

INTRODUCTION TO THE FAMILY / BUSINESS LIMITED PARTNERSHIP

(Internal Revenue Code § 704)
(California Corporations Code 15502)

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FOREWORD

The law prohibiting a creditor from reaching the assets of the partnership has been well established for many years. In fact, these particular provisions of partnership law were first adopted as part of the English Partnership Act of 1890, later being reaffirmed in 1907. Some portions of England's partnership act were subsequently adopted as part of the Uniform Partnership Act, which has been the basis of the law in the United States since the 1940's.

These provisions are necessary to accomplish a particular public policy objective. This policy is that the business activities of a partnership should not be disrupted because of the non-partnership related debts of one of the partners. Prior to the adoption of these provisions it was possible for a creditor of a partner to obtain a Writ of Execution ordering the local sheriff to levy directly on the property of the partnership to satisfy the creditor's debt. The local sheriff went to the partnership's place of business, shut down the business, seized all of the assets and sold them to satisfy the debt. These methods not only destroyed the partnership's business but also caused a significant economic injustice to the non-debtor Partner through the forced liquidation of partnership assets. The non-debtor partner did not do anything wrong. Why should he be forced to suffer?

In order to avoid precisely these unfair results, the law was formulated so that a creditor with a judgment against a partner, but not against the partnership, cannot execute directly on partnership assets. Instead, the law allows the creditor to obtain a charging order which affects only the actual distributions made to the debtor partner. The business of the partnership is allowed to continue unhampered and the economic interest of the non-debtor partner is not impaired.

The protection of partnership assets from the claims of one partner's creditors is deeply entrenched in the foundation of French, American, and English partnership law. Without such protection the formation of partnerships would be discouraged and legitimate business activities would be impeded. When understood in this light, it is clear that the asset protection features of a [*family*] Limited Partnership are neither a fluke nor a loop-hole in the law. Rather, these provisions are an integral part of partnership design and it is unlikely that changes in the law will ever be made which would impair these features.

INTRODUCTION TO THE FAMILY and/or BUSINESS LIMITED PARTNERSHIP

THE BIG WINNER IN ASSET PROTECTION

HISTORY AND SOURCE OF LIMITED PARTNERSHIP LAW

Since business employs both capital and services that may come from very different sources; a need exists for a form of association that permits capital investments without responsibility for services or management and without liability for losses beyond the amount invested¹.

That need gave rise to the modern corporation; but, much earlier, in the middle ages, it gave rise to the *commenda*², in continental Europe. In this commonly used arrangement, the *commendator* supplied money to the *commendatarius* (or *tractator*) to be employed in trade. The *commendator* received a portion of the profits, often one-fourth, but had no liability for losses, was not guilty of usury, and did not violate inhibitions against engaging in trade. He had no claim against the *commendatarius* for loss of the capital investment not caused by the latter's fault. The *commenda* was sanctioned by the French Ordinance on Commerce of 1673.

¹ Early case law history includes [Chick v. Robinson](#), 95 F. 619, 52 L.R.A. 833 (6th Cir. 1899); [Henkle v. Heyman](#), 91 Ill. 96 (1878); [Creham v. Megargel](#), 234 N.Y. 67, 136 N.E. 296 (1922); [White v. Eiseman](#), 134 N.Y. 101, 31 N.E. 276, 277 (1892); [Richardson v. Hogg](#), 39 Pa. 153 (1861); [Allegheny Natl Bank v. Bailey](#), 147 Pa. 111, 23 A. 439 (1892); [McKnight v. Ratcliff](#), 44 Pa. 156 (1863).

² According to the historical antecedents as written by the learned Surrogate Alexander Bradford, "Under the name of *la Societe en commandite*, it [the limited partnership] has existed in France from the time of the middle ages; ... in the early regulations of Marselles and Montpellier ... In the statutes of Pisa and Florence, ... also in the ordinance of Louis-le-Hutin, of 1315; the statutes of Marseilles, 1253; of Geneva, of 1588 ... even traveled under the protection of the arms of the Crusaders to the city of Jerusalem ... and brought the Commons into position as an influential estate in the commonwealth."

In the United States, the limited partnership has traditionally been regarded as a creature of legislation, unknown to the common law, although it has come to have some common law recognition. The French Code inspired the earliest U. S. limited partnership laws. The first statutes were adopted in New York (1822), Connecticut (1822), and Pennsylvania (1836). This was said by a leading contemporary commentator to be the first instance in which American states derived statutory law from a county other than England³.

As an interesting footnote, limited partnerships were not accepted in England until appropriate legislation was passed in 1907⁴.

AN OVERVIEW - LIMITED PARTNERSHIPS

The Baldwin Trust Group Contractual Business Organization (CBO) has seen a greatly increased awareness by the "informed community" of the three (3) primary uses of limited partnerships. Limited partnerships can be effectively used in these major situations:

1. As an **ASSET PROTECTION TOOL**, the limited partnership really reigns supreme. The single greatest proclamation in recent years to my estate planning clients is that **the limited partnership is without peer** in the asset protection area. The reasons why will be answered in detail herein.
2. As a **TOOL TO SPREAD INCOME** among the family; limited partnerships can effect a lower overall family income-tax rate. Recently we have seen a substantial increase in the use of limited partnerships.
3. As a **TOOL FOR ESTATE PLANNING**, few legal tools have the flexibility and control capabilities as does the [*family*] Limited Partnership. With only a one (01%) percent general partnership interests in a family limited partnership, Mom and Dad, as the general partners, can have effectively one hundred (100%) percent control. They also can generally avoid estate taxes up to eighty-five (85) percent of the value of the assets conveyed into the

³ J. Kent, Commentaries on American Law *36 (1828).

⁴ 7 Edw. VII. Ch 24 (1907).

limited partnership. Tragically, many overlook this tool.

INTRODUCTION TO LIMITED PARTNERSHIPS

Operating a business structured as a corporation is unsatisfactory for many investors and business owners, because of the risk of double taxation and the limitations on flexibility in design of stock interests. Therefore, many businesses and investment concerns are operated instead as general or limited partnerships, or as limited liability companies (LLC)⁵. Partnerships offer greater structural flexibility as well as enhanced ability to make tax-free contributions. Consequently, both the partnership and the LLC have become increasingly popular in recent years as vehicles for making gifts of diversified assets while retaining control over the assets' management and ultimate disposition, and for obtaining valuable tax discounts on both the transferred and retained interests. However, wealth transfers through [*family*] limited partnerships and limited liability companies are not without their complexities and difficulties. Despite the somewhat difficulties mentioned above; the [*family*] limited partnership, with its well established case law and one hundred years of maturity⁶, is still the ultimate statutory asset protection entity available to the American public today.

FAMILY LIMITED PARTNERSHIPS

A family limited partnership is created by the transfer of property, real or personal, from the title of a person or persons (“donor-partners”) to that of the “**partnership of persons**” acting together for their common economic benefit.

⁵ Under California LLC laws enacted in 1994; the California LLC cannot carry on any business within the state that requires a professional license (i.e., CA B&P Code) unless other provisions of law specifically permit such business. Stats. 1994, ch. 1200, § 93; Stats. 1996, ch. 57, § 30.

⁶

As of December 1999, only 35 reported cases addressing LLC legal and tax issues have hit the federal and state courts. Two cases, however, involved veil-piercing issues that of are interest are: [Ditty v. Checkrite, Ltd., Inc.](#), 1997 WL 471115 (D. Utah Aug. 1, 1997); and In re Multimedia Communications Group Wireless Associates of Liberty County; [Mills v. Webster](#), 212 B.R. 1006 (bankr. M.D. Fla. Aug. 28, 1997).

Any partners who receive their interest without contributing their own capital or services (“donee-partners”) receive a proportionate share of any property transferred to the partnership. Caution should be taken as the transfer of property to a family limited partnership is clearly a taxable gift to the extent the donees do not contribute valuable consideration for their interest. Additional gifts may be made merely by amending the partnership agreement to increase the donee-partner’s relative interests.

If a “custodianship of a minor” is a partner within the [*family*] limited partnership; it is often the simplest solution to give the partnership interest of a minor to a custodianship appointed under either the Uniform Transfer to Minors Act (UTMA) or to the Uniform Gift to Minors Act (UGMA), to hold on the minor’s behalf. If the total value of the partnership interests to be given to the donee over several years will be relatively small (*e.g., under \$50,000*), the legal and accounting expenses incident to a formal trust make the custodianship the most practical device for holding the interest. Because some states still operate under the UGMA, rather than the UTMA, either they do not permit custodians to hold partnership interest or permit custodians to hold only limited partnership interest. Also, custodial persons holding a partnership interest on behalf of a minor serve subject to “judicial supervision of the conduct of the fiduciary as is required by law,” and that the person file of such accountings and reports as be required by applicable state law. Because the UGMA and the UTMA are state laws and the custodian is a fiduciary (*although not a trustee*), a custodian appointed under these acts should be able to hold [*family*] partnership interest of a minor without the appointment of a legal guardian if state law so permits.

A “**Partnership of persons...**” - Section 101(9) of the Revised Uniform Partnership Act (RUPA), approved in 1994 by the Conference of Commissioners on Uniform State Laws declare a partner must be a person, defined as “*an individual, corporation, business trust, estate, trust, partnership, joint venture, government, governmental subdivision, agency or instrumentality, or any other legal or commercial entity.*” Likewise, according to the Uniform Partnership Act (UPA), approved in 1914 by the Conference of Commissioners on Uniform State Laws, in Section 2 a person “*includes individuals, partnerships, corporations, and other associations*” Finally, Section 101(11) of the revised Uniform Limited Partnership Act (RULPA), approved by the Conference of Commissioners on Uniform State Laws in 1976, and revised in 1985, a person “*means a natural person, partnership, limited partnership (domestic or foreign), trust estate, association or corporation.*” **Underscore for emphasis only.**

A trustee clearly may hold a donee's interest in a [family] limited partnership on behalf the donee as indicated above under the definition of a "partnership of persons." An independent trustee of an irrevocable trust who is unrelated to the grantor and who receives actual income distributions from the partnership is treated as the real owner of a partnership interest. A trustee is not independent if the trustee is "amenable to the will of the grantor," a much broader standard than the traditional "related or subordinate." Thus, if a trustee is to manage the interest of a donee (or common partners interest), it is advisable to operate as a [family] limited versus general partnership in order to reduce the trustee's responsibilities and duties. [see [Ginsberg v. Commissioner, 502 F. 2d 965 \(6th Cir. 1974\)](#); [Ballou v. United States, 370 F. 2d 663 \(6th Cir. 1966\)](#), cert. Denied, 338 US 911 (1966); [Krause v. Commissioner, 57 TC 890 \(1972\)](#), aff'd, [497 F. 2d 1109 \(6th Cir. 1974\)](#), cert. Denied, 419 US 1108 (1975)]

HOW THE LIMITED PARTNERSHIP IS STRUCTURED

A "family partnership" may be formed either as a general or limited partnership; however, the general partnership is not advisable because all partners share equally in the unlimited liability for the debts of the partnership, without regard to the value of their partnership interest, e.g.; unlimited liability for partnership recourse debts.

