \textit{Riviera Congress Associates v. Yassky},\textsuperscript{114} citing \textit{Meinhard} for the proposition that "a managing or general partner of a limited partnership is bound in a fiduciary relationship with the limited partners,"\textsuperscript{115} suggests that some fiduciary duties can be waived prospectively. Five out of approximately 350 limited partners were permitted to bring a derivative suit on behalf of the partnership. Although the defendants were the four general partners of the limited partnership, they were sued not in that capacity but in their capacity as parties who had assumed a rental obligation to the partnership. The defendants resisted the action for rent on the ground that they, in their capacity as general partners of the plaintiffs' partnership, had released themselves from the rent liability. The plaintiffs countered that the release was invalid because it constituted self-dealing in violation of their fiduciary obligations as general partners.\textsuperscript{116}

It would have been difficult to dispute the fact of self-dealing, given the general partners "leased the motel to their own thinly capitalized corporation and then consented" to a series of assignments to other entities they owned or controlled. The question was whether the self-dealing was inappropriate under the circumstances. "Ordinarily," said the court,

such self-dealing would render the defendants incapable, as general partners . . . from releasing themselves from liability on the lease . . . . However, partners may include in the partnership articles practically "any agreement they wish" and, if the asserted self-dealing was actually contemplated and authorized, it would not, ipso facto, be impermissible and deemed wrongful . . . . [T]he limited partners were fully apprised in the prospectus that the defendant general partners intended to lease the premises to their own [thinly capitalized] corporation . . . . This clear statement of purpose has the effect of "exonerating" the defendants, at least in part, "from adverse inferences which might otherwise be drawn against them" simply from the fact that they dealt with themselves.\textsuperscript{117}

The partner's duty of loyalty can be distinguished from his duty of care.\textsuperscript{118} Although the Uniform Act has a number of provisions that

\begin{itemize}
  \item \textsuperscript{114} 18 N.Y.2d 540, 223 N.E.2d 876, 277 N.Y.S.2d 386 (1966).
  \item \textsuperscript{115} \textit{Id.} at 547, 223 N.E.2d at 879, 277 N.Y.S.2d at 392.
  \item \textsuperscript{116} \textit{Id.} at 548, 223 N.E.2d at 877-78, 277 N.Y.S.2d at 390.
  \item \textsuperscript{117} \textit{Id.} at 548, 223 N.E.2d at 880, 227 N.Y.S.2d at 392-93 (citations omitted).
  \item \textsuperscript{118} See, e.g., Bassan v. Investment Exch. Corp., 83 Wash. 2d 922, 928, 524 P.2d 233
\end{itemize}
can be seen as embodying a duty of loyalty,\textsuperscript{119} it contains no direct statement of a duty of care. Although the duty of care is generally described as one of reasonableness, the concept remains relatively undeveloped. What little case law there is in the partnership context suggests that partners will not be liable for breach of a duty of care unless they are at least grossly negligent.\textsuperscript{120} Although there is much greater discussion of the duty of care in the corporate area, there is a similar paucity of cases imposing liability on directors simply for breach of a duty of care.\textsuperscript{121} Some of the most recent developments in the corporate area, however, have generated significant discussion of the appropriate statutory treatment of the duty of care.\textsuperscript{122}

There is a wide range of questions that should be considered in the revision of the Uniform Act, some of them very fundamental. Should a new partnership act explicitly define duties of loyalty and care that will govern the partners in the absence of agreement? Should those duties be imposed on all partners or only on managing partners? May the presumptive duties be drafted away or indemnified against? The

\textsuperscript{119} See, e.g., \textsc{Unif. Partnership Act} § 19, 6 U.L.A. 254 (1914) (duty to provide access to partnership books); \textit{id.} § 20 at 256 (duty to inform); \textit{id.} § 21 at 258 (partners accountable as fiduciaries); \textit{id.} § 22 at 284 (right to an account).

