

MINUTES OF THE SENATE COMMITTEE ON JUDICIARY

The meeting was called to order by Senator Elwaine F. Pomeroy at
Chairperson

10:00 a.m./~~p.m.~~ on February 8, 1983 in room 514-S of the Capitol.

All members were present ~~except~~

Committee staff present: Mike Heim, Legislative Research Department
Mark Burghart, Legislative Research Department

Conferees appearing before the committee:

John Brookens, Kansas Bar Association
Don Paxson, Columbian Securities Corporation
Jon Jossierand, Office of Secretary of State
John Wine, Office of Secretary of State

Senator Gaines moved that the minutes of February 4, 1983, be approved; Senator Werts seconded the motion, and the motion carried.

The chairman explained the written testimony before them is from a person who was going to testify yesterday on Senate Bill 107, was ill and unable to attend the hearing (See Attachment #1).

Senate Bill 106 - Revised Uniform Limited Partnership Act.

The chairman explained the revised uniform limited partnership act had been introduced last year, an interim committee study had been requested, and the interim committee suggested that the bill not be enacted. One reason they were not in favor was because there are a number of amendments to make it workable with the secretary of state's office. The Kansas Bar Association supports the bill. Their legislative counsel has worked with the secretary of state's office to work out the difficulties, which has been done with this bill.

John Brookens stated this proposal is highly technical and highly complex. A copy of his statement is attached (See Attachment #2). He presented several suggestions for changes to the bill, and he will submit these in writing. Mr. Brookens explained the language in the bill is partly from the Delaware act and some of it is verbatim from the uniform act. He reported there are 1,273 Kansas limited partnerships registered with the office of the secretary of state; there are 635 foreign limited partnerships registered. Attachment #3 is a copy of an article by Byron R. Schlosser, entitled "Time To Change Your Act".

Don Paxson testified he is in support of the bill. He said he is interested in having a modern administratively workable bill. He and others worked closely with the secretary of state's office to develop a workable bill. In answer to a question, Mr. Paxson stated an important part of the bill is section (25), on page 17; it is designed to eliminate potential problems with the Internal Revenue Service.

Jon Jossierand testified his office is in support of the bill. He referred to the two attachments that were handed out to committee members (See Attachments #4, #5). He explained the statutory highlights of the bill. He reported 18 states have enacted the revised uniform limited partnership act. It was intended that each state would modify it to dovetail with its corporation code. Mr. Jossierand stated the bill is workable in Kansas, there are no problems to administer and no fiscal impact.

CONTINUATION SHEET

MINUTES OF THE SENATE COMMITTEE ON JUDICIARY,

room 514-S, Statehouse, at 10:00 a.m./~~p.m.~~ on February 8, 1983

Senate Bill 106 continued

John Wine said he would be glad to answer any technical questions. He explained they have worked closely with Mr. Brookens and others who support the bill. He said the procedural change necessary for Kansas has been made in this draft, while still maintaining the desired uniformity. The chairman pointed out several areas in the bill and discussed suggested changes.

The chairman announced Senate Bill 141, that is scheduled for hearing on February 10, has been rescheduled for February 17.

The meeting adjourned.

2-8-83

GUESTS

SENATE JUDICIARY COMMITTEE

NAME

ADDRESS

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Lawrence

Steiniger

Gregg Matson

Lawrence

Steiniger

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Columbian Soc.

Becky Crenshaw

"

Comm of Ho Farm Orgs.

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"

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Janet Stubbs

"

NBAK

This person was scheduled to testify at the hearing on Monday, February 7, and was ill and unable to attend.

SIERRA CLUB &

KANSANS for #1
SAFE PEST CONTROL

RR 3
Lawrence, KS 66044
February 7, 1983

Senator E.F. Pomeroy, Chairman
Senate Judiciary Committee
State Capitol
Topeka, KS 66612

Dear Senator Pomeroy,

The Kansas Chapter of the Sierra Club and Kansans for Safe Pest Control support SB 107, which removes the severe restriction on access to the courts for those suffering injury from pesticides.

I would like to mention a few people who have been hurt by the 60-day statute of limitations.