All limited partnerships have at least one general partner and at least one limited partner; only the general partner(s) being fully liable for partnership recourse debts; while the limited partner(s) are liable for partnership debts only to the extent of their investment⁷. Section 301(1) of the R.U.P.A. makes it clear that each partner is an "agent" (*one who owes a fiduciary duty of loyalty, care, good faith and fair dealing*) for the partnership and has authority for carrying on all types of business "of the kind carried on by the partnership" whereas Sections 302 and 303 also state that the limited partners generally do not participate in the control of the business, but that the

⁷ LLC members and Corporate shareholders alike may be held personally liable under certain circumstances for all LLC or Corporate obligations, including judgments. CA Corp Code § 17101(b), (c); [People v. Clauson](#), 231 Cal. App. 2d 374, 378, 41 Cal. Rptr. 691 (1964).

partnership agreement may grant the limited partners a vote in partnership affairs. Usually, only the general partners participate in the management of partnership affairs.

ADVANTAGES AND DISADVANTAGES

A [*family*] limited partnership not only affords excellent asset protection but also enables a donor to divided a large asset, or pool of assets, in order to make several smaller gifts, in much the same way that a [*family*] corporation enables a donor to make multiple gifts of some desired number of shares of stock. Like the “S” corporation, a [*family*] partnership preserves the character of items of income, deduction, gain, and loss recognized at the partnership level and taxed directly to the partners.

Family partnerships offer a number of advantages as a means of transferring family wealth.

First, the creation of the family partnership is relatively simple; requiring (i) a partnership agreement, (ii) a deed of gift, and (iii) a partnership certificate. Only one transfer of property must be recorded, since subsequent changes of the donor and donee interest require only an amendment to the partnership agreement. Even for a transfer of real estate, only a single deed needs to be recorded. Even where a transfer of real estate is legally effective without recordation, it is prudent for the donor to record the deed transferring the property to the partnership, to make it clear that the interest of the donee-partners are completely perfected and superior to those of subsequent creditors of the donor.

Second, using a family partnership to make gifts of real estate located in a state in which the donor does not reside can eliminate ancillary probates. Real estate must be probated in the state where it is located - regardless of the state of residence of the deceased owner - but partnership interest is treated as personal property, even if the partnership owns the real estate.

Third, a family partnership enables the donor to retain control over the property being given away. The donor can be designated the general

partner and could retain most or all of the managerial controls over the property, until all of the property has been transferred to the donee-partners, without jeopardizing the estate tax advantages of the partnership. [*see IRS Private Letter Rulings 9415007, 9310039, 9310006.*]

Fourth, a partnership is not a taxable entity⁸ for income tax purposes, so the donor's interest in the family partnership's net income escapes taxation at the partnership level.

Fifth, to a very limited extent, the creation of multi-class partnership interest can be used to effectively freeze the value of the interest of a deceased partner for estate tax purposes.

Sixth, a partnership interest is relatively secure against the claims of the partner's creditors. A judgment creditor of a partner may (through the use of a "*charging order*") force the partner to transfer his or her partnership interest to the creditor, but the transferee becomes an "assignee," rather than a new partner, is merely entitled to receive distributions emanating from the partnership, and is not eligible to participate in partnership activities and management. The assignee may obtain a "*charging order*," only after receiving a judgment (*to be discussed in detail later in this pamphlet*), entitling the assignee to the assignor-partner's share of any partnership distributions that are actually made, and nothing more. Status as an assignee with a *charging order* is generally very undesirable, because the assignee is treated as a partner for federal tax purposes and is taxed on a share of partnership income, even if the partnership does not make any distributions. [*see IRS Revenue Ruling 77-137, 1977-1 CB 178, written in its entirety later in this article.*]

Seventh, an outright gift of a partnership interest in a family partnership (*or a gift in a trust that otherwise qualifies for the gift tax annual exclusion*) is generally eligible for the gift tax annual exclusion. If the donee-partners have the right to withdraw their capital accounts from the partnership (*a*

⁸ A partnership pays no taxes. It is a mere conduit through which all items of partnership income, loss, deduction, gain, or credit are "passed through" to the partners.

withdrawal right similar to a Crummey power), the annual exclusion should also be available for the increased value of a donee-partner's capital account attributable to an additional gift to the partnership by another partner. [*see IRS Private Letter Rulings 9415007, 9310039, 9310006; [Wooley v. United States, 736 F. Supp. 1506 \(D. Ind. 1990\)](#)*]

Family partnerships have relatively few disadvantages as a means of transferring family wealth or as an asset protection vehicle.

One disadvantage is that a donor's annual gifts of partnership interest are valued on the date of each individual gift. Thus, a donor who retains a significant partnership interest in a family partnership in which the underlying assets continues to appreciate in value is credited with the appreciation in the value of the retained interest, making it necessary to make even more gifts to give away the donor's entire asset. [*This same problem exists in outright gifts of partial interest, but does not exist with an installment gift.*]

Secondly, family partnerships are subject to certain special rules ("*the family partnership rules*") that must be met in order for a donee-partner to be recognized as a partner for income tax purposes. Specifically, capital must be a material income-producing factor for the partnership, and the donee-partner must be the real owner of an interest in that capital. If these rules, or test, are not met, partnership income will be taxed solely to the donor and others who invested their own capital or services, depriving the donor of the income-shifting advantages otherwise available through the family partnership. [*see IRS § 704(e)(1); [Culbertson v. United States, 337 US 733 \(1949\)](#); [Carriage Square Inc., v. Commissioner, 69 TC 119 \(1977\)](#); [Poggetto v. United States, 306 F. 2d 76 \(9th Cir. 1962\)](#).]*

HOW THE LIMITED PARTNERSHIP PROTECTS ASSETS FROM LAWSUITS AND PROVIDES SUIT PROTECTION

The Uniform Limited Partnership Act⁹ (U.L.P.A. (1916)), and the Revised

⁹ The Uniform Limited Partnership Act was presented in 1916 by the National Conference of Commissioners on Uniform State Laws (an offshoot of the American Bar Association) and writ-

Uniform Limited Partnership Acts (R.U.L.P.A. (1976 and 1985)), which have been accepted totally or in part by all states, provide in Section 703 that an individual partner's judgment creditor can only go against his limited partnership interest by means of a *charging order*. The court may only "*charge*" the partnership interest of the partner for the benefit of his judgment creditor.

THE LAW: THE CHARGING ORDER

A *charging order* is a statutory creation and is the only means by which a creditor satisfies his judgment against a limited partner. The following are examples of statutes that make *charging orders* the means by which a judgment creditor satisfies his judgment:

1. **California** Corporations Code provides in Section 15673:

On application to a court of competent jurisdiction by any judgment creditor of a partner, the court may charge the limited partnership interest of the partner with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of the limited partnership interest. This chapter does not deprive any partner of the benefit of any exemption laws applicable to the partner's limited partnership interest.

2. **Florida** Partnership Law provides in Section 620.153:

On application to a court of competent jurisdiction by any judgment creditor of a partner, the court may charge the partnership interest of the partner with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the

ten by the Committee on Commercial Law. This Committee was the same group that produced the Uniform Partnership Act of 1914, the Negotiable Instruments Law of 1896, and the Uniform Sales Act of 1906. The Revised Uniform Limited Partnership Act of 1976 was approved by the same organization that presented the 1916 Act. Because of modifications to the 1976 Act by states such as California and Delaware; the 1976 Act was again amended in 1985 to encourage capital investment by offering limited liability. The 1985 Act shifted emphasis from the limited partnership certificate to the agreement as the principal document. Most states now have the 1985 Act adopted in toto or as amendments to the previously adopted 1976 Act.

rights of an assignee of the partnership interest. This act does not deprive any partner of the benefit of any exemption laws applicable to his partnership interest.

3. **Illinois** Partnership Law 106½ in Section 157-3:

On application to a court of competent jurisdiction by any judgment creditor of a partner, the court may charge the partnership interest of the partner with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of the partnership interest to receive distributions. This Act does not deprive any partner of the benefit of any exemption laws applicable to his or her partnership interest.

4. **New York** Partnership Law (Vol. 30) provides in Section 111:

(a) On due application to a court of competent jurisdiction by any judgment creditor of a limited partner, the court may charge the interest of the indebted limited partner with payment of the unsatisfied amount of the judgment debt; and may appoint a receiver, and make all other orders, directions, and inquiries which the circumstances of the case may require.

(b) The interest may be redeemed with the separate property of any general partner, but may not be redeemed with partnership property.

(c) The remedies conferred by subdivision one of this section shall not be deemed exclusive of others which may exist.

(d) Nothing in this act shall be held to deprive a limited partner of his statutory exemption.

5. **Texas** provides in Civil Statutes (Vol. 17, Art. 6132a, Sec. 23):

(a) On due application to a court of competent jurisdiction by any judgment creditor or a limited partner, the court may charge the interest of the indebted limited partner with payment of the unsatisfied amount of the judgment debt; and may appoint a receiver, and make all other orders, directions, and inquiries which the circumstances of the case may require.

(b) The interest may be redeemed with the separate property of any general partner, but may not be redeemed with partnership property.

(c) The remedies conferred by paragraph (a) shall not be deemed exclusive of others which may exist.

(d) Nothing in this Act shall be held to deprive a limited partner of his statutory exemption.

A charging order is defined in American Jurisprudence 2d, Partnerships Section 391:

“A court, on application by any judgment creditor of a partner, may charge the partnership interest of the partner with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of the partnership interest. A partner is not deprived of any exemption laws applicable to his partnership interest.”

THE CHARGING ORDER IS THE ONLY REMEDY

The charging order is the only means by which a creditor can reach the partnership interest (*not assets*) of a limited partner. *See* **LEXIS[®]** **NEXIS[®]** *case beginning on page 29 through page 39 of this handout.*

In a 1986 Florida case, the court again emphasized: “[T]he statutory charging order is the only means by which a judgment creditor can reach the debtor's partnership interest.” [Atlantic Mobile Homes, Inc. v. LeFever, 481 So. 2d 1002 \(Fla. Dist. Ct. App. 1986\).](#)

Similar language was used by a Minnesota Appellate Court in which a creditor was seeking satisfaction of his judgment. The court held “[T]hat a charge order is the exclusive remedy for a judgment creditor of a limited partnership.” [Chrysler Credit Corp. v. Peterson Heller, 342 N.W. 2d 170 \(Minn. App. 1984\).](#)

The Supreme Court of California in [Baum v. Baum, 51 Cal. 2d 610, 335 P. 2d 481 \(1959\)](#) also construed that state's partnership charging order statute and found that a charging order of a partnership interest replaced levies of execution as the remedy for reaching such interests. In upholding the rationale enunciated in [Sherwood v. Jackson, 121 Cal. App. 354, 8 P. 2d 943 \(Cal. Ct. App. 1932\)](#), the court in [Baum, supra](#), determined that a creditor could not "[L]evy attachment or execution on a partner's right in specific partnership property or on his interest in the partnership, but only after first obtaining judgment, pursue the statutory remedy of seeking a charging order."

The decisions of other courts are in line with the reasoning enunciated in [Baum](#). See [Wills v. Wills, 750 S.W. 2d 567 \(Mo.App. 1988\)](#); [Krauth v. First Continental Dev. Constr. Inc., 351 So. 2d 1106 \(Fla. Dist. Ct. App. 1977\)](#).

In a recent bankruptcy proceeding in Georgia, the bankruptcy court stated; "It is clear that the charge order is a substitute for execution, attachment, levy and sale, or garnishment and that the charge order is the exclusive remedy for a creditor of a limited partner." [Matter of Smith, 17 Bankr. 541 \(Bankr. M.D. Ga. 1982\)](#).

The above court also found that several courts in other jurisdictions had similarly analyzed the charging order.