\textsuperscript{120} One commentator notes:

An examination of the particular facts in a number of these cases reveals . . . that courts are excusing as "mistakes" what would be regarded as negligent conduct in other contexts. The amount of negligence which will be excused has not been definitely determined by the courts, but more recent decisions interpreting the duty of care indicate a trend toward a gross negligence standard.

\textsuperscript{121} See Lee, Limiting Corporate Directors' Liability: Delaware's Section 102(b)(7) and the Erosion of the Directors' Duty of Care, 136 U. Pa. L. Rev. 239, 240 n.3 (1987) (there is a "paucity of cases in which a director's negligent actions, uncomplicated by any showings of bad faith or self-dealing, formed the basis of a finding of personal liability").

\textsuperscript{122} Lee continues:

Recently, a reawakening of the duty of care has broken the relative tranquility of corporate America. That awakening has brought about what many have called a "crisis," real or imagined. The talk of crisis has been sparked by recent well-publicized cases finding directors in breach of their duty of care, and by a concurrent violent swing in the insurance markets making directors' and officers' liability insurance ("D&O insurance") painfully expensive or simply unavailable. . . . These developments, in turn, have sent lobbyists scurrying to state legislative bodies seeking statutory remedies for their woes.

\textit{id.} at 240-41.
relation of the duty of care to the duty of loyalty ought be considered directly in part because there are many situations that can be approached from either duty. The Revised Model Business Corporation Act distinguishes the two by providing separate sections on General Standards for Directors, duty of care, and on Director Conflict of Interest, duty of loyalty. Similarly, the American Law Institute’s Corporate Governance Project continues the distinction. A basic question facing the Commissioners is the extent to which a new partnership statute should directly address these concepts and developments that have been so controversial in the corporate area.

V. Limited Liability

It is today the most ministerial of matters for entrepreneurs to set up a corporation, thereby avoiding the unlimited personal liability imposed on partners. Each state now has a “general incorporation act,” so called because it is a single statute that makes corporations generally available to anyone who follows a purely mechanical procedure. Creating a corporation is similar to what the process for obtaining a driver’s license would be if competency testing were stripped away. The result of one or two secretarial acts is the creation of what is, in the eyes of the law, a separate legal person, of potentially infinite life, that can engage in any lawful business activity. The general incorporation act provides for the relationships among the shareholders themselves, and the fundamental rule that the corporate entity insulates shareholders from liability to the outside world for claims arising from corporate business.

124. Id. § 8.31.
125. The Institute’s discussion of the duty of loyalty begins with the following statement of its relation to the duty of care:
   [B]oth analytically and normatively the principle of loyalty precedes that of due care. Analytically, the principle of loyalty has primacy in that the duty of care entails the principle of loyalty. As stated in § 4.01(a) of Tentative Draft No. 4, the conduct of an officer or director conforms to the duty of care when it is “in good faith, in a manner he reasonably believes to be in the best interest of the corporation . . . .” Normatively, the principle of loyalty to the corporation specifies the direction in which the efforts are to be made that are regulated by the due care requirement.
126. ABA Report, supra note 2, at 151.
General incorporation acts were hotly resisted throughout a large portion of our nation’s history. In the beginning of the nineteenth century, the idea of the large corporation was viewed as vaguely un-American. It sounded too much like advocacy for a return to a royal family, self-perpetuating, aggrandizing and above-the-law, to urge the creation of legal persons, of potentially infinite life, behind whom the wealthy classes could hide, to engage in any activity and accumulate unlimited wealth. Initially, state legislatures refused to create corporations any faster than one at a time; a special statute was required to create each corporation. Shareholder freedom from personal liability was seen as an extraordinary statutory privilege. The personal liability of partners was considered the norm, and extraordinary justification had to be shown for deviating from that norm. The extraordinary justification was often found in the nature of the endeavor. State legislators were more willing to create corporations to insulate shareholders from personal liability for projects that were perceived to be particularly beneficial to the common weal, such as the construction of roads, bridges and barge canals.

