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## The Wyoming Registered Limited Liability Partnership

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## Comment

# THE WYOMING REGISTERED LIMITED LIABILITY PARTNERSHIP

On January 1, 1998, Wyoming became the forty-eighth state<sup>1</sup> to authorize a registered limited liability partnership (RLLP) statute.<sup>2</sup> Wyoming's RLLP statute provides limited liability for obligations that arise from "tort, contract or otherwise" to any Wyoming general partnership registering as a Wyoming RLLP.<sup>3</sup> This comment addresses Wyoming RLLP formation, limited liability, taxation, out of state treatment, and application of partnership law to an RLLP, and includes a comparison of the Wyoming RLLP to other Wyoming business entities. Ultimately, this comment concludes that Wyoming should amend its RLLP statute to protect the public from possible abuse.

### BACKGROUND

A business need for increased limited liability protection coupled with preferential tax treatment<sup>4</sup> compelled states to enact legislation creating

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1. ALA. CODE § 10-9A-1 (1994); ARK. CODE ANN. § 4-43-101 (Michie 1996); ARIZ. REV. STAT. ANN. § 29-367 (West 1998); CAL. CORP. CODE § 15611 (West Supp. 1998); COLO. REV. STAT. ANN. § 7-62-101 (West 1997); CONN. GEN. STAT. ANN. § 34-100 (West 1997); DEL. CODE ANN. tit. 6, § 1544 (1996); D.C. CODE ANN. § 41-401 (1998); FLA. STAT. ANN. § 620.78 (West Supp. 1996); GA. CODE ANN. § 14-8-2 (Supp. 1994); HAW. REV. STAT. ANN. § 425D-101 (Michie 1997); IDAHO CODE § 53-201 (1994 & Supp. 1998); 805 ILL. COMP. STAT. ANN. 205/8.1 (West Supp. 1998); IND. CODE ANN. § 23-4-1-1 (Michie 1995); IOWA CODE ANN. § 487.101 (West Supp. 1998); KAN. STAT. ANN. § 56-1a101 (1994); KY. REV. STAT. ANN. § 362.401 (Michie Supp. 1996); LA. REV. STAT. ANN. § 9:3431 (West 1997); ME. REV. STAT. ANN. tit. 31, § 401 (West 1996); MD. CODE ANN., Corps. & Ass'ns § 10-101 (Supp. 1998); MASS. GEN. LAWS. ANN. ch. 108A §45 (Supp. 1998); MICH. COMP. LAWS ANN. § 449.1 (West 1994); MINN. STAT. ANN. § 322A.01 (West 1996); MISS. CODE ANN. § 79-14-101 (1996 & Supp. 1998); MO. ANN. STAT. § 359.011 (West Supp. 1998); MONT. REV. CODE ANN. § 35-12-501 (Smith 1997); NEB. REV. STAT. ANN. § 67-233 (Michie Supp. 1996); NEV. REV. STAT. ANN. § 88.315 (Michie Supp. 1997); N.H. REV. STAT. ANN. § 304-B:1 (1995); N.J. STAT. ANN. § 42:2A-1 (West 1993); N.M. STAT. ANN. § 54-1A-101 (Michie Supp. 1998); N.Y. PARTNERSHIP LAW § 90 (McKinney Supp. 1998); N.C. GEN. STAT. § 59-101 (1993); N.D. CENT. CODE § 45-10.1-01 (Supp. 1998); OHIO REV. CODE ANN. § 1782.01 (Anderson 1993); OKLA. STAT. tit. 54, § 1-1001 (Supp. 1999); OR. REV. STAT. § 70.005 (Supp. 1996); 15 PA. CONS. STAT. ANN. § 8501 (West 1995); R.I. GEN. LAWS § 7-13-1 (1992); S.C. CODE ANN. § 33-42-10 (Law Co-op. 1995); S.D. CODIFIED LAWS § 48-7-101 (Michie Supp. 1998); TENN. CODE ANN. § 61-2-101 (1996); TEX. REV. CIV. STAT. ANN. art. 6132a-1 (West Supp. 1998); UTAH CODE ANN. § 48-2A-101 (1998); VA. CODE ANN. § 50-73.1 (Michie 1998); WASH. REV. CODE ANN. § 25.04.700 (West Supp. 1998); WIS. STAT. ANN. § 179.01 (West 1997).