In [Bank of Bethesda v. Koch, 408 A. 2d 767 \(Md. Ct. Spec. App. 1979\)](#), the Court dealt with the nature of a charging order -- that is, whether a charging order against a limited partner is a form of judicial assignment or a form of attachment. Viewing neither alternative description as necessary nor especially desirable, the Court characterized a charging order as follows:

A ... "charging order" is nothing more than a legislative means of providing a creditor some means of getting at a debtor's ill-defined interest in a statutory bastard, sir named 'partnership', but corporately protecting participants by limiting their liability as are corporate shareholders ... Since the statutory offspring is unique, the rights of creditors against partnerships were necessarily peculiar as well; hence the charging order - which like the limited partner to which it applies - is neither fish nor fowl. It is neither an assignment nor an attachment. But, like many such questionable offspring, it resembles both progenitors in some of their characteristics. [Bank of Bethesda v. Koch, 408 A2d 767, 770 \(Md. 1979\)](#); [Tupper v. Kroc., 88 Nev 146, 494 P2d 1275 \(1972\)](#).

CHARGING ORDER IS THE RIGHT TO INCOME ONLY

A charging order gives the judgment creditor only a right to the income portion of the limited partner's interest held by a judgment debtor. The charging order therefore functions as a lien against the partnership interest of the debtor-partner¹⁰. The leading case to support this principle of law is [Evans v. Galardi, 546 P. 2d 313 \(1976\)](#). The California court held:

"...that a limited partner has no interest in the partnership property by virtue of his status as a limited partner, and such assets are not available to satisfy judgment against the limited partner in his individual capacity."

The court further held:

"...that where the judgment creditor could not secure satisfaction of his judgment by attaching personal property of the debtor, the court would make no exception to the general rule that a creditor has rights only to the income portion of a partnership..."

A typical case illustrating this general principle of law is [Rector v. Azzato, 539 A. 2d \(Md. App. 1988\)](#). The Maryland court held:

A partner's interest in partnership property ... is not subject to attachment or garnishment. A creditor of an individual partner is not, however, totally without remedy. He can apply to a court and obtain a charging order. The charging order leaves the partnership intact; it merely entitles the creditor to receive the debtor partner's share of any distribution of profits or capital.

In the previously mentioned Florida case of [Atlantic Mobile Homes Inc.](#), the court also stated:

"In order to proceed against a debtor/partner, a creditor must obtain a charging order pursuant to Florida Statutes Ann. §620.695, Florida Statutes (1985). Even then, the creditor cannot reach partnership assets but can only reach the debtor's share of profits from the partnership."

¹⁰ [City of Ark. City v. Anderson, 752 P2d 673, 684 \(Kan. 1988\)](#)

A judgment creditor cannot unwind the partnership and force sale of the assets. Once a charging order has been obtained, there is no cessation of the debtor partner's status as a partner in all respects, save his entitlement to receive profits and surplus. The judgment creditor who holds the charging order does not become the owner of the interest or a substituted limited partner; he is merely an assignee of the income interest held by the judgment debtor. Axelrod, [The Charging Order - Rights of a Partner's Creditor](#) 36 Ark. Law Rev. 90 (1982-83).

Pursuant to Section 27 of the Uniform Partnership Act and Section 702 of the Uniform Limited Partnership Act (1976), the assignee of a partner's interest does not become a substituted limited partner. Accordingly, without inspection and accounting rights, the assignee is very much at the mercy of the other partners. Crane and Bromberg, [Law of Partnerships](#) § 44, 248 (1968).

A person who owns a partnership interest in a limited partnership owns a personal property right rather than a real property interest, [Matter of Havik](#) 14 Bankr. 635 (Bankr. N.D. Ga. 1981). This personal property right entitles the partner to a pro rata share of the partnership profits and surplus. [Central Allied Profit Sharing v. Bailey](#), 759 P. 2d 849 (Colo. App. 1988). Yet, this does not mean a limited partner holds title to the assets of the partnership; [Centurion Corp. v. Crocker Nat'l Bank](#), 255 Cal. Rptr. 794 (Cal. App. 1989); [Maxco v. Volpe](#), 247 Ga 212, 274 S.E.2d 561 (1981). *See* **LEXIS[®] NEXIS[®]** *printout beginning on page 23 through top third of page 29 of this article.*

Since a limited partner has no rights in the partnership property¹¹ other than his distributive share of income, the income becomes the only means with which to satisfy a judgment the only way to reach that income is through a charging order. Most states codify the foregoing with the following language as reported from California R.U.L.P.A.:

(1) Nature of Partnership Interest. An interest in a limited partnership is personal property and a partner has no interest in specific partnership property (Corp. C. 15671 Both former Corp. C. 15518 and Revised U.L.P.A.

¹¹ Although partnership property is not subject to attachment for a partner's debts, property transferred into the partnership remains subject to all pretransfer liens.

Section 701 provide that an interest in a limited partnership is personal property.).

The lack of "power" and "control" by an assignee of a limited partnership interest is almost universally described in language such as in the [California Case of Kellis v. Ring, App., 155 Cal Rptr. 297](#) (1079), stating:

"While appellant has a right to receive the share of the profits or other compensation by way of income, or the return of his contributions to which his assignor would otherwise be entitled, he has no right to interfere in the management of the limited partnership."

and in the Florida case of [In re Stocks 110 bankr. 65 \(Bankr. N.D. Fla. 1989\)](#), wherein the court held that an assignee had no right to interfere in the management of a limited partnership, stating:

The charging order entitles [plaintiff] to the rights of an assignee of the partnership interest. As an assignee of a partnership interest, [plaintiff] is entitled to share in profits and surplus. This assignment does not dissolve the limited partnership interest or entitle the assignee to become or exercise any of the rights or powers of a partner. **[Emphasis Added]**

To further frustrate a would-be judgment creditor, some attorneys include a clause similar to the following in their Limited Partnership Agreement:

"Distribution of Profits. The earnings of the Partnership shall be distributed at least annually except that earnings may be retained by the Partnership and transferred to Partnership capital for the reasonable needs of the business as determined at the sole discretion of the General Partners."

The effect of this paragraph used in tandem with Internal Revenue Service policy (set forth in [I.R.S. Rev. Rule 77-137](#)) presents a judgment creditor with the "Poison Pill" -- it is often the final knockout blow to a judgment creditor with a charging order against a debtor.

THE JUDGMENT CREDITOR NOW MUST PAY INCOME TAXES ON THE UNDISTRIBUTED PROFITS AND INCOME OF THE PARTNERSHIP IN PROPORTION TO HIS INTEREST AS DETERMINED BY HIS CHARGING ORDER EVEN IF NO INCOME IS DISTRIBUTED BY THE PARTNERSHIP.

This is the ultimate coup de gras !!!

Partnership taxation is one of the most complex and least understood aspects of the Internal Revenue Code. The Tax Court itself has described the partnership provisions of the Code as “distressingly complex and confusing” which “present[s] a formidable obstacle to the comprehension of these provisions ... even by one who is sophisticated in tax matters” whose “complex provisions may confidently be dealt with ... [by] a comparatively small number of specialists ...” [Foxman v. Commissioner, 41 T.C. 535, 551 n.9 \(1964\)](#), aff’d F.2d 466 (3d Cir. 1966).

It is for this reason the Internal Revenue Code states, and we quote in its entirety;

26 CFR 1.761-1: Terms defined.

Limited partnership; assignment of interest. An assignee acquiring substantially all of the dominion and control over the interest of a limited partner is treated as a substituted limited partner for Federal income tax purposes.

REV. RUL. 77-137

“**A**, a limited partner in a limited partnership formed under the Uniform Limited Partnership Act of a state, assigned the limited partnership interest to **B**. The agreement of the partnership provides, in part, that assignees of limited partners may not become substituted limited partners in the partnership without the written consent of the general partners. However, it also provides that a limited partner may, without the consent of the general partners, assign irrevocable to another the right to share in the profits and losses of the partnership and to receive all distributions, including liquidating distributions, to which the

limited partner would have been entitled had the assignment not been made. Under the terms of the assignment **A**, who was the nominal limited partner under local law, agreed to exercise any residual powers remaining in **A** solely in favor of and in the interest of **B**.

Held, even though the general partners did not give their consent to the assignment, since **B**, the assignee, acquired in essence all the dominion and control over the limited partnership interest, for Federal income tax purposes **B** is treated as a substituted limited partner. Therefore, **B** must report the distributive share of partnership items of income, gain, loss, deduction, and credit attributable to the assigned interest on **B**'s Federal income tax return in the same manner and in the same amounts that would be required if **B** was a substituted limited partner."

<<END RULING>>

This revenue ruling is affirmed in [Jackson v. Commissioner](#), 81,594 T.C.M. (P-H) (1981), where the court held, "**if an assignee is determined to be a partner for Federal income tax purposes, he is liable for taxation as a new partner.**" See also, A. Willis, J. Pennell, P. Postlewaite, [Partnership Taxation](#), §2.03, at 2-11 (3d ed. 1981).

LLCS And Charging Order Update

Recently, several states have amended their LLC charging order statutes to specifically allow for foreclosure of a member's interest. Nevada's law is typical:

On application to a court of competent jurisdiction by a judgment creditor of a member, the court may charge the member's interest with payment of the unsatisfied amount of the judgment with interest.

A charging order constitutes a lien on the member's interest of the judgment debtor. The court may order a foreclosure of the member's interest subject to the charging order at any time.

NRS 86.401 (emphasis added).

No Case Could be Found Regarding a Foreclosure of an LLC Interest

Delaware's law is nearly identical. See Del. Laws, Tit. 6, § 18-703. Other states that have made similar changes are Colorado, Illinois, and Utah. See CRS 7-80-703; 805 ILCS 180/30-20; UCA 48-2C-1103. Interestingly, New Jersey amended its charging order statute in 1997 to specifically prohibit the foreclosure of an LLC membership interest. See N. J. Stats. Ann. § 42:2B-45. Most of the other states have the older type of charging order statutes, which do not specifically address the issue of foreclosure.

Not surprisingly, no case could be found regarding a foreclosure of an LLC interest. The newness of the LLC entity, coupled with the relative rarity of the remedy of foreclosure, is the probable cause.

In cases involving the foreclosure of partnership interests following a charging order, there are only two basic requirements that must be met. First, there must be statutory authority for the foreclosure. Second, the owner of the interest must be on notice that the other party is seeking foreclosure. The following cases show this.

In Tupper v. Kroc, 88 Nev. 146, 494 P.2d 1275 (1972), the Nevada Supreme Court upheld a foreclosure of Tupper's partnership interests to satisfy judgment creditor Kroc. The court stated:

The charging order was properly entered by the district court against Tupper's interest in the three partnerships. The district court also was authorized, in aid of the charging order, to make all orders and directions, as the case required. Pursuant to the provisions of this statute the district court was authorized to appoint a receiver to act as a repository for Tupper's share of the profits and surplus for the benefit of Kroc, or as the court did here, order the sale of Tupper's interest. In Kroc's application for the order charging Tupper's interest in the partnerships he requested an order directing a sale of that interest. Likewise in the notice to Tupper and his attorneys they were advised that Kroc was seeking a sale of Tupper's interest. The application and notice afforded Tupper an opportunity to take whatever steps he deemed necessary to either

limit the charging order or prevent the sale. Id. at 151.

In Bohonus v. Amerco, 124 Ariz. 88, 602 P.2d 469 (1979), the trial court issued a charging order in favor of a judgment creditor against Bohonus, and ordered a sale of Bohonus' partnership interest and certain partnership property. The Arizona Supreme Court reversed, holding that partnership property is not subject to attachment except for a debt of the partnership (as opposed to a personal debt of a particular partner). 602 P.2d at 470-71. However, the court upheld the right to sell the partnership interest:

With the foregoing statutes in mind, we note that it is only a partner's interest in the partnership that may be charged and, in some jurisdictions, sold. We concur with Applebee's position that the charged interest of a debtor-partner can be sold, but further enforcement of the creditor's rights must be pursuant to statute. See A.R.S. § 29-232(B) and Tupper v. Kroc, 88 Nev. 146, 494 P.2d 1275 (1972). Bohonus, 602 P.2d at 470.

