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Business Associations - Uniform Limited Partnership Act - Activites Making a Limited Partner Liable as a General Partner

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RECENT DECISIONS

BUSINESS ASSOCIATIONS—UNIFORM LIMITED PARTNERSHIP ACT—ACTIVITIES MAKING A LIMITED PARTNER LIABLE AS A GENERAL PARTNER—Marback Motor Co., a limited partnership, was formed in 1951 pursuant to the California Uniform Limited Partnership Act.¹ Defendant limited partner held a chattel mortgage on partnership assets and owned the building in which the business was located. He had authority to co-sign checks of the partnership, but checks could be drawn on the firm's account without his signature and he could not withdraw funds himself. In August 1953, without a prior dissolution of the limited partnership, defendant bought some assets of the firm at a purchase price found to represent the fair market value of the properties. At the time of sale the firm had more than sufficient assets to pay all creditors. The limited partnership then went out of active business and defendant took over operation of a similar business on the same premises under a different name. In 1954, the limited partnership was adjudicated bankrupt. Actions were brought by the trustee of the bankrupt limited partnership and a creditor's executor seeking to hold defendant as a general partner. *Held*, defendant did not exercise such control over the business as to become liable as a general partner under the California Uniform Limited Partnership Act. *Grainger v. Antoyan*, (Cal. 1957) 313 P. (2d) 848.

In Anglo-American law the limited partnership is purely a statutory creature. Since the original approval and adoption of the Uniform Limited Partnership Act by the National Conference of Commissioners on Uniform State Laws in 1916, it has been enacted in 38 states or territories.² Section 10 of the act expressly allows the limited partner certain rights: (1) to inspect and copy the partnership books; (2) to have on demand full information of all things affecting the partnership; (3) to have the partnership dissolved by a decree of the court; and (4) to receive a share in the profits or other compensation and to receive the return of his capital contribution. Section 13 of the act grants added rights, allowing the limited partner, subject to certain restrictions, to loan money and to transact other business with the partnership, and to receive on account of such claims a pro rata share of the assets with general creditors. On the other hand, section 7 of the act makes the limited partner liable as a general partner if he takes part in the "control" of the business.³ Yet nowhere in the act is the term "control" defined. It is possible to argue that the exercise of any

¹ Cal. Corp. Code Ann. (Deering, 1953) §§15501-15531.

² 8 Uniform Laws Annotated (Supp. 1956) 6. In addition to those listed, Ohio has also passed the act, Ohio Rev. Code. (Supp. 1957) c. 1781. There were, of course, limited partnership statutes in some states prior to 1916.

³ Uniform Limited Partnership Act §7, "A limited partner shall not become liable as a general partner unless, in addition to the exercise of his rights and powers as a limited partner, he takes part in the control of the business."

authority beyond the powers specifically authorized by the act will result in taking part in the control of the business, but the few cases on this issue ignore such reasoning.⁴ To the contrary, it seems clear that courts do not restrict the limited partner to his statutory powers, but instead approach each new fact situation on its merits, determining the legal import of the limited partner's acts as a matter of judicial discretion. Certain trends have emerged from the few decisions in point, however, and tentative conclusions can be made. First it is clear that section 7 precludes a limited partner from active domination and operation of the limited partnership or from taking part in decisions which determine business policy to any substantial degree.⁵ Conversely, it has been held in cases construing the act and earlier similar laws that the limited partner could consult with the general partner;⁶ act as surety for the firm;⁷ advise general partners as to the conduct of the business;⁸ do an occasional errand for the partnership;⁹ advise third persons as to the status of the partnership;¹⁰ bring an action for dissolution and act as receiver;¹¹ and take possession of firm property in winding up after dissolution.¹² In short, it would appear that the limited partner can traditionally transact and deal with the firm in the same manner that a stranger could, with the more recent cases evidencing greater liberality as to the permissible acts of the limited partner.¹³ This modern tendency, apparent in the principal case, is at least partially explained by an increased

⁴ Rathke v. Griffith, 36 Wash. (2d) 394, 218 P. (2d) 757 (1950), noted in 26 WASH. L. REV. 222 (1951); Holzman v. de Escamilla, 86 Cal. App. (2d) 858, 195 P. (2d) 833 (1948); Silvola v. Rowlett, 129 Colo. 522, 272 P. (2d) 287 (1954), noted in 27 ROCKY MT. L. REV. 98 (1954).