2. WYO. STAT. ANN. §§ 17-21-1101 to -1105 (Michie Supp. 1998).

3. *Id.* § 17-21-306.

4. Entity taxation stems from federal tax law, and in some states, state tax law. Preferential tax treatment is a subjective term relating to the pass-through tax feature of a partnership versus the double taxation feature of a corporation. Pass-through taxation will not be "preferential" in all situations. For a discussion of taxation of entities see generally DANIEL Q. POSIN, CORPORATE TAX PLANNING (1990)

nontraditional business forms.<sup>5</sup> Nontraditional forms include the limited liability company (LLC)<sup>6</sup> and, most recently, the RLLP.<sup>7</sup> An RLLP is a general partnership with a limited liability shield.<sup>8</sup> The RLLP has developed into a viable entity around the country, providing partnerships with another way to do business while retaining partnership attributes.<sup>9</sup>

The RLLP entity originated in Texas in 1991.<sup>10</sup> The original Texas Limited Liability Partnership Act offered protection from tort liability to a small category of partnerships.<sup>11</sup> However, Texas soon passed an amended statute providing for a larger liability shield.<sup>12</sup> Subsequently, the RLLP form

(discussing corporate taxation in detail); JAMES A. DOUGLAS & ROBERT E. HALEY, *PARTNERSHIP TAX DIGEST* (1987) (discussing partnership taxation in detail, with updates for recent changes in the federal, partnership tax laws); *Tax and Business Planning for the 90s* C748 A.L.I.-A.B.A. (1992) (providing a guide to taxation with business planning consequences).

5. See 137 Del. Laws 42 (1993) (discussing Delaware's reasons for enacting a limited liability partnership statute).

6. The LLC offers limited liability and partnership pass-through taxation. Wyoming was the first state to pass an LLC statute in 1977. 1977 Wyo. Sess. Laws 537-549. For a discussion of the Wyoming LLC see WILLIAM D. BAGLEY & PHILLIP P. WHYNOTT, *THE LIMITED LIABILITY COMPANY* (1997).

7. WYO. STAT. ANN. §§ 17-21-1101 to -1105 (Michie Supp. 1998). The limited liability partnership form has different names and acronyms in each state. The possibilities include: registered limited liability partnership (RLLP), and limited liability partnership (LLP). The Wyoming statute is entitled "Registered Limited Liability Partnerships" and will be referred to in this comment as the registered limited liability partnership or (RLLP).

8. See generally Martin I. Lubaroff, *Registered Limited Liability Partnerships: The Next Wave in Forming and Using Limited Liability Companies and Limited Liability Partnerships*, 505 PRAC. L. INST. 241 (1994); Thomas W. Van Dyke & Paul G. Porter, *Limited Liability Partnerships: The Next Generation*, 63 NOV. J. KAN. B.A. 16 (1994); Jennifer J. Johnson, *The Oregon Limited Liability Partnership Act*, 32 WILLAMETTE L. REV. 147 (1996); Bruce D. Bernard, *Recent Developments Affect Choice-of-Entity Decision*, 25 TAX'N FOR LAW. 260 (1997); Paul R. Erickson & Buddy J. Sanders, *Assessing LLCs v. LLPs*, 28 TEX. TECH. L. REV. 1005 (1997); Stephanie R. Breslow, *Choice of Entity: The Uses of Limited Liability Companies and Limited Liability Partnerships*, 869 PRAC. L. INST. 551 (1994); Carter G. Bishop, *The Limited Liability Partnership Amendments to the Uniform Partnership Act*, 53 BUS. LAW. 101 (1997); Hannah L. Thompson, *New Business Options in Pennsylvania: A Critical Analysis of the Pennsylvania Limited Liability Company and Limited Liability Partnership Act of 1994*, 57 U. PITT. L. REV. 129 (1995).

9. See *infra* notes 18-20 and accompanying text.

10. 1991 Tex. Gen. Laws 302. The Texas RLLP was enacted in response to government suits brought under section 15 of the Uniform Partnership Act against law and accounting firms who represented the failed savings and loan operations in the late 1980s. All partners shouldered the liability even though many of the liable partners did not know about or participate in illegal activities. These suits demonstrated that vicarious liability of this magnitude did not exist in any other professional business organization form. In an effort to protect such partners, the Texas legislature enacted a tailored and narrow statute which was soon amended to provide a larger liability shield. ALAN R. BROMBERG & LARRY E. RIBSTEIN, *BROMBERG & RIBSTEIN ON LIMITED LIABILITY PARTNERSHIPS AND THE REVISED UNIFORM PARTNERSHIP ACT*, § 1.01(a) (1998).