The Ligenstoffers live on the edge of Kiowa, Kansas. They have been farmers for more than 40 years. In 1978, 2,4-D drift from aerial application to a neighbor's wheat field killed their large garden and badly damaged their orchard, shade trees, and shrubs. They notified their neighbor and the applicator immediately, and Mrs. Ligenstoffer brought the applicator out to see the damage. They filed suit to recover damages, and before the case came up, the same farmer hired a different applicator, who again let 2,4-D drift onto their property, this time completely destroying their orchard. They then learned that the first suit had been thrown because they had failed to file the form. They filed suit on account of the second incident, but didn't have enough money to see it through.

A family living near Lecompton had their garden and some shade trees killed by herbicide drift. They notified the applicator, who reimbursed them for the cost of the seeds for the garden. He told them to "wait and see" about the trees--then refused to pay. The applicator eventually did settle out of court when he was facing criminal charges for misuse in another case.

A quite different case involved a house in Leawood that was said to have been inspected for termite damage before closing the sale. Termite damage was discovered, and it was learned that a complete inspection had not been done. All parties were notified, but the attorney did not file a pesticide damage claim--evidently, he knew nothing about it. Consequently, the family failed to pursue the matter after they learned of the 60-day statute of limitations and the potential cost in attorney's fees. The damage involved was about \$1500.

The 60-day statute of limitations has been discussed in both Agriculture Committees. The reason given for conferees for retaining the time limit is that an applicator must be notified soon enough to collect evidence for his defense.

Atch. 1

In fact, the 60-day time period has no relationship to the time residues can be expected to persist--those that persist for 30 days will probably last for several months or years; others will last for only 2-3 days.

Since laboratory analyses are so expensive to perform, a person who has been damaged by pesticides has a very real economic incentive to report the damage promptly to the Board of Agriculture to obtain an investigation. This law has no effect in making people report damage more promptly--the biggest determining factor in how soon people report damage is how soon they learn how to report it.

(In 1979, when my husband and I wanted to report suspected pesticide damage, we called the county attorney, who said he had nothing to do with it. It wasn't until a string of phone calls led us to the Board of Agriculture that we were able to inform the county attorney that he had some pesticide damage claim forms.)

The case in which a person would not want to report damage promptly is, of course, the case in which he knows the damage was not caused by pesticides. Obviously, in such a case, the person would find it difficult to prove the damage was caused by pesticides--and in particular, the specific pesticide used by the applicator at that time. House Bill 2615, passed last year, allowing court costs in frivolous suits to be assessed against the party maintaining a groundless suit, should reassure applicators on this point.

Sincerely,

Terry Shafer

Terry Shafer
Kansas Sierra Club
Kansans for Safe Pest Control



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Date: February 8, 1983

In Re: SB 106, Kansas Revised Uniform Partnership Act.

Statement of KBA: John W. Brookens, Legislative Counsel

The law of Partnership developed in the Common Law, and as early as 1866 our Legislature dealt with this subject. In 1972, Kansas adopted the Uniform Partnership Act, which appears in our statutes as K.S.A. 56-301, et seq.

The concept of a Limited Partnership was not recognized in the Common Law, but is a creature of statute. Kansas first enacted statutes dealing with Limited Partnerships in 1868, and adopted the Uniform Limited Partnership Act in 1967.

As you know, the National Conference of Commissioners on Uniform State Laws exists for the purpose of studying, drafting, approving and recommending adoption of uniform laws throughout the United States. Senator Elwaine Pomeroy is a member of the National Conference.

The National Conference has approved and recommended a Uniform Limited Partnership Act in 1916, but it was not until 1967 that Kansas adopted that Act, which now appears in our statutes as K.S.A. 56-122, et seq.

In 1976, the National Conference adopted a Revised Uniform Limited Partnership Act, which was approved by the American Bar Association in February, 1979.