In First Nat'l Bank of Denver v. District Court, 652 P.2d 613 (Colo. 1982), the trial court entered judgment for the bank against five defendants on a promissory note. The five owned partnership interests in three partnerships. Upon motion, the court charged those interests with payment of the judgment.

For two years, no payments were made by the partnerships to the bank. The bank then asked the judge, in an ex parte hearing with no notice to the partners or partnerships, to order the sale of the partnership interests through foreclosure. The trial court ordered the sale. The Colorado Supreme Court reversed. It did so because of the lack of notice.

The court stated:

The order charging the partnership interests with the judgment and directing the payment of the partners' shares of profits to the judgment creditor, was entered by the court after hearing and notice to all parties. The order was subject to later modification 'upon due application.' We have interpreted that term to mean an application made to the court upon adequate notice to the persons whose rights might be adversely affected by the grant of the relief sought.

We agree with the defendants that the ex parte order for execution and sheriff's sale was improperly entered because it was issued without due application to modify the court's earlier order charging the partnership interests. The court should have conducted another hearing . . . with proper notice to the affected parties. Id. at 617.

The last case is Deutsch v. Wolff, 7 S.W.3d 460 (Mo. App. 1999). Here, the appellate court upheld a charging order against the judgment debtor's partnership interest. The judgment debtor argued the trial court lacked the authority to enter the order. The appellate court disagreed. After reviewing state law, the court stated:

A partner's individual interest is not partnership property and therefore may be sold to satisfy that partner's individual debts. Accordingly, we affirm the trial court's order to authorize sale of Mr. Wolff's interest. Id. at 463.

As these cases reveal, if the law of a particular state does not prohibit foreclosure, and all parties are on notice of the possibility, the remedy is allowed. In the five states mentioned above, Nevada, Delaware, Colorado, Illinois, and Utah, foreclosure of an LLC interest is allowed "at any time" after a charging order is issued. Thus, with proper notice, the remedy will occur in these states (or in other states applying the law of these states).

As revealed in the previous research, the law of the state of formation travels with an LLC. In 49 of the states, this includes all issues of "liability." Thus, where one has a Nevada LLC and does business in California, Nevada law will follow it. This can be both good and bad.

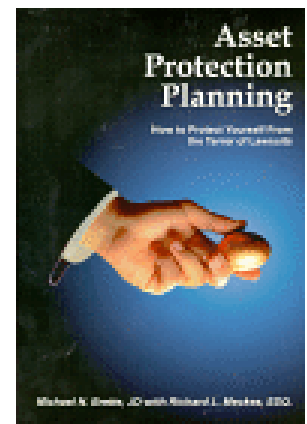
If the LLC owner winds up in litigation in California on a matter related to his business, and the plaintiff attempts to "pierce" the LLC and hold the owner personally liable for the debts of the entity, Nevada's piercing law will be applied. This is a tremendous benefit.

On the other hand, suppose the entity owner is sued for an incident unrelated to the LLC, and the plaintiff obtains a judgment. Upon discovering the existence of the LLC, the plaintiff can ask the California judge for a charging order. Since

Nevada law will apply to this liability issue, the charging order will issue, with the possibility of foreclosure "at any time" thereafter. (The plaintiff can also file his judgment from California in a Nevada district court, thus converting it to a Nevada judgment. He can then ask a Nevada judge for a charging order on the Nevada LLC interest, and get it, with foreclosure to follow.) Will California and other states soon follow Delaware and Nevada lead? Time will only tell, although this appears to be the trend.

Other Readings:

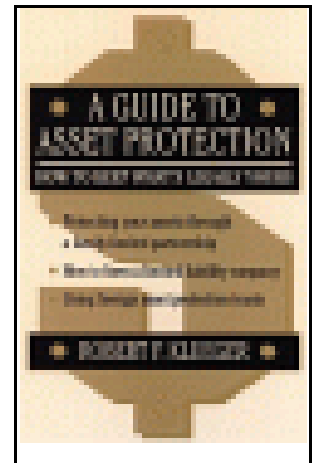
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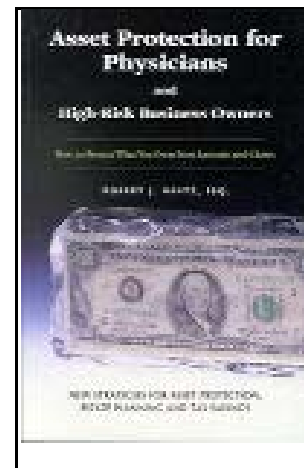
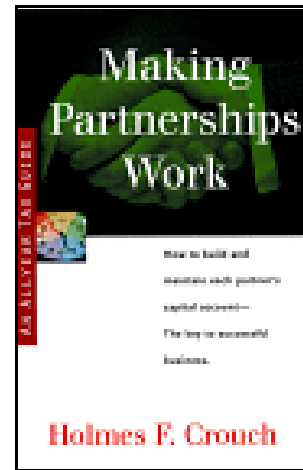
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By Robert F. Klueger, Esq.

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LEXIS® NEXIS® REPORTS

The following two LEXIS® NEXIS® printouts indicate how the same court can rule in two completely opposing manners ... it all depends on the aggressiveness of the Partners to defend the partnership. **Remedies** fall under four discrete formulas available to the court. They are (i) an order charging the interest of the debtor-partner, thereby directing that distributions made with respect to the debtor-partner's interest instead be made to the creditor; (ii) appointment of a receiver for the debtor's share of the profits to be paid to the creditor; (iii) the sale of the debtor's interest (not property) in the partnership; and (iv) possible dissolution of the partnership.

Additionally, it is very doubtful that a general partner owes any duties to the holder of a charging order and furthermore there is no fiduciary relationship between the general partner and the creditor because the creditor is not a partner. [[Kellis v. Ring](#), 92 Cal. App. 3d 854, 859, 155 Cal. Rptr. 297 (1979); [Griffin v. Box](#), 910 F2d 255, 261 n.6 (5th Cir. 1990)]

LEXIS® NEXIS® printout one covers the recent California case of *Crocker National Bank v. Perroton*. In this case, the limited partnership interest was ordered to be sold pursuant to a charging order. The limited partner moved to void the sale but the court, without discussion, held, even though the Uniform Partnership Act (UPA) dealt with general partnerships, it [UPA] had provisions applicable to limited partnerships and therefore stated that the limited partnership interest of the debtor-partner could be sold. The court erred by relying on a flawed California Continuing Education of the Bar publication instead of "full interpretation of the law and court precedence." The opinion of *Perroton* is suspect. The court never specifically discussed whether the UPA provisions were inconsistent with the Revised Uniform Limited Partnership Act (RULPA) provisions.

In our inclosed LEXIS® NEXIS® printout two; the California court in [Hellman v. Anderson](#) disagreed with the portion of the *Perroton* ruling requiring the consent of other partners in order to sell the interest subject to the charging order. *Hellman* involved a general partnership [not a limited partnership], so the court did not have occasion to distinguish between a general and limited partnership.

Even if the *Perroton* ruling is correct, the rights of the purchaser of the limited partnership interest is extremely limited. The purchaser is an assignee and has no voice in the management of the partnership and cannot control partnership investment or require partnership distributions.

2ND CASE of Level 1 printed in FULL format.

*** CROCKER NATIONAL BANK, Cross-complainant and Respondent,
v. JON R. PERROTON, Cross-defendant and Appellant ***

Reporter's Note: This case was previously entitled
"Centurion Corp. v. Crocker Nat. Bank."

No. A039366

Court of Appeals of California, First Appellate District,
Division Two

208 Cal. App. 3d 1; 1989 Cal. App. LEXIS 166; 255 Cal.
Rptr. 794

February 27, 1989

PRIOR HISTORY: [**1]

Superior Court of San Mateo County, No. 288028, Thomas McGinn Smith, Judge.

DISPOSITION: The judgment is affirmed.

COUNSEL: Jon R. Perroton, in pro. per., for Cross-defendant, Plaintiff, and Appellant.

Robert B. Kaplan, Joseph N. Demko and Frandzel & Share for Cross-complainant, Defendant and Respondent.

JUDGES: Opinion by Kline, P. J., with Smith and Benson, JJ., concurring.

OPINION BY: KLINE

OPINION: [*3] Introduction

Jon R. Perroton (Perroton) appeals the denial of his Code of Civil Procedure section 473 motion for an order voiding an order granting Crocker National Bank's motion for sale of Perroton's interest in a limited partnership known as Turn-Key Storage. He contends; (1) the trial court erred in ordering the sale of his partnership interest at an execution sale where the partnership was not the judgment debtor and (2) the order directing sale was precluded by the California Corporations Code and by the partnership agreement itself.

Statement of the Case/Facts

In December 1984, respondent Crocker National Bank (Crocker) obtained a judgment against Perroton for \$1,431,688.29. Thereafter, on February 6, 1985, the bank obtained an order pursuant to Corporations Code [*4] section 15673, charging Perroton's interest [**2] in the limited partnership known as California Self Storage with payment of the unsatisfied judgment plus interest. The charging order was subsequently corrected nunc pro tunc to change the name of the partnership to Turn-Key Storage doing business as California Self-Storage.

As of November 1985, Crocker had received no monies as a result of the charging order against Turn-Key Storage. Therefore, on November 26, 1985, Crocker moved for an order of sale of Perroton's interest in Turn-Key Storage. Notice was served on Perroton, the only limited partner, in care of the Federal Metropolitan Correctional Center in Tucson, Arizona, where he was a prisoner. Notice was also served on counsel for Perroton's mother, Bette Perroton, the only general partner of Turn-Key Storage.

No opposition was filed to the motion for sale. Bette Perroton filed a statement of "conditional non-opposition" to the sale. n1

----- Footnotes -----

n1 According to this declaration: "4. The Partnership does not object to the sale of Jon Perroton's partnership interest at Sheriff's Sale as sought by Crocker Bank provided that the rights of the purchaser at such sale are limited as set forth in the Stipulation and Order and amendment to Certificate of Limited Partnership as described above; to wit, the successor [sic] would have the rights to profits and losses but would not become a substituted limited partner in the Partnership."

----- End Footnotes -----

----- [**3]

After hearing on January 7, 1986, the limited interest in Turn-Key Storage was ordered sold. Perroton, Bette Perroton as general partner, and counsel for the general partner received notice of the order for sale of Perroton's interest in the limited partnership on January 27, 1986.

Approximately 15 months later, on April 22, 1987, Perroton moved pursuant to Code of Civil Procedure section 473, to void the order of sale. This motion was filed after Perroton had filed for bankruptcy and after Crocker had obtained relief from the automatic stay in the bankruptcy to allow it to sell the limited partnership interest of Perroton in Turn-Key Storage.

Perroton's motion to void the order of sale was denied on June 1, 1987. Perroton filed a notice of appeal on June 23, 1987.

[*5] Discussion

I.

The Court Did Not Abuse Its Discretion in Denying Perroton's Motion to Void the Prior Order of Sale

"A motion for relief under section 473 is addressed to the sound discretion of the trial court and an appellate court will not interfere unless there is a clear showing of an abuse. [Citation.] . . . [The] moving party has the burden of showing good cause. [[Citations.](#)]" ([Davis v. Thayer \(1980\) 113 Cal.App.3d 892, 904 \[170 Cal.Rptr. 328\]](#).)