11. The original statute protected against errors, omissions, incompetence, or malfeasance and covered doctors, lawyers, engineers, architects, and accountants. R. DENNIS ANDERSON ET AL. *Registered Limited Liability Partnerships*, 28 BULL. BUS. LAW. § 1 (1991), reprinted in 55 TEX. BAR J. 728 (1992). See also Susan Saab Fortney, *Seeking Shelter in the Minefield of Unintended Consequences—The Traps of Limited Liability Law Firms*, 54 WASH. & LEE L. REV. 717 (1997) (discussing the history of Texas law in the area of limited liability).

12. TEX. REV. CIV. STAT. ANN. art. 1528c (West 1997).

has evolved, and now offers a large liability shield in most states.<sup>13</sup>

The limited liability partnership was not a nationally recognized entity until 1993, when Delaware authorized an RLLP form.<sup>14</sup> The Delaware RLLP statute provides a great deal of limited liability, but requires the RLLP to purchase a one million dollar liability insurance policy.<sup>15</sup> This scheme provides partners with a valuable limited liability shield while protecting the public from the risk of doing business with an RLLP entity.<sup>16</sup> Following Texas and Delaware, all states now have an RLLP form, and most offer a great deal of limited liability.<sup>17</sup> This makes the RLLP a valuable entity for partnerships interested in an enlarged limited liability shield.

In an RLLP, the partnership aspects of the underlying entity are largely unchanged by registration;<sup>18</sup> therefore, the RLLP retains the stability provided by the Uniform Partnership Act<sup>19</sup> (UPA) and a developed body of partnership case law.<sup>20</sup> The RLLP also retains the ownership, governance, and partnership agreement aspects of a partnership in combination with

13. With the larger liability shield, some states require RLLPs to carry liability insurance to balance the interests of the RLLP with the interests of the public. The states requiring insurance are: Alaska, ALASKA STAT. § 32.05.416 (Michie Supp. 1996); California, CAL. BUS. & PROF. CODE § 15052 (West Supp. 1997); Connecticut, CONN. GEN. STAT. § 34-327 (West 1997); Delaware, DEL. CODE ANN. Ca. 15 tit. 6 § 1546(a) (Michie 1994); Florida, FLA. STAT. ANN. § 620.7851 (West Supp. 1996); Hawaii, HAW. REV. ST. § 425-178 (Michie 1997); Massachusetts, MASS. GEN. L. ch. 108, §45(8) (West 1993); New Mexico, N.M. STAT. ANN. § 54-1-47 (Michie Supp. 1998); Oklahoma, OKLA. STAT. ANN. tit. 54, § 1-309 (Michie 1997); Rhode Island, R.I. GEN. L. ANN. § 7-12-58 (Supp. 1997); South Carolina, S.C. CODE ANN. § 33-41-1130(A)(1)-(2) (Law Co-op. Supp. 1997); Washington, WASH. REV. CODE ANN. § 25 (West 1996). Even in states that do not require liability insurance, partners in an RLLP are often subject to other requirements under licensing or professional statutes. See COLO. S. CT. RULE 265.I.A.4 (Michie 1996); MODEL RULES OF PROFESSIONAL CONDUCT Rules 5.1-5.4 (1997).

14. Paul R. Erickson & Buddy J. Sanders, *Assessing LLCs vs. LLPs*, 28 TEXAS TECH L. REV. 1005 (1997).

15. DEL. CODE ANN. tit. 6, §§ 1515(b) & 1546(d) (1993).

16. 138 Del. Laws 76 (1995) (discussing the insurance requirement in Delaware).

17. See *supra* notes 1-13 and accompanying text.

18. RLLP statutes are typically added to the partnership act in existence. Most states provide that an RLLP must be a partnership before registration, and many states define an RLLP as a partnership. See BROMBERG & RIBSTEIN, *supra* note 10, table 2-1 at 84.

19. UNIF. PARTNERSHIP ACT, §§ 101-1007 (1994), 6 U.L.A. 10-124 (1995); WYO. STAT. ANN. §§ 17-21-101 to -1003 (Michie 1997).