The Revised Act was offered as SB 828 in the 1982 Legislative Session. Apparently, preliminary background research had not been undertaken by proponents of this legislation to ascertain whether or not the procedural aspects of that proposal was administratively workable in Kansas. The office of Secretary of State had reservations about the administration of that proposal, and SB 828 was held over for an interim study, as Proposal 13. In a report to the Interim Study Committee, the Office of Secretary of State stated:

"1982 Senate Bill No. 828, with few exceptions, incorporates the text of the Revised Uniform Limited Partnership Act as proposed by the National Conference of Commissioners on Uniform State Laws in August of 1976. We support the concept of uniform laws when compatible with the particular circumstances of Kansas, and encourage your committee to consider the substantive provisions of S.B. 828. However, the Revised Uniform Limited Partnership Act is intended to be integrated with the corporation code of each state in which it is adopted. Without revision S.B. 828 would impose different requirements and procedures for limited partnerships and corporations."

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SB 106, Kansas Revised Uniform Partnership Act
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In other words, the office of Secretary of State supported the substantive provisions of the Revised Act, but correctly commented that the proposed bill, SB 828 of the 1982 Session, was not compatible with Kansas procedural law.

The Interim Committee quite properly declined to recommend SB 828, Proposal 13, for enactment into law.

As previously stated, there was not sufficient initial thought given to the Kansas administrative aspects of SB 828 of the 1982 Legislative Session. This was not caused by any act of commission or omission of the office of the Secretary of State, but rather was the lack of foresight of the proponents of that bill. The proponents were thinking of substantive law only.

Since receiving the report of the Legislative Interim Study Committee as to Proposal 13, (SB 828 of the 1982 Session), we have worked closely with Mr. Josserand and Mr. Wine of the office of the Secretary of State, and with practitioners in this very specialized field of law, and we believe S.B. 106, now before you incorporates not only the substantive law of the 1976 Revised Uniform Limited Partnership Act as approved and recommended by the National Conference of Commissioners on State Laws, but also this legislation conforms to recognized Kansas procedural provisions. It creates uniform procedural treatment of business entities not only among the states, but within Kansas. I am authorized to state that the Counsel for the Secretary of State approves of the provisions contained in SB 106, the legislation now being considered by you.

Our Kansas Corporation Code is modeled after the Corporation Code of the State of Delaware. Delaware is one of some 16 States that have now adopted the Revised Uniform Limited Partnership Act; we have studied the Delaware Act adopted in 1982 and have used it as a research source for this proposal. It dovetails with our Kansas administrative law now in existence.

We would like to quote from a legislative comment on the Delaware Revised Uniform Limited Partnership Act.

"The limited partnership has become a business vehicle of significant and increasing popularity. As in the case of corporations, an increasing number of limited partnerships are being formed under Delaware law. The proposed bill modernizes Delaware statutory law on limited partnerships, staying within the concept of the 1976 Uniform Act and ensuring that Delaware will continue as an attractive jurisdiction for the formation of limited partnerships."

"The proposed Revised Delaware Uniform Limited Partnership Act improves upon the present Delaware statute in many areas. For example, the proposed law sets forth definitions, provides for the registration of foreign limited partnerships doing business in Delaware and covers many other areas not in the current Delaware statute. It sets forth rules relating to the service

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of process with respect to both domestic and foreign limited partnerships, adopts provisions similar to those in the corporate area for the administrative treatment of limited partnerships in the Secretary of State's Office and establishes a schedule of fees for filings in that Office."

We think this comment is equally true for Kansas.

JWB:nmm

Time To Change Your Act

The Revised Uniform Limited Partnership Act



One of the most popular vehicles for promoting tax-oriented investments has been the limited partnership. The commingling of the laws of general partnerships with that of corporations, created for the investor-limited partner an ability to share in profits and losses of the venture (as would a partner) while still enjoying the benefit of limited liability (as would a corporate stockholder).

For the promoter-general partner of the limited partnership, the preservation and consolidation of the traditional corporate functions of the Board of Directors and Corporate Officers in the general partner created a flexible and governable investment vehicle.

The acquiescence by the Internal Revenue Service that a limited partnership may, where proper procedures and rulings are heeded, be taxed as a partnership and not as a corporation adds the benefit of being able to pass through taxable losses and credits to the partners (sometimes in excess of their investment), or avoiding the double taxation of our corporate tax structure by passing through taxable income to the partners with no tax being imposed upon the limited partnership itself.