[**4] If the Corporations Code absolutely bars the sale of a partnership interest in satisfaction of a debt of an individual partner, abuse of discretion would be established. n2 However, under the facts presented, we conclude that the order of sale was not void. Hence, the court did not abuse its discretion in denying Perroton's notion.

----- Footnotes -----

n2 If the order of sale were void, abuse of discretion would be established, unless the court denied the section 473 motion for some procedural reason, such as lack of timeliness. Crocker does not contend that Perroton's motion was untimely. It appears the motion was made pursuant to the last sentence in the statute which provides, "The court . . . may, on motion of either party after notice to the other party, set aside any void judgment or order." (Code Civ. [Proc., @ 473.](#)) Unlike that part of the statute allowing relief from a judgment or order taken by mistake, inadvertence, surprise or excusable neglect, no time limits are provided for applications for relief from a void order.

----- End Footnotes -----

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255 Cal. Rptr. 794

[**5]

“A creditor with a judgment against a partner, but not against the partnership, ordinarily cannot execute directly on partnership assets or on the partner's interest in the partnership.” (Advising California Partnerships 2d (Cont.Ed.Bar 1988) @ 6.88, p. 428, citing Code Civ. Proc., @ 699.720; see also Corp. Code, @ 15025, subd. (2) (c).) n3 The reasons for the rule were discussed at some length in [Taylor v. S & M Lamp Co., supra, 190 Cal.App.2d 700, 707-708](#): “Prior to California's adoption of the Uniform Partnership Act (Corp. Code, @ 15001 et seq.) a judgment creditor of a partner whose personal debt, as distinguished from partnership debt, gave rise to the judgment, could cause a sale at execution of partnership assets, [*6] including specific items of partnership property, to satisfy his judgment. [Citation.]”

----- Footnotes -----

n3 Code of Civil Procedure section 699.720 lists among the types of property not subject to levy under a writ of execution, “(2) The interest of a partner in a partnership where the partnership is not a judgment debtor.” Corporations Code section 15025, subdivision (2)(c) provides in relevant part: “A partner's right in specific partnership property is not subject to enforcement of a money judgment, except on a claim against the partnership.”

Courts have allowed the creditor to execute directly on partnership assets in a few situations, such as where partnership assets have been transferred in fraud of creditors. (See [Taylor v. S & M Lamp Co. \(1961\) 190 Cal.App.2d 700, 708, 711 \[12 Cal.Rptr. 323\]](#); 8 Witkin, Cal. Procedure (3d ed. 1985), Enforcement of Judgment @ 290, pp. 249-252; Advising California Partnerships, supra, @ 6.88, p. 428.) No allegation of such attempt at fraudulent transfer has been made here.

----- End Footnotes -----

[**6]

“ . . . ”

“Lord Justice Lindley gave the following reason for the English rule forbidding execution sale of a partner's interest in the partnership to satisfy his nonpartnership debt:

““When a creditor obtained a judgment against one partner and he wanted to obtain the benefit of that judgment against the share of that partner in the firm, the first thing was to issue a fi. fa., n4 and the sheriff went down to the partnership place of business, seized everything, stopped the business, drove the solvent partners wild, and caused the execution creditor to bring an action in Chancery in order to get an injunction to take an account and pay over that which was due the execution debtor. A more clumsy method of proceeding could hardly have grown up.” ([28 Wash.L.Rev. 1](#); see also [9 Cal.L.Rev. 117.](#))”

----- Footnotes -----

n4 The abbreviation for fieri facias, literally “that you cause to be made,” the term used to describe a writ of execution commanding the sheriff to levy and make the amount of a judgment from the goods and chattels of the judgment debtor. (Black's Law Dict. (4th ed. L963 rev.) p. 754.)

----- End Footnotes -----

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[**7]

“It was to prevent such “hold up” of the partnership business and the consequent injustice done the other partners resulting from execution against partnership property that the quoted code sections and their counterparts in the Uniform Partnership Act and the English Partnership Act of 1890 were adopted. As we view those code sections they are not intended to protect a debtor partner against claims of his judgment creditors where no legitimate interest of the partnership, or of the remaining or former partners is to be served.”

Therefore, a judgment creditor must seek a charging order to reach the debtor partner's interest in the partnership. (See Corp. Code, @@ 15028, 15522, 15673; Code Civ. Proc., @@ 699.720, 708.310-708.320; *Advising California Partnership*, supra, @ 6.88, pp. 428-429.) Through a charging order, the court may charge the debtor's interest in the partnership with payment of the unsatisfied judgment, plus interest. The court may also appoint a receiver of subsequent profits or other money due to the debtor partner. (Corp. Code, @ 15028, subd. (1).) n5

----- Footnotes ----- n5
Corporations Code section 15028 provides in relevant part., “(1) On due application to a competent court by any judgment creditor of a partner, the court which entered the judgment, order, or decree, or any other court, may charge the interest of the debtor partner with payment of the unsatisfied amount of such judgment debt with interest thereon; and may then or later appoint a receiver of his share of the profits, and of any other money due or to fall due to him in respect of the partnership, and make all other orders, directions, accounts and inquiries which the debtor partner might have made, or which the circumstances of the case may require. [para.] 2. The interest charged may be redeemed at any time before foreclosure, or in case of a sale being directed by the court may be purchased without thereby causing a dissolution: [para.] (a) With separate property, by any one or more of the partners, or [para.] (b) With partnership property, by any one or more of the partners with the consent of all the partners whose interests are not so charged or sold. [para.] (3) Nothing in this act shall be held to deprive a partner of his right, if any, under the exemption laws, as regards his interest in the partnership.”

Corporations Code section 15673 provides with respect to limited partnerships: “On application to a court of a competent jurisdiction by any judgment creditor of a partner, the court may charge the limited partnership interest of the partner with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of the limited partnership interest. This chapter does not deprive any partner of the benefit of any exemption laws applicable to the partner's limited partnership interest.”

----- End Footnotes -----
[**8]

[*7] Perroton concedes the validity of the charging order obtained by Crocker. He contends, however, that under the foregoing statutory scheme, the court may not order sale of his partnership interest at execution sale. We conclude that the authorities support the order for sale of a judgment debtor partner's partnership interest as distinct from the property of the limited partnership, where the creditor has shown that it was unable to obtain satisfaction of the debt under the charging order, and where the remaining partner, here the general partner Bette Perroton, has consented to the sale.

It is clear that “the limited partner is given no property interest in the specific partnership assets as such. Rather, he is entitled, among other things, ‘to receive a share of the profits or other compensation by way of income, and to the return of his contribution . . .’ (@ 15510, subd. (2).)” (*Evans v. Galardi* (1976) 16 Cal.3d 300, 306-307 [128 Cal.Rptr. 25, 546 P. 2d 313], fn. omitted.) “[The] limited partner has no interest in the partnership property by virtue of his status as a limited partner. Thus, such assets are not available [**9] to satisfy a judgment against

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the limited partner in his individual capacity. [Citation.]” (*Id.*, at p. 307; Corp. Code, @ 15671.) “[The] very nature of the limited partner’s relationship with the business organization indicates that he has no property interest in the specific partnership assets which would render them available to his personal creditors.” (*Evans v. Galardi, supra, at p. 308.*)

The question remains whether, nevertheless, the court may order sale of the debtor’s partnership interest itself as distinct from the partnership assets in the circumstances presented here. We think the answer is yes.

Corporations Code section 15028 itself, which sets forth the creditor’s charging order remedy, refers to the possible court ordered sale of a [*8] partnership interest which is subject to a charging order. Subdivision (2) provides: “The interest charged may be redeemed at any time before foreclosure, or in case of a sale being directed by the court may be purchased without thereby causing dissolution.: [para.](a) With separate property, by any one or more of the partners, [**10] or [para.](b) With partnership property, by any one or more of the partners with the consent of all the partners whose interests are not so charged or sold.” (Italics added.) Referring to this provision, an authoritative treatise on California partnerships states as follows: “The judgment creditor does not own the partnership interest by virtue of the charging order but may become the owner by foreclosing the interest. Any of the other partners may, however, redeem the interest before foreclosure or court-ordered sale, using their individual property or partnership property if all the partners other than the debtor consent.” (*Advising California Partnerships, supra, at p. 429*, italics added.)

Cases requiring creditors to obtain charging orders also indicate that sale of the partnership interest is permissible where the creditor has first obtained a charging order and has demonstrated that monies collected under the charging order are insufficient to satisfy the judgment.

In *Evans v. Galardi, supra, 16 Cal.3d 300*, the court refused to allow a levy on partnership assets to satisfy a partner’s debt. The court required the [**11] creditor to use the charging order instead. However, in so holding, the court stated: “Where, as in the instant case, the partnership is a viable business organization and plaintiff does not show that he will be unable to secure satisfaction of his judgment by use of a charging order or by levy of execution against the debtors’ other personally owned property, there is no reason to permit deviation from the prescribed statutory process.” (*Id.*, at p. 311.) The clear implication is that such levy and sale may, in certain circumstances be permitted even in the absence of fraud.

In *Taylor v. S & M Lamp Co., supra, 190 Cal.App.2d 700*, the creditor obtained a charging order and thereafter without obtaining any court order supplementing the charging order, obtained a writ of execution on his judgment against two partners and caused the sheriff to levy on all the beneficial interests of the two partners in the partnership. The trial court memorandum of opinion read: “The charging order . . . impressed a lien on the interests of Ben and Eugene Stephens in the partnership, but the proceeding thereafter followed [**12] by plaintiff did not conform to the law. Another order could have been obtained directing the sale of said interests.” (*Id.*, at p. 710.) The Court of Appeal termed the trial court memo “a correct statement of the law as applied to the ordinary case,” where the partnership continues and where no fraudulent transfer is made. (*Ibid.*)

[*9] Thus, both the Corporations Code and the cases seem to contemplate that a court may authorize sale of the debtor partner’s partnership interest, even in the absence of fraud, where three conditions are met: first, the creditor has previously obtained a charging order; second, the judgment nevertheless remains unsatisfied; and third, all partners other than the debtor have consented to the sale of the interest.

The concerns which form the basis for the exemption of partnership interests and property are satisfied by this procedure. Allowing sale in such instance is consistent with the purpose of these code sections to avoid disruption

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to the partnership business and with the observation of Taylor that the sections “are not intended to protect a debtor partner against claims of his judgment creditors where [**13] no legitimate interest of the partnership, or of the remaining or former partners is to be served.” ([190 Cal.App.2d at p. 708.](#))

II.

Because the Sale Is of the Limited Partner's Interest in the Partnership and the Remaining Partner Has Consented, the Order of Sale Does Not Violate the Partnership Agreement.

Perroton contends that the order of sale was void as it was inconsistent with the terms of the limited partnership agreement. n6 Perroton points out that he is strictly a limited partner; his interest in the partnership is limited by the agreement to 50 percent of the capital and profits; and he has no cognizable or legal “interest” whatsoever in either the real or personal property of the partnership. Further, he argues that as a limited partner, he has no right to be active in the affairs of the partnership, and he may not sell, assign or encumber his interest in the partnership.

----- Footnotes -----

The order specifically provides. “It Is Hereby Ordered that John Perroton, aka J. Perroton, aka Jon Perroton, aka John R. Perroton, aka Jon R. Perroton's interest in Turn-Key Storage, a California Limited Partnership, doing business as California Self-Storage be sold at execution sale pursuant to Code of Civil Procedure Section 701.530 and Sections 701.545-701.830.” n6

“It Is Further ordered that the Santa Clara County Sheriff sell said interest at execution sale upon the written request of Crocker National Bank upon the receipt of a writ of execution directed against John Perroton, aka J. Perroton, aka Jon Perroton, aka John R. Perroton, aka Jon R. Perroton.” (Italics added.)