20. See generally *P & M Cattle Co. v. Holler*, 559 P.2d 1019 (Wyo. 1977) (discussing the intent of parties to form a partnership); *Murphy v. Stevens*, 645 P.2d 82 (Wyo. 1982) (discussing the express purpose of forming a partnership); *State v. Bemis*, 242 P. 802 (Wyo. 1926) (discussing contract formation of a partnership); *Dinkelspeel v. Lewis*, 62 P.2d 294 (Wyo. 1936) (discussing the amount of evidence sufficient to show a partnership); *Ridgely v. First Nat'l Bank*, 75 F. 808 (D. Wyo. 1896) (discussing documents that must be executed by all partners to be valid); *Wood v. Western Beef Factory*, 378 F.2d 96 (10th Cir. 1967) (discussing the applicability of partnership law to third parties); *Stone v. First Wyo. Bank*, 625 F.2d 332 (10th Cir. 1980) (discussing the applicability of partnership law to joint ventures and third parties); *Horseshoe Estates v. 2M Co.*, 713 P.2d 776 (Wyo. 1986) (discussing the ability of a partner to bind a partnership); *Bergh v. Mills*, 763 P.2d 214 (Wyo. 1988) (discussing individual liability based on another partner's actions); *Douglas Reservoirs Water Users Ass'n v. Maurer & Garst*, 398 P.2d 74 (Wyo. 1965) (discussing the scope of a partner's authority).

limited liability.<sup>21</sup> Growing use of the RLLP evidences its utility.<sup>22</sup> However, the RLLP's usefulness in a particular state depends on that state's granting statute.<sup>23</sup>

### THE WYOMING RLLP

General partners engaged in business through a Wyoming general partnership are not only directly liable for their own conduct, but are also vicariously liable for all obligations of the partnership.<sup>24</sup> This includes obligations arising from the conduct of other partners acting in the ordinary course of partnership business<sup>25</sup> and might also include vicarious liability for punitive damages awards.<sup>26</sup> The increase in malpractice suits with large damage awards has created a need for limited liability protection for faultless partners.<sup>27</sup> The need for limited liability coupled with an increase in the number of out of state RLLPs doing business in Wyoming led the Wyoming legislature to enact the RLLP statute.<sup>28</sup>

Wyoming's RLLP statute was intended to provide large multistate law and accounting firms with the ability to conduct business free from vicarious liability.<sup>29</sup> The Wyoming RLLP is similar to the Delaware RLLP.<sup>30</sup> However, Delaware's one million dollar liability insurance requirement precludes many partnerships from registering as a Delaware RLLP.<sup>31</sup> Wyoming has no insurance requirement.<sup>32</sup> The lack of an insurance re-

21. Bridget O'Brian, *Goldman Chooses Limited Liability for New Structure*, WALL ST. J., May 21, 1996, at C13.

22. Between 1993 and 1996, 16,082 limited liability partnerships were formed nationwide. BROMBERG & RIBSTEIN, *supra* note 10, § 1.01(e). This includes all of the "big six" accounting firms, many of which are converting from the general partnership form after 100 or more years. Rick Telberg, *Big 6 Race into LLPs*, 8 ACCT. TODAY 41 (1994). Seventeen RLLPs have been formed in Wyoming as of November 25, 1998. Telephone Interview with Sharon Cochran, Wyoming Deputy Secretary of State (November 25, 1998). See also BROMBERG & RIBSTEIN, *supra* note 10, § 1.01(e).

23. BROMBERG & RIBSTEIN *supra* note 10, § 1.01(e).

24. WYO. STAT. ANN. §§ 17-21-305 to -306 (Michie 1997).

25. *Id.* §§ 17-21-101 to -1003.

26. *Id.* § 17-21-307. Fraud is among the tortious acts included. *Bergh v. Mills*, 763 P.2d 214 (Wyo. 1988) (decided under former § 17-3-305). See also Michael A. Rosenhouse, Annotation, *Derivative Liability of Partner for Punitive Damages for Wrongful Act of Copartner*, 14 A.L.R. 4th 1335 (1982).

27. See *infra* note 32 and accompanying text.

28. See *infra* note 32 and accompanying text.

29. Telephone Interview with John Hanes, Wyoming State Senator (May 26, 1998).

30. See DEL. CODE ANN. tit. 6, § 1544 (Supp. 1996).

31. The lack of interest in the Delaware RLLP is evidenced by the sparse number of RLLPs created in Delaware since the enactment of the 1993 statute. Since 1993 only 72 entities have registered as Delaware RLLPs. Compare that to the 59,367 domestic and 195 foreign entities that have registered as Delaware LLCs since Delaware enacted the LLC Act in 1992. Telephone Interview with the Delaware Secretary of State's office (October 9, 1998).