Venture capitalists pressed their case for a share in profits without exposure to unlimited personal liability. In 1822, decades before states were willing to pass general incorporation acts, New York and Connecticut passed this country’s first limited partnership statutes. Based on the French Societe en Commandite, the limited partnership acts generally authorized the creation of partnerships with two classes of “partners,” general and limited. This basic approach is a distant antecedent to that used today. General partners were what we normally think of as partners, persons who are unlimitedly personally liable to the contract and tort creditors of the business. Limited partners, on the other hand, were passive investors who could lose their protected status as limited partners if they took part in the control of the business. In short, if the limited partners were truly passive investors, and if they followed a statutorily prescribed procedure for publicly recording their status as passive investors, they would be insulated from personal liability to the creditors of the partnership.

Limited partnership statutes later spread, and limited partnerships became quite popular. However, by the late nineteenth century, interest in limited partnerships began to fade as the corporate form became more freely available. State legislatures had been passing, and then liberalizing, general incorporation acts. Initially, for example, it was common for state statutes to limit how long a corporate charter could last. Like today’s so-called “sunset” legislation, corporate charters were created to expire, for example, after twenty years. Only in time would perpetual corporations become acceptable. There were also lim-
its on the amount of capital any particular corporation could have, because the fear of unlimited accumulations of wealth lingered. Over time, various restrictions were gradually—then rapidly—liberalized, as some states actually competed with each other for success in what came to be perceived as the lucrative business of selling corporate charters.

With the advent of more permissive state incorporation laws, the limited partnership entered a period of relative dormancy that would last until the last half of the twentieth century when, for reasons of federal income tax law rather than state law, it exploded into popular usage. It was in this period of relative dormancy that the Uniform Limited Partnership Act (ULPA)\textsuperscript{127} was drafted. The National Conference of Commissioners on Uniform State Laws approved the ULPA in 1916, just two years after it approved the Uniform Act.

The ULPA replaced the assumptions of the prior law of limited partnerships with two boldly different ones:

First: No public policy requires a person who contributes to the capital of a business, acquires an interest in the profits, and some degree of control over the conduct of the business, to become bound for the obligations of the business; provided creditors have no reason to believe at the times their credits were extended that such person was so bound.

Second: That persons in business should be able, while remaining themselves liable without limit for the obligations contracted in its conduct, to associate with themselves others who contribute to the capital and acquire rights of ownership, provided that such contributors do not compete with creditors for the assets of the partnership.\textsuperscript{128}

The ULPA Official Comment, which is quite brief, does make one fundamental point repeatedly: henceforth, a limited partner, "though in accordance with custom called a limited partner, is not in any sense a partner. He is, however, a member of the association."\textsuperscript{129} The basic pattern of the old laws continued. The limited partner was still required to indicate her limited status on a recorded certificate of limited partnership and refrain from taking part in the control of partnership business.

For decades after the adoption of the ULPA, the limited partnership remained a relatively insignificant form of business association.

\textsuperscript{128} Id. § 1 comment at 564.
\textsuperscript{129} Id.
By the early 1960’s, however, it had become clear that limited partnerships were being classified as partnerships for federal income tax purposes. Limited partners were thus offered limited liability similar to that available in the corporate form, minus the corporate income tax, plus the “pass through” of tax losses available to those who are classified as partners for federal income tax purposes. Because of this attractive combination of advantages, limited partnerships began to proliferate, particularly in depreciable real estate and oil and gas. In 1976, the Conference of Commissioners replaced the bare-bones original act with a new act (1976 Act). Although the 1976 Act was generally viewed as an improvement, it was but one step needed to update the statutory foundation for a form of business organization that had exploded in currency and come to be used in a wide range of sophisticated transactions involving many investors and large sums of money. In 1985, the Conference of Commissioners issued the latest version of the ULPA, the Revised Uniform Limited Partnership Act (RULPA).