No wonder the use of the limited partnership structure has increased. Along with this increase in use has come an increase in litigation by limited partners or creditors of limited partnerships. The increase in the necessity for judicial resolutions of these disputes evidences some inadequacies of our Kansas Uniform Limited Partnership Act (K.S.A. 56-122 et. seq.) which could be corrected in the 1983 Legislative Session.

Although the Kansas Uniform Limited Partnership Act was adopted by our legislature in 1967, it is modeled after the 1916 U.L.P.A. formulated and promoted by the National Conference of Commissioners on Uniform State Laws. Kansas is therefore subject to a 66 year old code regulating business activities which were largely unknown and unforeseen at the time the model was drafted.

Of course, the basic concepts need not be changed. But in 1976, the National Conference of Commissioners on Uniform State Laws published a revised model for U.L.P. Acts. Recognizing that limited partnerships were now a common investment vehicle for real estate projects, movies, oil and gas development, livestock operations, mining ventures and even public relation campaigns, the Commission did not opt to re-state or change the structure of the Act, but did choose to provide additional protection for limited partners and creditors, while streamlining and clarify-

Circuit Rider

By Bryon R. Schlosser



Bryon R. Schlosser, '71 is Treasurer and General Counsel of McBiz Corporation in Topeka, Kansas. He has been an adjunct at the law school for several years.

ing organizational and operation procedures.

Senate Bill 828 of the 1982 Legislative Session was considered by the Senate Judiciary Committee during the later part of the 1982 session. This bill simply repealed the Kansas Uniform Limited Partnership Act and replaced it with the 1976 revision of the U.L.P.A. approved by the National Conference of Commissioners on Uniform State Laws.

At hearings before the Senate Judiciary Committee, it was pointed out by a representative of the Secretary of State's office that S.B. 828 repealed all of the recording and annual fees currently being paid by approximately 1,500 foreign and domestic limited partnerships registered in Kansas with no substitute provisions. The representative from the Secretary of State's office also disclosed that his office had been considering a change in these fees and would prefer additional time to report the conclusions of the Secretary of State before recommending repeal or confirmation of those statutes.

The entire matter was then placed on the interim agenda for study, and hearings were held by the Special Committee on Judiciary on July 2, 1982. Appearing before the Special Committee at this time were representatives of the Secretary of State's office, the Kansas Bar Association and John M. McCabe, Legal Counsel and Legislative Director of the National Conference of Commissioners of Uniform State Laws. There was no testimony in opposition to the substantive provisions of the proposed changes, and if my analysis is correct, Kansas is well on its way to substituting the 1976 revised Uniform Limited Partnership Act for the 1916 model act provisions currently embodied in K.S.A. 56-122 et. seq.

Although the changes and additions to the 1916 model act are too numerous to mention in this article, the major changes may be summarized as follows:

(continued on next page)

Atch. 3

Time To Change Your Act *continued:*

1. The current requirement for filing the partnership certificate in the county in which the partnership has its principal place of business is deleted.

2. A procedure for reserving a name for the partnership prior to filing the certificate is provided.

3. Each limited partnership (foreign and domestic) will be required to maintain a registered office in Kansas and a resident agent for service of process.

4. A current list of all partners and their addresses, a copy of the certificate, the partnership's last three years' tax returns and financial statements, and a copy of the partnership agreement must be maintained at the registered office and be made available to any partner for inspection or copying upon reasonable request.

5. Much greater flexibility is permitted by allowing the partnership agreement to provide for admission of new partners and withdrawal of partners without the necessity of amending the agreement. Also, the partnership agreement is permitted to provide for distribution of assets to a withdrawing partner without dissolution of the partnership.

6. A "safe harbor" rule is provided to guide limited partners as to what duties each may assume without forfeiting their limited liability status. The revised act allows a limited partner to be a contractor, agent or employee of the limited partnership or one of the general partners. A limited partner may also consult with and advise the general partner; act as surety for the partnership; and vote on (a) dissolution and winding up of the partnership, (b) the sale, exchange, lease, mortgage, pledge or transfer of all or substantially all of the assets, (c) the incurrance of indebtedness (except in the ordinary course of business), (d) the change of the nature of partnership business, or (e) the removal of a general partner.

7. Limited partners are permitted to perform services in exchange for their interest in the partnership.

8. In the absence of an agreement to the contrary, profits, losses and asset distribution is set in proportion to the value of each partner's contributions.