32. See WYO. STAT. ANN. § 17-21-1101(a) (Michie Supp. 1998). The Wyoming legislature intended to pass an RLLP statute which would allow the Wyoming business community to compete with businesses from other states. The RLLP was rapidly becoming a popular form in other states and Wyoming

quirement and the large liability shield make the Wyoming RLLP an exciting and valuable prospect for any type of partnership.<sup>33</sup> However, while Wyoming's RLLP statute may be beneficial to many Wyoming partnerships, the lack of an insurance requirement or any other stringent formalities make this an entity that should be tempered.<sup>34</sup> Wyoming has dealt with this powerful entity in a potentially dangerous way by offering a large liability shield<sup>35</sup> without providing safeguards against potential abuse.<sup>36</sup>

### *Formation*

The Wyoming RLLP statute is included as part of the Wyoming Uniform Partnership Act (WUPA).<sup>37</sup> In addition to several formal requirements, the RLLP must initially be a partnership.<sup>38</sup> A partnership in Wyoming is "an association of two (2) or more persons to carry on as co-owners of a business for profit formed under W.S. 17-21-202, predecessor law, or comparable law of another jurisdiction, and includes for all purposes of the laws of this state, a registered limited liability partnership."<sup>39</sup> Any Wyoming business entity classified as a partnership may become a registered limited liability partnership.<sup>40</sup>

Many business ventures may unknowingly be partnerships;<sup>41</sup> a partnership may be formed without a written agreement.<sup>42</sup> However, in order to register as an RLLP, a formal partnership must exist.<sup>43</sup> In exchange for limited liability, RLLP members sacrifice the informality and anonymity of the general partnership by registering.<sup>44</sup> This trade-off limits the utility of an RLLP in some situations.<sup>45</sup>

businesses would have been at a disadvantage without the option of the RLLP as a business tool. Interview with John Vinich, Wyoming State Senator, in Laramie, Wyo. (Oct. 13, 1998).

33. See *supra* notes 13-21 and accompanying text.

34. The lack of an insurance requirement in the Wyoming RLLP statute might be explained by the nonexistence of an insurance requirement in the other business entity statutes in Wyoming. However, other Wyoming entities arguably offer a smaller liability shield coupled with procedural, statutory, or judicial safeguards, therefore minimizing the need for an insurance requirement.

35. WYO. STAT. ANN. § 17-21-306 (Michie Supp. 1998).

36. Safeguards can include formation requirements, formalities, or insurance requirements. See *supra* note 15 and accompanying text.

37. WYO. STAT. ANN. §§ 17-21-101 to -1003 (Michie 1997).

38. *Id.* § 17-21-1102(a) (Michie Supp. 1998).

39. *Id.* § 17-21-101(a)(vi).

40. *Id.* § 17-21-1101.

41. Peggy A. Taylor, Note, *Determining the Existence of a Partnership* 13 LAND & WATER L. REV., 1021 (1978); P&M Cattle Co. v. Holler, 559 P.2d 1019, 1021 (Wyo. 1977).

42. "'Partnership agreement' means an agreement, written or oral, among the partners concerning the partnership." WYO. STAT. ANN. § 17-21-101(a)(v) (Michie 1997).

43. WYO. STAT. ANN. § 17-21-101(a)(i)-(vi) (Michie Supp. 1998).

44. *Id.* § 17-21-1101.

45. See generally BROMBERG & RIBSTEIN, *supra* note 10 (discusses when a partner or partnership may desire anonymity).

Once a partnership is formed, and the partners decide to register as an RLLP, the process is simple.<sup>46</sup> Wyoming allows a partnership to become an RLLP by filing a statement of registration with the secretary of state.<sup>47</sup> The statement of registration is supplied by the secretary of state and must include: (1) the name of the partnership;<sup>48</sup> (2) the name and address of the principal place of business and the registered agent;<sup>49</sup> (3) a statement of the business that the partnership will engage in;<sup>50</sup> (4) any other matters the partnership wishes to include,<sup>51</sup> and a statement that the partnership thereby registers as a limited liability partnership.<sup>52</sup> The statement of registration must be executed by one or more authorized partners and must be accompanied by a written consent to appointment signed by the registered agent.<sup>53</sup> Registration is completed by the secretary of state immediately upon filing and payment of a service fee set by the secretary of state.<sup>54</sup> The simple registration process is one of the benefits of the Wyoming RLLP statute.<sup>55</sup> However, perhaps the greatest benefit of the RLLP is the availability of a large limited liability shield.<sup>56</sup>