The RULPA is dramatically different from the first limited partnership act approved by the Commissioners. It is true that a limited partnership is still formed by filing a certificate of limited partnership. On the other hand, although the name and business address of each general partner must be shown on the certificate, it is no longer necessary to name the limited partners, much less list their contributions. Furthermore, whereas under prior law a limited partner could receive her interest for cash or property but not services, under the

132. Section 201(b) provides:
   (b) A limited partnership is formed at the time of the filing of the certificate of limited partnership in the office of the Secretary of State or at any later time specified in the certificate of limited partnership if, in either case, there has been substantial compliance with the requirements of this section.
Id. § 201(b) at 249.
133. Id. § 201(a)(3).
134. The Official Comment to the RULPA explains:
   The 1985 Act requires far fewer matters to be set forth in the certificate of limited partnership than did Section 2 of the 1916 Act and Section 201 of the 1976 Act. This is in recognition of the fact that the partnership agreement, not the certificate of limited partnership, has become the authoritative and comprehensive document for most limited partnerships, and that creditors and potential creditors of the partnership do and should refer to the partnership agreement and to other information furnished to them directly by the partnership and by others, not to the certificate of limited partnership, to obtain facts concerning the capital and finances of the partnership and other matters of concern.
Id. § 201 comment at 249-50.
RULPA a limited partner may receive her interest for services or for the mere promise to render services in the future. In addition, the RULPA anticipates that limited partners may be given voting rights on a wide range of matters, and strengthens the provisions that protect their limited liability.

There are three basic ways the RULPA enhances the protection of the limited liability of limited partners. First, it expressly imposes a reliance requirement on plaintiffs who pursue the personal liability of limited partners on the ground that they have taken part in the "control" of the partnership business. "If the limited partner participates in the control of the business, he . . . is liable only to persons who transact business with the limited partnership reasonably believing, based upon the limited partner's conduct, that the limited partner is a general partner." Second, the RULPA provides that a limited partner does not participate in control by proposing, approving, or disapproving, by voting or otherwise, one or more of a wide range of matters. Third, the RULPA provides that a wide range of active participations in partnership affairs will not be deemed, singly or in combination, to constitute participation in control. The RULPA abandoned the concept that a limited partner's participation in control is excessive if it is "substantially the same as the exercise of the powers of a general partner." In short, under the new safe harbor provisions, a limited partner can be much more active both in fundamental business decisions and in day-to-day operations than many general partners and still not run afoul of the control limitation.

135. Id. § 101(2) at 230.
136. "Subject to Section 303, the partnership agreement may grant to all or a specified group of the limited partners the right to vote (on a per capita or other basis) upon any matter." Id. § 302 at 281.
137. Id. § 303(a) at 282.
138. Id.
139. Id. § 303(b)(6).
140. Id. § 303(b).
141. REVISED UNIF. LIMITED PARTNERSHIP ACT, 6 U.L.A. 205, 282 (1976) (West Supp. 1987) (amended 1985). Section 303(a) of the 1976 Act provided, in part: "If the limited partner's participation in the control of the business is not substantially the same as the exercise of the powers of a general partner, he . . . is liable only to persons who transact business . . . with actual knowledge of his participation in control." Id. § 303(a). The Official Comment explained: [B]ecause of the difficulty of determining when the "control" line has been overstepped, it was thought it unfair to impose general partner's liability on a limited partner except to the extent that a third party had knowledge of his participation in the control of the business. On the other hand, in order to avoid permitting a limited partner to exercise all of the powers of a general partner while avoiding any direct dealings with third parties, the "is not substantially the same as" test was introduced. Id. § 303 comment at 283.
142. Certain states have enacted provisions even more protective of the right of limited part-
It is unclear how, if at all, the developments in the law of limited partnerships should inform the general partnership statute. For one thing, it seems that the state policy in favor of imposing personal liability on a profit sharer who takes part in the control of an unincorporated business has all but vanished. Why should there continue to be personal liability in the case of general partnerships? What if a system of registration is adopted for general partnerships? Should members of registered partnerships be free from personal liability? Should the law of the "silent partner" be reconsidered? Why impose unlimited personal liability on a silent inadvertent partner if a silent limited partner, indeed, an active limited partner, has no liability? More generally, why should a creditor who has not relied on the personal liability of another ever be able to establish it? Further, and not unrelated, how far have we deviated from the notion that partnerships are informal, personal relationships with each partner participating directly in management? Should the partnership law assume such intimacy and agency authority unless it is drafted away? If voting rights are authorized by statute in the case of a limited partnership, should they also be addressed in the general partnership statute? And, if there are voting rights, haven't we come almost all the way to recognizing that a partnership is an entity with centralized management very much like that in a corporation? Why not, then, consider a range of specific statutory provisions that honestly and directly embrace the entity model? Specific provisions could aim at narrow problem areas facing all partnerships, such as preventing future decisions like *Fairway Development.* More broadly, a wide range of other provisions could accommodate the world of the large partnership and make analogies between partnership and corporate law more accessible.