⁵ Holzman v. de Escamilla, note 4 supra (limited partner exercised managerial dictation and veto power over finances); Strang v. Thomas, 114 Wis. 599, 91 N.W. 237 (1902) (board of directors chosen by limited partner); Farnsworth v. Boardman, 131 Mass. 115 (1881) (limited partner executed contracts for the partnership on his own authority); In the matter of Sucesores De José Hernaiz, 3 Porto Rico Fed. Rep. 202 (1907) (limited partner exercised managerial domination and was agent for the firm); Richardson v. Hogg, 38 Pa. 153 (1861) (appointee of limited partner became the controlling manager of the firm).

⁶ Ulman & Co. v. Briggs, Payne & Co., 32 La. Ann. 655 (1880).

⁷ Rayne & Co. v. Terrell, 33 La. Ann. 812 (1881).

⁸ Lewis v. Graham, 4 Abb. Pr. (N.Y.) 106 (1857); Silvola v. Rowlett, note 4 supra.

⁹ McKnight v. Ratcliff & Johnson, 44 Pa. 156 (1863).

¹⁰ Ulman v. Briggs, note 6 supra.

¹¹ Continental Nat. Bank of Boston v. Strauss, 137 N.Y. 148, 32 N.E. 1066 (1893).

¹² Lawson v. Wilmer, 3 Phila. 122, 15 Leg. Int. 133 (Pa. 1858).

¹³ In Silvola v. Rowlett, note 4 supra, a limited partner was held not to have exercised control where he gave advice to the general partner and was authorized to extend credit to persons known to him personally. In Rathke v. Griffith, note 4 supra, the court held that the limited partner had not exercised such control as to make him personally liable even though he executed a power of attorney, helped the general partner to negotiate a loan, negotiated with a contractor, signed contracts, signed leases with the general partners in the partnership name, and was at least in name a member of the board of managing partners. In the principal case the court stated that since there was no evidence of reliance by the creditors on the limited partner as a general partner, his acts would not render him liable as a general partner. The case implies that an added condition is needed to render a limited partner liable as a general partner under §7, viz.,

emphasis in section 7 decisions upon the factor of creditor reliance in determining the question of control. The principal case seems to consider the aspect of creditor reliance significant, stressing the fact that the limited partner purchased the assets at their fair market value at a time when the assets were sufficient to pay all creditors.¹⁴ Such a requirement of reliance is not expressed in section 7. In fact it can be fairly argued that since the act specifically refers to the question of reliance in sections 5 and 6,¹⁵ requiring reliance in some other section is not justified. On the other hand, a requirement of creditor reliance does not seem adverse to the policy assumptions of the act, one of which is the protection of creditors.¹⁶ Thus while the principal case adds little to the sparse body of judicially-approved activities of a limited partner, its inferential support for increased consideration of creditor reliance appears significant. Continued respect for this additional factor in cases construing section 7 will clearly mean greater latitude for the limited partner who does not by his activities lead creditors astray.

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that the creditors of the limited partnership rely on the acts of the limited partner, believing him to be a general partner. See also *Lawson v. Wilmer*, note 12 supra; *Rayne v. Terrell*, note 7 supra.

¹⁴ But see *First Nat. Bank of Canandaigua v. Whitney*, 4 Lans. 34 (1871), affd. 53 N.Y. 627 (1873).

¹⁵ Section 5 provides that a limited partner whose surname appears in the partnership name is liable as a general partner to partnership creditors who extend credit to the partnership without actual knowledge that he is not a general partner. Section 6 provides that if the certificate of limited partnership contains a false statement, a person who suffers loss by reliance on such statement can hold liable any partner who knew the certificate was false at a time prior to the reliance.

¹⁶ Commissioners' Note, 8 U.L.A. 4 (1922): "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 time their credits were extended that such person was so bound."