### *Limited Liability*

Limited liability is defined as liability that is limited by statute.<sup>57</sup> Many business forms offer the “gift” of limited liability, and several types of limited liability exist in each entity.<sup>58</sup> The availability of the federal “check-the-box” tax regulations, which provide for pass-through partnership taxation,<sup>59</sup>

46. *Id.*

47. WYO.STAT.ANN. § 17-21-1101(a) (Michie Supp. 1998).

48. *Id.* § 17-21-1101(a)(i).

49. *Id.* § 17-21-1101(a)(ii).

50. *Id.* § 17-21-1101(a)(iv).

51. *Id.* § 17-21-1101(a)(v).

52. *Id.* § 17-21-1101(a)(v), (vi).

53. *Id.* § 17-21-1101(b).

54. *Id.* § 17-21-1101(c), (d), (f).

55. However, even minimal disclosure is often too much for a particular partner or partnership. In situations where a partner or partnership wants to retain complete anonymity, the RLLP is not an appropriate entity. See *supra* notes 42-45 and accompanying text.

56. The RLLP provides limited liability to a partnership form. This is a benefit of the RLLP statute because it provides limited liability for faultless partners. See *infra* notes 57-105 and accompanying text.

57. WEBSTERS NEW INTERNATIONAL DICTIONARY 1313 (3d ed. 1983).

58. The corporation offers limited liability to shareholders and directors. However, the veil-piercing doctrine tempers corporate limited liability. See *infra* note 80. The LLC also offers limited liability to its members and managers; however, veil-piercing might apply to the LLC as well. See *Ditty v. Checkrite, Ltd.*, 973 F. Supp. 1320 (D. Utah 1997); *Hollowell v. Orleans Reg'l Hosp.*, 1998 U.S. Dist. WESTLAW 283298, (E.D. LA. May 19, 1998). The professional corporation offers corporate style limited liability to professionals. Each of these entities is difficult to form and requires that formalities such as annual meetings and minutes be strictly kept, often making the limited liability difficult to maintain. The Wyoming RLLP, however, offers a type of limited liability that is nearly “bulletproof.” While some formalities must be followed, such as registration and statutory compliance, the Wyoming RLLP is free to conduct business and rely on the limited liability shield provided by the statute. See *infra* note 71 and accompanying text.

59. See *infra* notes 107-125 and accompanying text.

make limited liability an increasingly important factor in choice of business entity decisions in Wyoming.<sup>60</sup>

Generally, there are several broad types of limited liability available to a Wyoming RLLP.<sup>61</sup> First, the Wyoming RLLP statute limits the vicarious liability for the debts of the partnership.<sup>62</sup> Second, once a partnership becomes an RLLP, alteration of the joint and several liability rule with respect to partnership obligations provides limited liability in certain situations.<sup>63</sup>

[A] partner of a registered limited liability partnership is not liable, directly or indirectly (including by way of indemnification, contribution, assessment or otherwise), for any debts, obligations or liabilities of, or chargeable to, the registered limited liability partnership or another partner or partners, whether arising in tort, contract or otherwise, solely by reason of being such a partner . . . .<sup>64</sup>

### 1. General Exceptions to Limited Liability

There are a number of exceptions to Wyoming RLLP limited liability. First, the limited liability shield does not protect a partner from his or her own negligence, wrongful act, or misconduct.<sup>65</sup> Thus, responsibility for misconduct lies with each individual RLLP partner. This exception extends to any negligence, wrongful act, or misconduct of any person who is under the partner's "direct supervision and control."<sup>66</sup> Second, a majority of the partners may alter or extinguish limited liability by subsequent agreement.<sup>67</sup> Therefore, alteration by a partnership agreement may void limited liability protection or may make a partner liable for the amount invested in the firm, particularly if a partner agreed to contribute to partnership losses.<sup>68</sup> Third, a partner in an RLLP may contract for personal liability.<sup>69</sup> This provides flexi-

60. See generally BROMBERG & RIBSTEIN, *supra* note 10.

61. *Id.*

62. WYO. STAT. ANN. § 17-21-306 (Michie 1997). The introduction of limited liability in forms other than the corporation has sparked a debate regarding the propriety of such limits. For a discussion of the pros and cons of limited liability see BROMBERG & RIBSTEIN, *supra* note 10; UNIF. PARTNERSHIP ACT § 15, 6 U.L.A. 15 (1914); REVISED UNIF. PARTNERSHIP ACT § 306, 6 U.L.A. 306 (1994); ALAN R. BROMBERG & LARRY E. RIBSTEIN, BROMBERG & RIBSTEIN ON PARTNERSHIP § 5.08 (1988).