VI. LESSONS OF PARTNERSHIP TAX LAW

The federal income tax law governing the taxation of partners and partnerships should be considered for two basic reasons. First, the tax law suggests that pragmatism rather than partisanship be brought to the entity/aggregate controversy. Just as there are separate statutes under state law governing corporations and partnerships, there are separate subchapters of the Internal Revenue Code (the Code) governing corporations and partnerships. The tax law of Subchapter K, governing partners and partnerships, is helpful because it indicates a

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pragmatic approach to the entity/aggregate dichotomy. It suggests that there is no need to adopt one theory as the exclusive theory. It suggests, instead, that some questions are best handled with an entity approach whereas others are best, or at least satisfactorily, handled through an aggregate approach. It also suggests that in other cases, the partners themselves may elect either an entity or an aggregate approach. Second, tax law may be the ultimate constraint on the partnership project.

Tension between the entity and aggregate approaches exists in federal income tax law even though none of our general revenue codes has ever taxed partnerships as entities.  

A certain amount of schizophrenia is unavoidable because of the basic structure of the tax law. Although the partnership is not a separate tax-paying entity, it is a separate entity for the purposes of computing, reporting, and allocating the economic and tax consequences of partnership activities. The partnership has its own taxable year and it, rather than the individual partners, makes the basic decisions with respect to the computation of partnership income. The partnership determines, for example, the method of computing depreciation of partnership property, whether to use a cash or accrual method of accounting, and whether to elect to report income under the installment method.  

It is clear that in many cases the entity approach is preferred not so much because it reaches the "right result" but because of its simplicity. At the extreme, the partnership-level audit provisions were the only way the Internal Revenue Service could begin to deal with tax shelter syndications. In other situations, the entity approach is used in a more narrow way to prevent the partners from entering arrange-

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144. The War Revenue Act of 1917 is a notable supplement to the basic revenue code because it imposed an income tax on partnerships as entities:  

Sec. 201. That in addition to the taxes under existing law and under this act there shall be levied, assessed, collected, and paid for each taxable year upon the income of every corporation, partnership, or individual, a tax . . . equal to the following percentages of the net income . . . .  

The tax was based on the ratio of "net income" to "invested capital for the taxable year," and was supplemental to taxes imposed by the Revenue Act of 1916, which provided that "[p]ersons carrying on business in partnership shall be liable for income tax only in their individual capacity." Revenue Act of 1916, Pub. L. No. 64-271, 39 Stat. 756, 762 (1917).

146. Id. § 703(b).
147. Id. § 167.
150. Id. §§ 6221-6231.
ments that could violate basic policies of federal income taxation. For example, certain transactions between a partner and the partnership will be treated as transactions between the partnership and an outsider in order to assure that compensation for services will be reported as ordinary income.\textsuperscript{151}

Other provisions give partners the choice of an aggregate or an entity model. For example, the general rule is that, when a partner purchases his partnership interest, he will not be given a special basis in each of the partnership's assets to reflect the price he paid for his partnership interest.\textsuperscript{152} On the other hand, if the partnership files an election, those who purchase partnership interests may ignore the entity approach and claim they purchased a direct interest in the underlying assets of the partnership. As a result, each partner will be given a special basis in the underlying partnership assets to reflect the price she paid for her partnership interest.\textsuperscript{153} Another example of the choice given partners to opt out of an entity approach and into an aggregate approach is the provision that gives certain partners the opportunity to "elect out" of the partnership provisions of Subchapter K.\textsuperscript{154}