----- End Footnotes -----

[**14]

“The judgment creditor does not acquire any greater rights than the debtor is entitled to for his own benefit. [Citations.]” (6 West's U. Laws Ann. (1985) U. Limited Partnership Act, Off. Com. to @ 28.) Just as a charging order cannot grant the creditor a greater interest in the partnership than that of the debtor partner at the time of the order (Corp. Code, @@ 15028, 15673; [Ribero v. Callaway \(1948\) 87 Cal.App.2d 135, 138 \[196 P.2d \[**10\] 1091; \[Advising California Partnerships, supra, at p. 429\]\(#\)\]](#)), a supplementary order for sale, does not allow the purchaser to acquire more rights in the partnership than the debtor partner possessed.

Nevertheless, as the Nevada Supreme Court pointed out in rejecting a debtor partner's claim that assignment of his partnership interest was inconsistent with the terms of the partnership agreement: “[The] partnership agreements could not divest the district court of its powers provided by statute to charge and sell an interest of a partner in a partnership.” ([Tupper v. Froc \(1972\) 88 Nev. 146 \[494 P.2d 1275, 1280\]](#).)

Crocker concedes that the “sale of Perroton's interest [**15] in Turn-Key Storage ordered by the superior court is not an order for the sale of any real or personal property owned by Turn-Key Storage. To the contrary, it is simply a sale of whatever interest, legal, equitable, or otherwise, which Perroton holds in Turn-Key Storage by virtue of his being a limited partner. The eventual purchaser . . . will acquire no greater rights . . . than Perroton would have if he had remained a limited partner.”

Further, both the limited partnership agreement and the consent to the sale by Bette Perroton make clear that a purchaser of Perroton's limited partnership interest would have rights to profits and losses, but would not become

208 Cal. App. 3d 1, *9; 1989 Cal. App. LEXIS 166, **13;
255 Cal. Rptr. 794

a substituted limited partner in the partnership, absent consent by the general partner.

For these reasons, it is apparent that there is no inconsistency between the agreement and the court's order granting Crocker's motion for sale of Perroton's partnership interest.

As we see no statutory prohibition on the sale in these circumstances and sale does not violate the terms of the limited partnership agreement, the court did not abuse its discretion in denying Perroton's Code of Civil Procedure section 473 motion.

The judgment [**16] is affirmed.

[EMPHASIS ADDED]

233 Cal. App. 3d 850 printed in FULL format.

*** FRED N. HELLMAN et al., Plaintiffs and Respondents, v. JOHN B. ANDERSON, Defendant and Appellant; EUREKA FEDERAL SAVINGS AND LOAN ASSOCIATION, Interveners and Appellants. ***

No. C008611.

Court of Appeal of California, Third Appellate District

[233 Cal. App. 3d 840](#); 1991 Cal. App. LEXIS 979; 284 Cal. Rptr. 830; [91 Daily Journal DAR 10708](#)

August 20, 1991.

NOTICE: [**1] THE LEXIS PAGINATION OF THIS DOCUMENT IS SUBJECT TO CHANGE PENDING RELEASE OF THE FINAL PUBLISHED VERSION.

PRIOR HISTORY:

Superior Court of Yolo County, No. 52196, Frank D. Francis, Judge. n*

n* Judge of the Nevada Superior Court sitting under assignment by the Chairperson of the Judicial Council.

DISPOSITION: Affirmed.

COUNSEL:

Calfee & Young, Kent N. Calfee and Christopher J. Konwinski for Defendant and Appellant.

Steeffel, Levitt & Weiss, Michael J. Lawson, Leonard H. Watkins, Hansen, Boyd, Culhane & Watson, Kevin R. Culhane and Betsy S. Kimball for Interveners and Appellants.

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Services of Mead Data Central, Inc.

Page 30 of 43.

Reuben, Quint & Valkevich, Matthew F. Quint and Jeffrey S. Rosen for Plaintiffs and Respondents.

JUDGES: Sims, J. Sparks, Acting P.J., Davis, J., concur.

OPINION BY: SIMS

OPINION: [*842] SIMS, J.

In this case, we hold that a judgment debtor's interest in a partnership (meaning the right to share in the profits and surplus) may be foreclosed upon and sold, even though other partners do not consent to the sale, provided foreclosure does not unduly interfere with the partnership business.

Judgment debtor John B. Anderson (Anderson) appeals from the trial court's order authorizing the foreclosure and sale of Anderson's interest in a California general partnership [**2] known as Rancho Murieta Investors (RMI). The foreclosure and sale was requested to enforce a money judgment against Anderson in his individual capacity by judgment creditors Fred N. [*843] Hellman, Peter N. Hellman, Lesleigh A. Hellman, Judith S. Johnson, and D. James Fajack (hereafter collectively referred to as Hellman). Interveners Eureka Federal Savings and Loan Association (Eureka) and Eric J. Tallstrom (Tallstrom) have also appealed the trial court's order. Eureka is Anderson's largest creditor. Tallstrom is Anderson's partner in RMI.

Appellants contend (1) the foreclosure sale is not authorized by law where the partnership is not the judgment debtor and (2) sale cannot be ordered where, as here, the "innocent" partner does not consent. Anderson additionally argues the trial court abused its discretion in ordering foreclosure in this case. We will conclude that such foreclosure is authorized by law and, while consent of nondebtor partners is not an inflexible requirement, the trial court should consider whether foreclosure of a charged partnership interest will unduly interfere with partnership business before the court exercises its equitable powers to order foreclosure. [**3] Because the parties in this case relied on authority requiring nondebtor partner consent, no evidentiary showing was made on the effect of foreclosure on partnership business. We therefore reverse the trial court's order directing foreclosure and remand for the trial court to make a finding whether foreclosure will unduly interfere with partnership business.

FACTUAL AND PROCEDURAL BACKGROUND

In 1985 and 1986, Hellman filed lawsuits against Anderson for accounting, breach of contract, breach of fiduciary duty, mandatory injunction, rescission, and fraud. In 1987, Anderson and Hellman settled the suits. Anderson failed to make any of the payments required by the settlement agreements, and in October 1987, stipulated judgments totaling more than \$440,000 were entered against Anderson and in favor of Hellman.

In July 1988, after various unsuccessful attempts to enforce the judgments, Hellman obtained an "Order Charging Debtor John B. Anderson's Partnership Interest" in RMI pursuant to Corporations Code section 15028. nl Anderson owns 80 percent of RMI; Tallstrom owns the other 20 percent and is the managing partner of RMI. The charging order stated that Anderson's interest in RMI [**4] was charged with the unsatisfied judgment in the amount of \$494,885 plus interest. Thus, all profits or other monies due Anderson by virtue of the charged partnership interest were thereafter to be conveyed to Hellman.

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284 Cal. Rptr. 830

nl Undesignated statutory references are to the Corporations Code.

----- End Footnotes -----

Despite the above orders, Hellman has not received any monies in satisfaction of the judgments. Anderson testified in an October 1988 debtor's [*844] examination that RMI had not generated profits and was not expected to do so in the near future.

In December 1988, Hellman filed a motion for an order authorizing and directing a foreclosure sale of Anderson's charged partnership interest in RMI, based on the unlikelihood that the charging order would result in satisfaction of the judgment within a reasonable time. On December 15, 1989, the trial court ordered that the interest of the judgment debtor in the profits and surplus of RMI would be sold at a public sale by the Sheriff of Yolo County. The trial court retained jurisdiction [**5] over all phases of the sale.

All appellants assign error to the trial court's order directing foreclosure and sale of the partnership interest. n2

----- Footnotes -----

n2 All appellants filed notice of appeal from the December 15, 1989, order directing foreclosure of the partnership interest. Additionally, Anderson appeals from the trial court's March 2, 1990, denial of a motion for new trial and Eureka appeals from a denial of a motion for reconsideration on the same date. However, denial of a motion for new trial is not an appealable order. ([Rodriguez v. Barnett \(1959\) 52 Cal.2d 154, 156 \[338 P.2d 907\]](#).) Anderson's appeal from this nonappealable order is dismissed. Assuming denial of the motion for reconsideration is an appealable order (but see [Rojas v. Riverside General Hospital \(1988\) 203 Cal.App.3d 1151, 1160-1161 \[250 Cal.Rptr. 435\]](#), overruled by the same court on other grounds in [Passavanti v. Williams \(1990\) 225 Cal.App.3d 1602, 1607 \[275 Cal.Rptr. 887\]](#)), Eureka raises no issues as to the merits of the ruling on reconsideration.

----- Footnotes -----

[**6]
DISCUSSION

I. California's Uniform Partnership Act (@ 15001 et seq.) Authorizes Foreclosure of a Partner's Charged Interest Without the Consent of the Other Partners.

Appellants contend foreclosure of Anderson's charged interest in RMI is contrary to law. Anderson argues foreclosure was improper because a partnership interest is statutorily exempt from execution. All appellants argue that the trial court cannot order foreclosure unless the nondebtor partners consent.

A. The applicable statutes authorize the foreclosure of a charged partnership interest.

In [Crocker Nat. Bank v. Perroton \(1989\) 208 Cal.App.3d 1 \[255 Cal.Rptr. 794\]](#), n3 the First District recently addressed the question whether a charged partnership interest was subject to foreclosure and sale. Crocker's analysis [*845] begins with a summary of the background of the adoption of relevant provisions of the Uniform Partnership Act:

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284 Cal. Rptr. 830

n3 Appellants originally cited this case by the caption under which it appeared in the advance sheets Centurion Corp. v. Crocker National Bank.

----- Footnotes -----
[**7]

“A creditor with a judgment against a partner but not against the partnership ordinarily cannot execute directly on partnership assets or on the partner's interest in the partnership.” (Advising California Partnerships 2d (Cont.Ed.Bar 1988) @ 6.88, p. 428, citing Code Civ. Proc., @ 699.720; see also Corp. Code, @ 15025, subd. (2)(c).) The reasons for the rule were discussed at some length in [Taylor v. S & M Lamp Co . \[\(1961\)\] 190 Cal.App.2d 700, 707-708 \[12 Cal.Rptr. 323\]](#): “Prior to California's adoption of the Uniform Partnership Act (Corp. Code, @ 15001 et seq.) a judgment creditor of a partner whose personal debt, as distinguished from partnership debt, gave rise to the judgment, could cause a sale at execution of partnership assets, including specific items of partnership property, to satisfy his judgment. [Citation.]” n4 [OMITQE]

----- Footnotes -----

n4 Section 15028, as part of the Uniform Partnership Act, was adopted in 1949. (Stats. 1949, ch. 383, @ 1.) We note, however, the same provisions regarding partnership interests and charging orders were previously contained in Civil Code, sections 2418 to 2422. (Stats. 1929, ch. 864, pp. 1903-1904.) [Sherwood v. Jackson \(1932\) 121 Cal.App. 354 \[8 P.2d 943\]](#) held a creditor could not properly proceed by execution sale pursuant to an ex parte order to levy execution on the debtor's partnership interest. The creditor's remedy was through the charging order procedure. ([Id. at pp. 356-357.](#))

----- End Footnotes -----
[**8]

Lord Justice Lindley gave the following reason for the English rule forbidding execution sale of a partner's interest in the partnership to satisfy his nonpartnership debt:

“When a creditor obtained a judgment against one partner and he wanted to obtain the benefit of that judgment against the share of that partner in the firm, the first thing was to issue a fi . fa . [’ fieri facias' term used to describe writ of execution commanding the sheriff to levy on goods and chattels], and the sheriff went down to the partnership place of business, seized everything, stopped the business, drove the solvent partners wild, and caused the execution creditor to bring an action in Chancery in order to get an injunction to take an account and pay over that which was due the execution debtor. A more clumsy method of proceeding could hardly have grown up.” ([28 Wash.L.Rev. 1](#); see also [9 Cal.L.Rev. 117.](#))

“It was to prevent such ‘hold up’ of the partnership business and the consequent injustice done the other partners resulting from execution against partnership property that the quoted code sections and their counterparts in the Uniform Partnership Act and [**9] the English Partnership Act of [1846] 1890 were adopted. As we view those code sections they are not intended to protect a debtor partner against claims of his judgment creditors where no legitimate interest of the partnership, or of the remaining or former partners is to be served.”