9. A derivative action for limited partners is created paralleling the rights of a corporate stockholder.

10. Voting rights may be granted to limited partners or classes thereof in the partnership agreement.

11. The name of the limited partnership must contain ~~without abbreviation~~ the words "limited partnership". *or "L.P."*

Based upon a memorandum to the Special Committee on Judiciary from John R. Wine, Jr., Legal Counsel and Deputy Assistant Secretary of State, it is anticipated that the 1976 Revised Uniform Limited Partnership Act will be further modified so that procedures and fees for filing, name reservation,

annual reporting, foreign registration and reinstatement will closely resemble that of our corporation code.

Many of these changes statutorily clarify what the adept limited partnership attorney would have already provided in the partnership agreement. Nevertheless, the revised act obviously attempts to increase protection for the limited partners and creditors while stressing procedural changes permitting easier management of those limited partnerships which have hundreds of limited partners.

These added protections and clarifications, particularly in light of the changes in business and investors' needs since 1916, justify our profession's support of the Kansas Legislature's substitution of the substantive provisions of the 1976 Revised Uniform Limited Partnership Act for our current Kansas act.



Dean Carl Monk shares a few words with Meyer Ueoka during Homecoming activities.



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January 25, 1983

Statement of Kansas Bar Association relative to Revised Uniform Limited Partnership Act.

John W. Brookens, Legislative Council

This is a proposal of the Kansas Bar Association. We feel there is a significant interest in updating our laws on Limited Partnerships.

In 1916, the National Conference of Commissioners on Uniform State Laws drafted, approved and recommended for enactment in all of the States a Uniform Limited Partnership Act. This act was adopted in Kansas.

As time passed, as business practices changed, it became apparent that a modernized version of the code would be better. In 1976, the National Conference drafted, approved and recommended for enactment in all of the states, a revised Uniform Limited Partnership Act. It was intended to modernize the prior law while retaining the special character of limited partnerships as compared with corporations. A limited partnership has a wide degree of flexibility in defining the relations among the partners that is not possible in a corporation. The relationship of the partners is by agreement of the parties under circumstances that corporate management would deem not only unworkable, but unthinkable.

The Revised Uniform Limited Partnership Act was offered in the 1982 legislative session, and was the subject of an interim study as Proposal 13. Senators Burke and Feleciano were members of the interim committee. That committee was faced with certain objections to that draft of the Act by the office of the Secretary of State. The committee also felt there was no particular compelling need for the revised Act.

Since receiving the Interim Committee Report, we have met with the office of Secretary of State, with accountants and lawyers knowledgeable in this specialized field. We have reached a

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Revised Uniform Limited Partnership Act
Kansas Bar Association

consensus on a workable draft of the bill. Objections of the office of Secretary of State have been met, and they now approve of this proposal.

Our corporation code is modeled after that of the State of Maryland. We have used the Maryland revised Uniform Limited Partnership Act as a model for our present proposed Act, and the office of Secretary of State has conformed this to our Kansas administrative procedures.

I am authorized to say that counsel for the Secretary of State now joins us in this present proposal.

A limited partnership is a very useful legal vehicle to promote investment in Kansas. It is useful in oil field explorations, land development, and can be used in management of family farms. It creates the legal possibility of many persons joining together by agreement to share profits and losses as a partner while still retaining the benefits of limited liability as would a corporate stockholder.

We believe Kansas should join the 15 or so States that have enacted some form of this Revised Uniform Limited Partnership Act. We would prefer these be formed in Kansas and be controlled by Kansas law. Kansas is now operating under a 66 year old code regulating business activities which were largely unknown and unforeseen at the time the 1916 model act was drafted. We think it is time to bring Kansas up-to-date.

We therefore respectfully request the Senate Judiciary Committee introduce this proposal as a Committee bill, ask that it be referred back to the Committee for hearings thereon.

STATUTORY HIGHLIGHTS OF SENATE BILL NO. 106
KANSAS REVISED UNIFORM LIMITED PARTNERSHIP ACT

2883
#4
PRESENT STATUTE
Kansas Uniform Limited Partnership Act
[K.S.A. 56-122, 56-124 through 56-151;
K.S.A. 1982 Supp. 56-123 through 56-123c]

RULPA (1976)
Revised Uniform Limited Partnership Act
[§101 et seq.]