New Uniform Partnership Act provisions should be considered in light of their impact on federal income tax classification. As under state law, intent to be classified as partners is evidence of partnership, but the ultimate "intent" question is not the parties' thoughts concerning how they are classified; the ultimate question is whether they intended to enter a relationship, however denominated, the essence of which is tax partnership.\textsuperscript{155} People can be partners for tax purposes even though their relationship is not one of partnership under state law. Tax classification is determined under the Code and is ultimately independent of state law classification.\textsuperscript{156}

\textsuperscript{151} Id. § 707(a)(2).
\textsuperscript{152} I.R.C. § 743(a) (1982).
\textsuperscript{154} I.R.C. § 761(a) (West Supp. 1988).
\textsuperscript{155} On the matter of intent, the Supreme Court has said that all facts must be considered:
The question is . . . whether, considering all the facts—the agreement, the conduct of the parties in execution of its provisions, their statements, the testimony of disinterested persons, the relationship of the parties, their respective abilities and capital contributions, the actual control of income and the purposes for which it is used, and any other facts throwing light on their true intent—the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise.
Commissioner v. Culbertson, 337 U.S. 733, 742 (1949). For a much more recent case in which the parties were held to be tax partners even though neither they nor their government regulators considered them partners, see Madison Gas & Elec. Co. v. Commissioner, 633 F.2d 512 (7th Cir. 1980), aff'd 72 T.C. 521 (1979).
\textsuperscript{156} Treas. Reg. § 301.7701-1(c) (as amended in 1983).
The Code defines the term "partnership" to include any "syndicate, group, pool, joint venture or other unincorporated organization through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of this title, a corporation or a trust or estate." Thus, the Code defines partnership in the negative, and that is why the category of tax partnership is potentially enormous. Partnership is a residual category. If any unincorporated business group is nothing else for tax purposes (a corporation or trust or estate), it is a partnership. And "partner" is defined to include any member of the group. The "term 'partnership' is broader in scope than the common law meaning of partnership, and may include groups not commonly called partnerships." On the other hand, an organization will not necessarily be deemed a partnership for tax purposes simply because it is classified as some kind of partnership under state law.

Great controversy has surrounded the tax classification of limited partnerships, particularly publicly syndicated and traded partnerships. The present classification regulations, as interpreted by a major tax court decision in which the Service indicated its acquiescence, have made it extremely difficult for any ULPA limited partnership, including one that has a sole corporate general partner, to be treated as anything other than a partnership for tax purposes.

The regulations begin in what seems like a reasonable way by listing:

a number of major characteristics ordinarily found in a pure corporation which, taken together, distinguish it from other organizations. These are: (i) associates, (ii) an objective to carry on business and divide the gains therefrom, (iii) continuity of life, (iv) centralization of management, (v) liability for corporate debts

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157. I.R.C. § 761(a) (West Supp. 1988) (applicable for income tax purposes only). See also id. § 7701(a)(2) (a virtually identical definition that applies to all of Title 26, which includes subtitles relating to income tax, estate and gift tax, employment tax, and procedure and administration).
158. Id. §§ 761(b), 7701(a)(2).
161. Regulations under the Revenue Act of 1916 first took the position that all limited partnerships were taxable as corporations. However, these regulations were soon replaced by regulations that applied a "resemblance" test. For a history of the classification question, see Sexton & Osteen, Classification as a Partnership or an Association Taxable as a Corporation, 24 TUL. TAX INST. 95 (1975). Cf. Heritage Hills v. Zion's First Nat'l Bank, 601 F.2d 1023 (9th Cir. 1979) (holding that a limited partnership composed entirely of corporations was not a corporation for purposes of Chapter XII of the Bankruptcy Act).
limited to corporate property, and (vi) free transferability of interests.162