“Therefore, a judgment creditor must seek a charging order to reach the debtor partner's interest in the partnership. (See Corp. Code, @@ 15028, 15522, 15673; Code Civ. Proc., @@ 699.720, 708.310-708.320; [Advising California Partnership, supra , @ 6.88, pp. 428-429.](#)) Through a charging order, the court may charge

the debtor's interest in the partnership with payment of the unsatisfied judgment, plus interest. The court may also appoint a receiver of subsequent profits or other money due to the debtor partner. (Corp. Code, @ 15028, subd. (1).)" (Crocker, supra, 208 Cal.App.3d at pp. 5-6, fns. omitted.)

Crocker concluded the trial court could order the "sale of a judgment debtor partner's partnership interest as distinct from the property of the partnership, where the creditor has shown that it was unable to obtain satisfaction of the debt under the charging [**10] order, and where the remaining partner [] has consented to the sale." (Id. at p. 7.)

Crocker's requirement of nondebtor partner consent will be discussed below. Before reaching that question, we must reexamine another question resolved in Crocker whether foreclosure is authorized at all. Our reexamination is necessary because appellants tender some statutory arguments not considered by Crocker. We therefore begin with the basics, discuss the applicable statutes, and conclude Crocker correctly decided that court-ordered foreclosure and sale of a charged partnership interest is statutorily authorized.

First, we clarify the nature of the property interest at issue in this case, i.e., Anderson's interest in the partnership, not in the partnership property.

"A partner's right in specific partnership property is not subject to enforcement of a money judgment, except on a claim against the partnership. . . (@ 15025, subd. (2)(c).)"

However, a partner's right in specific partnership property is different from his interest in the partnership. "The property rights of a partner are (1) his rights in specific partnership property, [**11] (2) his interest in the partnership, and (3) his right to participate in the management." (@ 15024, italics added.) "A partner's interest in the partnership is his share of the profits and surplus, and the same is personal property." (@ 15026.)

[*847] Code of Civil Procedure section 708.310 provides: "If a money judgment is rendered against a partner but not against the partnership, the judgment debtor's interest in the partnership may be applied toward the satisfaction of the judgment by an order charging the judgment debtor's interest pursuant to Section 15028 [general partnership] or 15673 [limited partnership] of the Corporations Code."

Section 15028 n5 authorizes a charging order on the debtor partner's partnership interest and further allows the trial court to "make all other orders . . . which the circumstances of the case may require." (@ 15028, subd. (1); see also 6 West's U.Laws Ann. (1969) Uniform Partnership Act, @ 28.) The statute clearly implies judicial authority to order foreclosure and sale of the charged interest because it further says the interest charged may be redeemed "at any time before foreclosure, or in case of a sale being directed by the court" [**12] may be purchased by nondebtor partners without causing a dissolution of the partnership. (@ 15028, subd. (2), italics added.) "It is a settled axiom of statutory construction that significance should be attributed to every word and phrase of a statute, and a construction making some words surplusage should be avoided." (People v. Woodhead (1987) 43 Cal.3d 1002, 1010 [239 Cal.Rptr. 656, 741 P.2d 154].) We cannot imagine why the statute would give advice about redemption prior to foreclosure and sale unless foreclosure and sale were contemplated.

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n5 Section 15028 provides: "(1) On due application to a competent court by any judgment creditor of a partner, the court which entered the judgment, order, or decree, or any other court, may charge the interest of the debtor partner with payment of the unsatisfied amount of such judgment debt with the interest thereon; and may then or

later appoint a receiver of his share of the profits, and of any other money due or to fall due to him in respect of the partnership, and make all other orders, directions, accounts, and inquiries which the debtor partner might have made, or which the circumstances of the case may require.”

“(2) The interest charged may be redeemed at any time before foreclosure, or in case of a sale being directed by the court may be purchased without thereby causing a dissolution :”

“(a) With separate property, by any one or more of the partners, or”

“(b) With partnership property, by any one or more of the partners with the consent of all the partners whose interests are not so charged or sold.”

“(3) Nothing in this act shall be held to deprive a partner of his right, if any, under the exemption laws, as regards his interest in the partnership.” (Italics added.)

----- End Footnotes -----

[**13]

Foreclosure sales of charged partnership interests are also implicitly recognized in section 15032 n6 which deals with partnership dissolutions and makes reference to “the purchaser” of a partner's interest under section 15028.

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n6 Section 15032 provides in part;

“(2) On the application of the purchaser of a partner's interest under Sections 15027 [conveyance of partnership interest] and 15028 [fn. 5, ante] [the court shall decree a dissolution].”

“(a) After the termination of the specified term or particular undertaking,”

“(b) At any time if the partnership was a partnership at will when the interest was assigned or when the charging order was issued.”

----- Footnotes -----

[*848] Anderson contends foreclosure is contrary to law because Code of Civil Procedure section 699.720, subdivision (a) n7 says a partnership interest is not subject to execution where the partnership is not a judgment debtor. Anderson notes that section 15028, subdivision (3) (fn. 5, ante), specifies the charging order statute does not affect a partner's [**14] right under the exemption laws.

----- Footnotes -----

n7 Code of Civil Procedure section 699.720 provides in part., “(a) The following types of property are not subject to execution: . . . [P] (2) The interest of a partner in a partnership where the partnership is not a judgment debtor. . . . [P] (b) Nothing in subdivision (a) affects or limits the right of the judgment creditor to apply property to the satisfaction of a money judgment pursuant to any applicable procedure other than execution.”

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However, contrary to Anderson's argument, "the exemption laws" do not exempt a partnership interest from enforcement of judgment. Those exemptions which protect property from enforcement of judgment are found in article 3 "Exempt Property" (Code Civ. Proc., @@ 704.010-704.210) of chapter 4 "Exemptions" (Code Civ. Proc., @ 703.010 et seq.) of division 2 ("Enforcement of Money Judgments") of title 9 ("Enforcement of Judgments") of the Code of Civil Procedure. Partnership interests are not listed as exempt property under Article 3. (Code Civ. Proc., [**15] @@ 704.010-704.210.)

Subdivision (a) of Code of Civil Procedure section 699.720, on which Anderson relies, protects a partnership interest only from execution, not from enforcement of judgment. Thus, subdivision (b) of section 699.720 provides: "Nothing in subdivision (a) affects or limits the right of the judgment creditor to apply property to the satisfaction of a money judgment pursuant to any applicable procedure other than execution." As we shall explain, foreclosure of a statutory charging order is a "procedure other than execution."

Code of Civil Procedure section 699.720 is found in chapter 3 ("Execution" @ 699.010 et seq.) of division 2 ("Enforcement of Money Judgments" @ 695.010 et seq.) of title 9 ("Enforcement of Judgments" @ 680.010 et seq.).

As we have noted, charging orders are authorized under Code of Civil Procedure section 708.310. That section is part of chapter 6 "Miscellaneous Creditors' Remedies" (Code Civ. Proc., @ 708.010 et seq.).

There is a difference between an execution sale (pursuant to a writ of execution) and a foreclosure sale (of a debtor partner's charged interest). Code of Civil Procedure section 699.510 provides in part that, with exceptions [**16] inapplicable here, "after entry of a money judgment, a writ of [*849] execution shall be issued by the clerk of the court upon application of the judgment creditor and shall be directed to the levying officer in the county where the levy is to be made and to any registered process server." Thus, in ordinary civil actions, after entry of a money judgment and upon the judgment creditor's application, the court clerk acts in a ministerial capacity and has no discretion to refuse issuance of a writ of execution. ([in re Marriage of Farner \(1989\) 216 Cal.App.3d 1370 \[265 Cal.Rptr. 531\]](#).) The levying officer then executes the writ in accordance with written instructions of the judgment creditor. (Code Civ. Proc., @ 699.530.) No court intervention is required.

In contrast, a court-ordered, sale to foreclose the lien n8 created by a charging order on a partnership interest involves judicial supervision. The charging order procedure has replaced levies of execution as the remedy for reaching partnership interests. ([Baum v. Baum \(1959\) 51 Cal.2d 610, 612-613 \[335 P.2d 481\]](#).)

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n8 Code of Civil Procedure section 708.320 provides; "(a) Service of a notice of motion for a charging order on the judgment debtor and an the other partners or the partnership creates a lien on the judgment debtor's interest in the partnership. [P] (b) If a charging order is issued, the lien created pursuant to subdivision (a) continues under the terms of the order. If issuance of the charging order is denied, the lien is extinguished."

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Thus, Code of Civil Procedure section 699.720, subdivision (a) on which Anderson relies, is inapplicable because Hellman seeks to foreclose on the charging order, not to proceed by writ of execution.

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As we have mentioned, the statutory authority for the sale of a partnership interest in satisfaction of a debt of an individual partner was recognized in [Crocker Nat. Bank v. Perroton, supra, 208 Cal.App.3d 1](#). Courts from other jurisdictions have agreed that the charging order provision of the Uniform Partnership Act authorizes sale of a charged partnership interest. ([FDIC v. Birchwood Builders \(1990\) 240 N.J.Super. 260 \[573 A.2d 182\]](#); [Wills v. Wills \(Mo.App. 1988\) 750 S.W.2d 567](#); [Bohonus v. Amerco \(1979\) 124 Ariz. 88 \[602 P.2d 469\]](#); [Tupper v. Kroc \(1972\) 88 Nev. 146 \[494 P.2d 1275\]](#); [Beckley v. Speaks \(1963\) 39 Misc.2d 241 \[240 N.Y.S.2d 553\]](#); see First Nat. Bank of Denver v. District Court (Colo. 1982) 652 P.2d 613.) In Tupper v. Kroc, supra [**18] the Nevada Supreme Court affirmed denial of a motion to set aside a court-ordered sale of a charged partnership interest. The Nevada statute, just as Californian's, authorized the trial court to make all orders and directions as the case required, and this, said the court, included sale of the charged interest. ([494 P.2d at P. 1278](#).) Bohonus V. Amerco, supra, emphasized the distinction between a partnership "interest" and partnership "property," the latter of which may not be sold. ([602 P.2d at p. 471](#).)

[*850] Anderson attempts to distinguish cases from other jurisdictions by referring to the California rule that a partnership interest is not subject to execution. (Code. Civ. [Proc., @ 699.720](#), subd. (a), fn. 7, ante .) However, as we have discussed, that statute is not implicated in court-ordered foreclosures.

Eureka mentions Georgia law as precluding a forced sale; however, the cited law review article merely indicates that Georgia's statute, by not providing for foreclosure, differs from the [Uniform Partnership Act. \(Ribstein, An Analysis of Georgia's New Partnership Law \(1985\) \[**19\] 36 Mercer L.Rev. 443, 490](#).) The Georgia statute says a charged interest "is not liable to be seized and sold by the judgment creditor under execution." (Ga. Code Ann. @ 14-8-28, sub d. (b).) We are presented with no persuasive authority or argument that the Georgia statute compels a prohibition against foreclosure and sale otherwise authorized in California by section 15028.