SENATE BILL NO. 106
Kansas Revised Uniform Limited
Partnership Act

only one definition [56-122]

adds eleven more definitions
of important terms [§101]

expands scope of foreign L.P., G.P. & L.P.
definitions [Section 1 (d), (e) & (f)]

no provisions for a registered office
or resident agent, change of address
of registered office, or resignation
and succession of resident agent

also no such provisions

adds the provisions [Section 4]

no provision for record-keeping

provides for an over-broad
record-keeping function &
depository [§105]

deletes such provision

no provision for service of process
on domestic L.P.'s

also no such provision

adds the provision [Section 5]

provides for mandatory amendment of the
L.P. certificate if there is a change of
name of L.P. [56-145 (2) (a)]

has no such provision

puts the provision back in; also makes
amendment mandatory when there is a
change of address for resident agent or
registered office [Section 9 (c) (5)]

amendments and cancellations of certificates
must be signed and sworn to by all "members"
[56-146 (1) (b)]

provides for execution by
attorney-in-fact [§204 (b)]

retains power-of-attorney situation,
but further provides for non-filing of such
with Secretary of State [Section 11 (b)]

to be a valid L.P., certificate must be
filed for record with Secretary of State
procedure
[Supp. 56-123 (1) (b)]

requires two originals to be
signed and filed [§206]

requires only one original, with one duplicate
(signed or conformed); simplifies filing
[Section 13]

requires domestic L.P.'s to file an annual report
and payment of franchise tax [Supp. 56-123a]

no such provisions

continues annual report and franchise tax
provisions [Section 69]

Att. 4

PRESENT STATUTE

provides for liability of party to L.P. certificate who allowed false statement in certificate, such liability flowing to one who suffers loss in reliance thereon [56-127]

no provision for a restated L.P. certificate

no safe-harbor provisions describing activities L.P. may undertake without risking their status as L.P.

allows a capital contributor to an L.P. to back out of what he thought was his L.P. status [56-132]

no provision for the addition of G.P.'s

doesn't present a logical delineation of the events creating, surrounding and terminating, the statuses of G.P. & L.P.

provides for the dissolution of a L.P. in the event of the death, retirement, bankruptcy or mental illness of a G.P. [56-141]

allows for the assignment of a L.P.'s interest [56-140] to a "substitute" L.P.

RULPA (1976)

retains such provision [§207]

also no such provision

adds a voting power on threshold L.P. issues [§303 (b) (5)]

expands and formalizes the required activities of the capital contributor if he wishes to back out, and amplifies the circumstances upon which his liability to third parties is predicated (including the necessity of "actually believing in good faith" that the contributor was a G.P. [§304]

adds such provision [§401]

provides a structured presentation of G.P. and L.P. status (§301 through 305, 401 through 405, 602, 603, 702, 704 and 705]

expands the bases for a G.P.'s withdrawal from a L.P. and anticipates that entities other than natural persons will become G.P.'s [§402]

doesn't differentiate between L.P.'s and G.P.'s and deletes concept of "substitute" [§702]

SENATE BILL NO. 106

restricts liability to material falsehoods, requires reasonable reliance and contains a 30-day grace period for filing a corrected certificate [Section 14]

adds one [Section 17]

adds the voting power on threshold L.P. issues [Section 20 (b) (5)] and allows a L.P. broader involvement vis-a-vis "material matters related to the business" without converting his status to G.P. [Section 20 (b) (6)]

further expands the contributor's activities, but in addition to actual belief in good faith, emphasizes reliance by the third party on such belief as another prerequisite to the imposition of liability [Section 21]

liberalizes the possibilities of admission [Section 23]

same [Sections 18 through 24, 26, 27, 33, 34, 41, 43 & 44], but specifies G.P. liability to third-party creditors, partnership, and other partners [Section 25]

same [Section 24]

same [Section 41]