The regulations also state, without explanation, that in addition to these "major" factors, "other factors may be found . . . which may be significant in classifying an organization as an association, a partnership, or a trust."163 The regulations proceed, however, to make it virtually impossible for any Uniform Act partnership or ULPA limited partnership to be classified as anything other than a partnership for tax purposes.164 They do this in two ways. First, they state that the first two characteristics are common to both partnerships and corporations and that three of the four remaining characteristics must be found before an organization will be classified as a corporation.165 This "numerical supremacy test" provides that, if only two of these remaining four characteristics are present, partnership classification results.166 Second, the regulations define these characteristics in bizarre ways. The regulations are biased toward partnership classification because they are the remnants from the days when the Service was attempting to tax professional associations as partnerships. They remain controversial because they classify as partnerships for tax purposes organizations that look very much like corporations. It was not until December of 1987 that Congress took a different tack by declaring that certain publicly traded limited partnerships are to be taxed as corporations.167

Some of the suggested changes to the Uniform Act appear to bear at least indirectly on the tax classification of partnerships. Continuity of life and free transferability of interests appear to be enhanced by provisions such as those requiring registration of partnerships and those redefining dissolution and its consequences. Centralized management might be strengthened by provisions authorizing voting and limiting the agency of certain partners. None of the changes more broadly discussed, however, would restrict the unlimited personal liability of partners. That personal liability has great significance for federal income tax purposes. Indeed, given that the unlimited personal liability of profit sharers is a policy upon which states seem to place

163. Id.
166. Id.
little or no value, as indicated by their recent liberalization of limited partnership statutes, one wonders whether the tacit concession of the personal liability of partners is in recognition of the fact that the federal tax tail really wags the state organization dog.

VII. Conclusion

Two principal developments should be considered in a reevaluation of the law of partnership. First, the business and investment use of the partnership has changed. The partnership continues to be used in ventures involving family members and small groups of businesspersons, but it is also used in associations of unprecedented size and complexity. The drafters of the original act might have marveled at both the extraordinarily detailed prospectuses attendant publicly syndicated partnerships, and at the fact that single offerings have involved as much as hundreds of millions of dollars. Although by far the greatest number of syndicated partnership offerings are of limited partnerships, general partnerships have also been syndicated, and "privately" held partnerships have increased in size and complexity. Legal and accounting firms with hundreds of partners in offices that necklace the globe command at least part of our attention. Even in small towns, it is common to have partnerships that consist of corporate partners or that have other partnerships or limited partnerships as members. Second, the legal climate has also changed. As a regulatory matter, partnership law now covers many situations that are also regulated by federal or state securities laws. More basically, however, the law of other business organizations has changed.

168. The Empire State Building, for example, was the object of a publicly syndicated offering of units of participation in general partnership interests. The prospectus in that syndication described the investors as "joint venturers" and reflected an opinion of counsel that they would qualify as partners for federal income tax purposes. Empire State Building Associates Prospectus (Oct. 31, 1961), reprinted in 1 S. Rouiac, Syndication Landmarks 105, 117 (1974). It does seem clear that the absence of control of a joint venturer or partner can at least raise a serious question whether she has purchased a security:

A general partnership or joint venture interest can be designated a security if the investor can establish, for example, that (1) an agreement among the parties leaves so little power in the hands of the partner or venturer that the arrangement in fact distributes power as would a limited partnership; or (2) the partner or venturer is so inexperienced and unknowledgeable in business affairs that he is incapable of intelligently exercising his partnership or venture powers; or (3) the partner or venturer is so dependent on some unique entrepreneurial or managerial ability of the promoter that he cannot replace the manager of the enterprise or otherwise exercise meaningful partnership or venture powers.