Other commentators, though cited by Eureka, support Hellman's position that the Uniform Partnership Act's charging order provision is widely accepted as authorizing the sale of the charged partnership interest. ([Gose, The Charging Order Under the Uniform Partnership Act \(1953\) 28 Wash.L.Rev. 1, 6-7, 10-12, 16](#) [partnership interest may be sold if charging order ineffectual]; [Lewis, The Uniform Partnership Act \(1915\) 24 Yale L.J. 617, 634](#) [charging order avoids undue interference with rights in partnership business and property].)

Anderson is concerned that the sale will detrimentally affect his other creditors, whose interests are subordinate to Hellman. However, the priority of creditors' interests is not a legitimate concern. Creditors with subordinate [**20] interests are always subject to the interests of prior creditors.

We conclude section 15028 authorized the trial court's order directing foreclosure and sale of the charged partnership interest. ([Crocker, supra, 208 Cal.App.3d at pp. 8-9](#).)

B. The consent of nondebtor partners is not invariably required.

In Crocker, the nondebtor partner effectively consented to the foreclosure and sale of a limited partnership interest. Crocker concluded a trial court "may authorize sale of the debtor partner's partnership interest even in the absence of fraud, where three conditions are met: first, the creditor has previously obtained a charging order; second, the judgment nevertheless remains unsatisfied; and third, all partners other than the debtor have consented to the sale of the interest." ([Crocker, supra, 208 Cal.App.3d at p. 9](#).)

[*851] Appellants contend Crocker requires that nondebtor partners consent to foreclosure and that the trial court here erred in deciding Crocker's statement was mere dictum. Hellman considers the consent requirement in Crocker

to be dictum because the nondebtor [**21] partner in that case had effectively consented to the sale and therefore the issue of partner consent was never raised. While we agree Crocker Is consent requirement was not dictum, we disagree with Crocker Is requirement that other partners must invariably consent to a foreclosure sale. n9

----- Footnotes -----

n9 It is undisputed in this case that the nondebtor partner, Tallstrom, does not consent. We agree with appellants that Tallstrom's prior consent to Anderson's assignment of his interest to Eureka as collateral has no bearing on the question of consent in the context of this dispute. Nor do we consider it relevant that Tallstrom did not seek to oppose the order imposing the charging order in the first place. On the other hand, we do not consider Tallstrom's consent compelled by the trial court's rulings (1) that Tallstrom was entitled to notice of the foreclosure motion, or (2) that Tallstrom be permitted to intervene.

----- End Footnotes -----

The ratio decidendi, as opposed to dictum, is the “principle or rule which constitutes the ground of the [**22] decision, and it is this principle or rule which has the effect of a precedent. It is therefore necessary to read the language of an opinion in the light of its facts and the issues raised, to determine (a) which statements of law were necessary to the decision, and therefore binding precedents, and (b) which were arguments and general observations, unnecessary to the decision, i.e., dicta, with no force as precedents.” (9 Witkin, Cal. Procedure (3d ed. 1985) Appeal, @ 783, p. 753.)

There can be no dispute that the partner consent requirement was necessary to the Crocker decision. The court said so. That consent was given in that case does not mean the issue, was not raised; it merely means the requirement imposed by the court was met.

Nevertheless, we respectfully disagree with that requirement.

First, the statutes do not say that nondebtor partner consent is required for foreclosure on a charging order. Yet section 15028, subdivision (2)(b) (fn. 5, ante) expressly requires the consent of nondebtor partners before partnership property may be used to redeem the charged interest. Plainly, if the Legislature wants to make partner consent a condition, it knows how to do so. [**23] Thus, the very code provision authorizing foreclosure expressly requires consent of nondebtor partners in connection with redemption but is silent on the question of nondebtor partner consent in connection with foreclosure. “[W]hen the drafters of a statute have employed a term in one place and omitted it in another, it should not be inferred where it has been excluded.” (People v. Woodhead, supra, 43 Cal.3d at p. 1010.)

A second consideration is the policy underlying the Uniform Partnership Act of avoiding undue interference with partnership business. [*852] ([Crocker, supra, 208 Cal.App.3d at p. 9.](#)) However, we do not think that foreclosure of a partner's interest will always unduly interfere with the business of the partnership. This is because the statutory scheme itself limits the interest subject to foreclosure and sale. As we have mentioned, a partner's “interest in the partnership” is a personal property right separate and distinct from the partner's (1) rights in specific partnership property and (2) right to participate in management. (@@ 15024, 15026.) The “interest in the partnership” [**24] means only the partner's share of profits and surplus. (@ 15026.) Foreclosure entails no execution upon partnership assets, and the interest acquired by foreclosure does not include the right to participate in management.

The limited nature of the interest being sold was emphasized in [Beckley v. Speaks, supra, 240 N.Y.S.2d 553](#). That case held that, under the Uniform Partnership Act provisions, the purchaser of a charged liquor store partnership interest acquired only the debtor partner's share of profits and surplus and did not acquire any interest

in specific partnership property or any right to participate as partner in applying for renewal of the liquor license. ([Id. at pp. 556-557.](#))

We conclude that since the interest acquired by the purchaser of a partnership interest is limited by operation of law to the partner's share of profits and surpluses, with no acquisition of interest in partnership property or management participation, the foreclosure and sale of the partnership interest will not always unduly interfere with the partnership business to the extent of requiring consent of the nondebtor partners. In some cases, foreclosure [**25] might cause a partner with essential managerial skills to abandon the partnership. In other cases, foreclosure would appear to have no appreciable effect on the conduct of partnership business. Thus, the effect of foreclosure on the partnership n10 should be evaluated on a case-by-case basis by the trial court in connection with its equitable power to order a foreclosure.

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n10 Eureka contends the trial court failed to consider its interests as senior lienholder. However, the interest at issue is the effect of the court's order on the partnership, not upon other creditors.

----- End Footnotes -----

Because we believe the effect of foreclosure on the partnership should be determined on a case-by-case basis, we respectfully disagree with Crocker's inflexible requirement of partners' consent in order for the court to authorize a sale of a charged partnership interest. n11

----- Footnotes -----

n11 The parties do not challenge the other two prerequisites to foreclosure that (1) the creditor previously obtained a charging order, and (2) the judgment nevertheless remained unsatisfied. ([Crocker, supra, 208 Cal.App.3d at p. 9.](#)) The first condition seems obvious obtaining a charging order is a prerequisite to foreclosing on the charging order. The second condition that the charging order be unsuccessful is, we believe, implied in the statute, which authorizes "all other orders . . . which the circumstances of the case may require." (@ 15028, subd. (1), fn. 5, ante.)

----- End Footnotes -----

[**26]

[*853] In this case, we are not satisfied that a full record was made on the effect of foreclosure on the partnership, because appellants apparently relied on the consent requirement found in [Crocker, supra, 208 Cal.App.3d 1](#). Therefore, no evidentiary showing of the effect on partnership business was made. The trial court rejected Crocker's consent requirement as dictum and found, in line with the other two requirements set forth in Crocker's that: "Judgment creditors have received nothing from their Charging Order. It is unlikely that the Judgment will be satisfied within a reasonable time." Thus, we cannot infer that the trial court considered the effect on partnership business before granting the equitable relief sought by Hellman.

Since we disagree with Crocker's consent requirement, remand is required in order for the trial court to make a finding, upon such evidence as may be presented by the parties, on the question whether foreclosure in this case will unduly interfere with partnership business of the nondebtor partnership.

On remand, the burden of proving undue interference with partnership business will be upon defendant [**27] and appellant Anderson. Evidence Code section 500 provides, "Except as otherwise provided by law I a party has

the burden of proof as to each fact the existence or nonexistence of which is essential to the claim for relief or defense that he is asserting.” (italics added.) “The general rule allocating the burden of proof applies ‘except as otherwise provided by law.’ The exception is included in recognition of the fact that the burden of proof is sometimes allocated in a manner that is at variance with the general rule. In determining whether the normal allocation of the burden of proof should be altered, the courts consider a number of factors: the knowledge of the parties concerning the particular fact, the availability of the evidence to the parties, the most desirable result in terms of public policy and the absence of proof of the particular fact, and the probability of the existence or nonexistence of the fact.” (Cal. Law Revision Com. com., 29B West’s Ann. Evid. Code, @ 500 (1966 ed.), p. 430, Deering’s Ann. Evid. Code, @ 500 (1986 ed.) p. 215; see 1 Witkin, Cal. Evidence (3d ed. 1986) Burden of Proof and Presumptions, @@ 136-138, pp. 119-121.) Here, because knowledge [**28] about (and evidence of) the effect of foreclosure upon the partnership is peculiarity known to defendant and appellant Anderson, in his capacity as a partner, the burden of proving undue interference as a consequence of foreclosure is properly placed upon him.

Since we conclude remand is necessary, we need not address appellants’ other contentions that the trial court abused its discretion.

[*854] **DISPOSITION**

The order of December 15, 1989, is reversed and the matter remanded to the trial court for further proceedings consistent with this opinion. The parties will bear their own costs on appeal.

[EMPHASIS ADDED]

Sparks, Acting P. J., and Davis, J., concurred.

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MONEY LAUNDERING CONTROL ACT

THE MONEY LAUNDERING CONTROL ACT (the "Act") makes it criminal for anyone to conduct, or attempt to conduct, certain financial activities which involve the proceeds of unlawful activities. As the transfer of assets into a limited partnership, trust, or other entity may constitute a financial activity within the scope of the Act, it is necessary that you swear under oath that none of the assets intended to be transferred into such entities was derived from any of the criminal activities specified in the Act.

- (a) The specified unlawful activities under the Act consist primarily of drug-trafficking offenses, financial misconduct and environmental crimes. Drug-trafficking offenses include the manufacture, importation, sale, or distribution of controlled substances; the commission of acts constituting a continuing criminal enterprise; and transportation of drug paraphernalia.
- (b) Covered financial misconduct includes the concealment of assets from a receiver, custodian, trustee, marshal, officer of the court, creditors in a bankruptcy proceeding, the Federal Deposit Insurance Corporation, the Resolution Trust Corporation, or a similar agency or person; the making of a fraudulent conveyance in contemplation of a bankruptcy proceeding or with the intent to defeat the bankruptcy law; the giving of false oaths or claims in relation to a bankruptcy proceeding; bribery; the giving of commissions or gifts for the procurement of loans; theft, embezzlement, misapplication of bank funds, or funds of other lending, credit, or insurance institutions; the making of fraudulent bank or credit institution entries, loan, or credit applications; and mail, wire, bank fraud, bank, or postal robbery or theft.
- (c) Environmental crimes include violations of the Comprehensive Environmental Response, Compensation and Liability Act of 1980 as amended, the Clean Water Act, the Hazardous Material Transportation Act, the Toxic Substance Control Act, Federal Water Pollution Control Act, the Ocean Dumping Act, the Safe Drinking Water Act, the Resources Conservation and Recovery Act of 1976, the California Hazardous Waste Control Law, the Porter-Cologne Water Quality Control Act, and any similar Federal, State, and/or local statutes and ordinances.
- (d) Other specified crimes include counterfeiting, espionage, kidnaping or hostage-taking, copyright infringement, entry of goods by means of false statements, smuggling goods into the United States, removing goods from the custody of Customs, illegally exporting arms, and trading with United States enemies.

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