PRESENT STATUTE

only mentions the concept of "dissolution" in the context of distribution [56-144]

has provisions relating to foreign L.P.'s requiring filing of any application to do business [Supp. 56-123b] and requiring filing of an annual report and payment of franchise tax [Supp. 56-123c]

no provision for allowing L.P.'s formed under pre-existing statutory authority some choice vis-a-vis the timing of their submission to the new law

various references to fees [Supp. 56-123 through 56-123c]

RULPA (1976)

enlarges the concept to include distribution of assets, winding up, judicial intervention [§§801 through 804]

foreign L.P. provisions [§§901 through 908]

adopts such a provision [§1104] but in a disjointed way

no references to fees

SENATE BILL NO. 106

same [Section 45-48]

augments foreign L.P. provisions [Sections 49 through 58]: requires maintenance of a resident agent and registered office [Section 52]; prevents an unregistered foreign L.P. from doing business in Kansas [Section 56]; makes foreign L.P.'s ministerially responsible the same as a domestic L.P. [Section 57]; and provides for service of process on both registered and unregistered foreign L.P.'s [Section 58]; continues annual report and franchise tax provisions [Section 70]

logically restructures the effective dates of submission to the new law [Section 66]

explicit fee schedule [Section 68]

LEGAL TIMES

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Many States Enact RULPA Despite IRS Doubts

By Kim Masters
Legal Times Staff

A growing number of states—some of which hope to attract new business—are enacting a five-year-old uniform limited partnership act despite fears that the Internal Revenue Service will not permit partnerships formed under the new code to enjoy the intended tax advantages.

From the IRS viewpoint, the key question is whether partnerships formed under the new act display more characteristics of a corporation than of a limited partnership. Two years ago, the IRS indicated in proposed rules that it generally would tax as partnerships most entities formed under the new law. Since then, the IRS has signaled that it may be having some second thoughts. The proposed rules remain lodged in the Office of the Chief Counsel as lawyers become increasingly eager for IRS action.

These attorneys are impatient be-

cause states that have not yet revised their laws are beginning to recognize that states with revised limited partnership laws have created a much more workable investment device that may attract desirable business. Some of the states that recently have enacted revision of the old laws are deliberately adding features to make themselves appealing home bases for limited partnerships.

Limited partnerships are attractive ways to start certain businesses, particularly those likely to lose money in the early stages, or those that might show a tax loss despite a positive cash flow (for example, in real estate transactions in which partners can take advantage of generous depreciation allowances). They are frequently used in research-and-development ventures, or in oil and gas exploration and development. They allow investors to raise capital without incurring fiduciary duties and other obligations imposed by laws governing corporations, although

general partners usually enjoy close control over management. For limited partners, they allow individuals to invest with limited liability, and to enjoy direct tax benefits that do not accrue to corporate shareholders.

The uniform limited partnership law being adopted by a growing number of states is actually a revised version of a uniform law, originally adopted in 1916 by the National Conference of Commissioners on Uniform State Laws. No one disputes that the Revised Uniform Limited Partnership Act (RULPA) is an improvement over the old law. More and more states now are overcoming their concerns about IRS reaction because they are eager to reap the benefits of an improved version of the law.

Delaware, long recognized for its attractive corporation laws, revised its limited partnership law during the summer (the change becomes effective

in January). Lawyers who worked on the revisions say they tried to preserve uniformity, but also built in existing features of Delaware law that make the state an appealing base.

"I'm involved in any number of situations where out-of-state attorneys are forming Delaware limited partnerships, and they're forming them here because they feel the Delaware statute

More and more states are overcoming their concerns about IRS reaction because they are eager to reap the benefits of an improved version of the law.

and Delaware courts are an attractive forum," said Martin I. Lubaroff of Wilmington's Richards, Leyton & Finger. Lubaroff was a member of a state bar association committee that drafted the new Delaware law.

Provision Expands Rights

A key provision of Delaware's law expands the voting rights that limited partners may exercise without incurring the greater liability to third-party creditors that accrues to general partners. Although the revised statute grants voting rights to limited partners on certain matters, the Delaware law permits them to vote on "any material matter" specified beforehand in the partnership agreement.

"This is the most attractive feature of the Delaware statute," said John H. Small of Wilmington's Prickett, Jones, Elliot, Kristol and Schnee. "When you go into the deal, as long as you [specify] the type of decision that the limited partners are able to participate in, they can participate without becoming general partners . . . The Delaware statute has enough flexibility so you can structure the deal just like the parties want."