There are five basic changes in the law of business associations that should be considered in the revision of the Uniform Partnership Act. First, and perhaps of least importance, general incorporation acts have been liberalized and made more flexible. If nothing else, this liberalization indicates the diminishing state policy in favor of personal liability of entrepreneurs. Second, the RULPA has radically liberalized the extent to which limited partners may take part in the control of the business and still retain their limited liability. These changes not only reflect a strong move to the entity theory in the partnership context but also a virtual extinguishment of state policy favoring personal liability for unincorporated profit-sharers. Third, special statutory provisions have been drafted to deal with the subject of the closely-held corporation. These provisions outline the different types of relief courts can award to dissatisfied shareholders. Compared to the current statutory provisions for dissatisfied partners or assignees of partnership interests, these close corporation provisions are much more clear and offer a broader, more even continuum of remedies. Fourth, there has been considerable discussion in the corporate context concerning duties of care and of loyalty—when they arise, when they can be drafted away, and when they can be indemnified against. Particularly if partnerships are to be substituted for corporations because of the new federal income tax regime, the Commissioners ought at least keep these developments in mind. Fifth, and perhaps of greatest importance, the Uniform Act was adopted prior to the imposition of the federal income tax.

The federal income tax law suggests that a pragmatic rather than a doctrinaire approach be taken to the entity/aggregate dichotomy. It also suggests a major reason why partnerships, general or limited, continue at all. The federal tax law presently taxes corporations and partnerships very differently. It refuses to adopt a “check the box” approach that permits business organizations to elect to be taxed consistently according to one model or the other. On the other hand, the tax law permits the effect of an election out of the corporate income tax by the more indirect and cumbersome route of forming an organization that is classified as a partnership under state law. Although tax classification is a matter of federal law and not state law, federal law as a practical matter relies very heavily on state law. One result is that limited partnerships that have no general partners other than corporations are routinely classified not as corporations but as partnerships for federal income tax purposes. After years of controversy surrounding this rule, the only significant inroad is that certain publicly-traded limited partnerships will now be taxed as corporations.169 As a practi-

cal matter, the state law of partnership now provides a foundation for businesses that seek to avoid the corporate income tax. Stated somewhat differently, state law has come to help the federal tax law avoid the appearance of elevating form over substance.\textsuperscript{170}

The present law of general partnerships should continue to deal with the inadvertent partnership and the informal partnership. As in the time of Ames and Lewis, a central task of the statute is to serve as the partnership agreement in the absence of one crafted by the participants. The whole area of dissolution remains as troubled as it was in the time of Ames, if not more so, and requires a careful reconsideration. The Commissioners should consider whether to continue to provide very powerful liquidation remedies for the dissatisfied partner or whether to confine certain partners to less drastic remedies analogous to those provided in close corporation acts. If the power of a partner to compel liquidation is limited, it may then become even more important to have more fully developed notions of the duties of care and loyalty that will provide the basis for lesser remedies. Those duties appear to merit more direct statement than exists under the present act. The Commissioners may wish to consider the extent to which these duties may be drafted away and indemnified against. Recent thinking in the corporate area should inform the discussion.

This article does not mean to suggest that the law of business organizations be rewritten within the confines of a partnership project. On the other hand, it does seem appropriate to observe that, if the law could be written today on a \textit{tabula rasa}, there would not be separate statutes for the partnership, the limited partnership, the corporation and the close corporation. More narrowly, consideration of the general partnership statute might have preceded the revision of the limited partnership statute. On the other hand, given that the Revised Uniform Limited Partnership Act has only recently been completed, receiving at least the initial blessings of the Internal Revenue Service

\textsuperscript{170} The American Law Institute Federal Income Tax Project recently recommended continued reliance on state law classification except in the case of publicly-traded partnerships:

\textbf{PROPOSAL O — PARTNERSHIP CLASSIFICATION}

\textbf{1. GENERAL RULE}

A partnership organized and operated under the Uniform Partnership Act or the Uniform Limited Partnership Act, as either act is substantially in effect in any State, and not publicly traded within the meaning of Paragraph 2 below, shall be treated as a partnership for Federal income tax purposes.

\textbf{2. DEFINITION OF PUBLICLY-TRADED PARTNERSHIPS}

An interest in a limited partnership shall be considered publicly-traded only if at any time in the partnership's existence, interests in the partnership are traded in an established securities market.

for tax classification purposes, the partnership project can proceed to move the general partnership more toward the corporate or entity model without fear of adverse tax consequences.