63. WYO. STAT. ANN. §§ 17-21-1101(f), -306 (Michie Supp. 1998).

64. *Id.* § 17-21-306(b).

65. *Id.* § 17-21-306(c).

66. *Id.*

67. *Id.* § 17-21-306(d).

68. A partner may agree to assume liability in order to guarantee partnership debts or financing. Although this seems to defeat the purpose of RLLP limited liability, it is often an essential part of doing business as a partnership, and many partners are willing to assume liability to maintain the partnership business. BROMBERG & RIBSTEIN, *supra* note 10, § 3.05.

69. WYO. STAT. ANN. § 17-21-306(d) (Michie Supp. 1998). Wyoming's statute provides:

all or specified partners of a registered limited liability partnership may be liable in



bility by allowing a contracting partner to change the amount of limited liability protection in order to provide financing or other benefits to the partnership.<sup>70</sup> Fourth, courts might impose liability on RLLP partners for the partnership's debts using theories similar to corporate "veil-piercing."<sup>71</sup> However, at this point, it is unclear whether corporate veil-piercing theories will apply to RLLPs.<sup>72</sup>

## 2. Possible Veil-Piercing Exceptions to Limited Liability

While some state statutes specifically provide that corporate veil-piercing standards will apply to RLLP's, Wyoming's statute is silent on the issue.<sup>73</sup> Courts can always apply veil-piercing theories on their own initiative; however, statutory silence, coupled with the structure of the Wyoming RLLP statutes make application of corporate veil-piercing theories to Wyoming RLLP's inappropiate.<sup>74</sup>

Thin capitalization has been a traditional justification for piercing the corporate veil; however, applying an undercapitalization doctrine to an RLLP is more difficult.<sup>75</sup> For instance, a professional RLLP may be considered undercapitalized if it is unable to adequately compensate for possible

their capacity as partners for all or specified debts, obligations or liabilities of a registered limited liability partnership to the extent at least a majority of the partners shall have agreed unless otherwise provided in any agreement between the partners.

*Id.*

70. For instance, if an RLLP needed financing on a particular project but the bank refused to loan unless one or all of the partners personally guaranteed the loan, as many partners as necessary could waive the limited liability shield for that one loan while retaining it for other purposes.

71. Wyoming case law depicts situations where the corporate veil can and will be pierced by creditors; they include: (1) corporate formation to perpetrate a fraud; see *Langdon v. Lutheran Bhd.*, 625 P.2d 209 (Wyo. 1981); *Kloefkom-Ballard Constr. & Dev. Inc. v. North Bighorn Hosp. Dist.*, 683 P.2d 656 (Wyo. 1984); *Bergh v. Mills*, 763 P.2d 214 (Wyo. 1988). HARVEY GELB, PERSONAL CORPORATE LIABILITY, A GUIDE FOR PLANNERS, LITIGATORS, AND CREDITORS' COUNSEL § 1.9 (1991); (2) to prevent injustice or inequitable consequences; see *Lutheran Bhd.*, 625 P.2d at 209; *Amfac Mechanical Supply Co. v. Federer*, 645 P.2d 73 (Wyo. 1982). See also GELB, *supra* § 1.9; (3) thin capitalization; see *Amfac Mechanical Supply Co.*, 645 P.2d at 73. See also GELB, *supra* § 1.6; (4) disregarding corporate formalities; see *United States v. Van Diviner*, 822 F.2d 960 (10th Cir. 1987); *Yost v. Harpel Oil Co.*, 674 P.2d 712 (Wyo. 1983); *Miles v. CEC Homes, Inc.*, 753 P.2d 1021 (Wyo. 1988). See also GELB, *supra* § 1.8; (5) not advising creditor of debtor's corporate status; see *Inryco, Inc. v. CGR Bldg. Sys., Inc.*, 780 F.2d 879 (10th Cir. 1986); *Ely v. Kirk*, 707 P.2d 706 (Wyo. 1985); *Valentine v. Ormsbee Exploration Corp.*, 665 P.2d 452 (Wyo. 1983). But see *Rivermcadows, Inc. v. Zwaanshoek Holding & Fin.*, 761 P.2d 662 (Wyo. 1988) (which held that knowledge on the part of the creditor of the alter ego corporate status is a legitimate defense). See also GELB, *supra* § 1.13; and (6) commingling of assets; see *Yost*, 674 P.2d at 712; *CEC Homes, Inc.*, 753 P.2d at 1021; *Jackson Hole Traders, Inc. v. Joseph*, 931 P.2d 244 (1997). See also GELB, *supra* § 1.7. By analogy, the RLLP entity may be subject to some of the same situations that could lead to "veil-piercing."