Howard P. Walthall, a professor at Samford University's Cumberland School of Law in Birmingham, Ala., said Delaware appears to have made "a modest attempt" to attract business through its revised law. He said that California has undertaken an ambitious plan to become "the Delaware of limited partnerships" through its new law, which bears little resemblance to RULPA.

But John M. McCabe, legal counsel and legislative director of the National Conference of Commissioners on Uniform State Laws, said attorneys who developed the California law "probably pretty well outfoxed themselves." McCabe and other attorneys said the California law includes so many new provisions and obligations that in some ways, it is more cumbersome than RULPA, and less likely to pass IRS scrutiny. These difficulties are so great that the state has postponed the January 1983 effective date of its plan for at least a year, and some attorneys predict that the law never will take effect.

The crux of the tax question is whether the limited partnerships include certain provisions that make the resulting entity appear to the IRS to be a corporation rather than a partnership. If that results, the tax benefits that are often the purpose of the limited partnership could be lost, because IRS would tax the entity as a corporation.

One issue involves the liability of general partners. According to the original 1916 model law, general partners in limited partnerships are fully liable to third-party creditors. The revised law includes the same language, but says it applies "except as provided in . . . the partnership agreement."

The IRS's concern is whether this language means that general partners can draft a partnership agreement limiting their liability to third-party creditors. If so, the IRS is far more likely to conclude that the entity has lost a crucial characteristic of a limited partnership.

Sentence Shifted

Lawyers familiar with RULPA say its drafters never intended to allow general partners to limit their liability. One sentence in the comments to RULPA would have clarified that point, the lawyers said, but the sentence was moved inadvertently from the correct place when the comments were printed. McCabe said the conference is changing the comments in order to clarify that general partners may not limit their liability.

Some attorneys question whether the comments to RULPA carry enough weight to persuade the IRS that the law does not permit dilution of general partners' liability. Robert M. Berger, of Chicago's Mayer, Brown & Platt, head of an American Bar Association subcommittee on RULPA, said he hopes the question of the IRS reaction to RULPA will be straightened out soon. "The private bar generally has been waiting and watching for the Service's wheels to grind . . . It really is time to get off the dime and get some

action for the Service," he said. An IRS spokesman said it is developing final rules, but that they will require clearance from the Treasury Department when completed.

Meanwhile, states apparently are beginning to overcome their anxieties about the IRS and enact versions of RULPA anyway. According to Walthall, 14 states have adopted some version of RULPA. Berger said states are not acting primarily to attract business, but simply are engaging in good, objective law-making. But Walthall says the result clearly is that partnerships, given a choice, prefer RULPA states.

Replaces 'Byzantine' Laws

Walthall and other attorneys agree

that RULPA contains some essential modifications and simplifications from the 1916 version of the law. "Under the old partnership law, it was almost Byzantine, some of their things you had to do," said Small.

Although Walthall said most limited partnerships prefer RULPA states, choosing among states that have enacted versions of RULPA raises much finer questions. But he added that some big-money, multistate partnerships certainly would find it worthwhile to "spend an afternoon researching what would be the best place of domicile."

Walthall says a number of factors would influence a final choice:

- *The simplicity of filing and amending a certificate of partnership.* According to Walthall, the old 1916 law requires lengthy and unwieldy procedures each time a certificate of partnership is amended (for example, if a limited partner is added). RULPA greatly simplifies those procedures, and the California statute goes even further.

- *The ease of adding general partners.* The old law is not clear on what procedures must be followed, Walthall said. It requires written consent of other partners, but most lawyers have assumed that that can be done in advance through the partnership agreement. RULPA appears to add some extra procedures at the time the general partner is added, but Walthall said the comments to RULPA are being amended to clarify that these extra procedures are not really necessary.

- *The extent of the safe-harbor provisions describing activities limited partners may undertake without risking their status as limited partners.* The 1916 law contains no safe harbor, although some states added safe harbors independently. RULPA contains a safe harbor allowing limited partners to exercise some voting rights and to act as agents of the partnership. States like Delaware and California have added to those provisions. ■