72. BROMBERG & RIBSTEIN, *supra* note 10, § 3.07.

73. Compare COLO. REV. STAT. § 7-60-153(2) (1997) and N.D. CENT. CODE § 44-22-9 (Michie Supp. 1998), with WYO. STAT. ANN. §§ 17-21-1101 to -1105 (Michie Supp. 1998).

74. BROMBERG & RIBSTEIN, *supra* note 10, § 3.07.

75. *Id.*

malpractice claims.<sup>76</sup> Application of veil-piercing theories would require an RLLP to plan for all possible future malpractice claims of any amount. Under this regime, proper capitalization of a typical RLLP would be impossible. This outcome makes it difficult to properly pierce the RLLP veil using an undercapitalization theory.<sup>77</sup>

Failure to observe corporate formalities is another traditional justification for veil-piercing. The number of formalities required by statute is proportional to the likelihood that the RLLP will lose its limited liability shield.<sup>78</sup> However, the Wyoming RLLP statute does not require the observance of *corporate* type formalities.<sup>79</sup> For example, some state RLLP statutes require that the name and address of each partner be disclosed on the registration; Wyoming does not require this disclosure.<sup>80</sup> Nor does the Wyoming RLLP statute require corporate operational formalities such as annual meetings.<sup>81</sup> The Wyoming RLLP statute does, however, enumerate several RLLP formalities that must be observed. For instance, the RLLP must pay a fee and submit a statement of renewal each year.<sup>82</sup>

The Wyoming RLLP statute also requires a name formality. The name of an RLLP must end with "Registered Limited Liability Partnership," "Limited Liability Partnership," "R.L.L.P.," "L.L.P.," "RLLP," or "LLP."<sup>83</sup> This requirement is similar to the name requirement in the Wyoming LLC statute.<sup>84</sup> However, while the Wyoming LLC act lists statutory consequences

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76. *Id.*

77. See generally William P. Hackney & Tracey G. Benson, *Shareholder Liability for Inadequate Capital*, 43 U. PITT. L. REV. 837 (1982); Cathy S. Krendl & James R. Krendl, *Piercing the Corporate Veil: Focusing The Inquiry*, 55 DEN. L.J. 1 (1978); Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036 (1991); Walkovsky v. Carlton, 223 N.E.2d 6 (1966) (corporate veil-piercing case in which the court refused to pierce for inadequate capitalization, citing statutory compliance by the defendant).

78. Formalities in this context include requirements for annual meetings, specific voting requirements, and specific name requirements. The nature of a partnership is that it can be formed simply for the purpose of doing business for profit. A partnership could be informal, with no partnership agreement or other formalities. Because the Wyoming RLLP has few formal requirements, meeting the enumerated requirements is simple. The argument follows that the limited liability shield of an RLLP should not be subject to veil-piercing doctrines dealing with failure to meet formalities. See *supra* notes 37-40 and accompanying text.

79. WYO. STAT. ANN. §§ 17-21-1101 to -1105 (Michie Supp. 1998).

80. *Id.* This disclosure is a burdensome requirement for those partnerships that would like to remain discrete. This is another area where the Wyoming statute caters to the business entity rather than the public interest.

81. This provides a great advantage over corporations which are subject to numerous formalities. Noncompliance with such corporate formalities often supports veil-piercing cases, although the presence of other factors such as undercapitalization is essential. See *Miles v. CEC Homes, Inc.*, 753 P.2d 1021 (Wyo. 1988). See also GELB, *supra* note 71, § 1.8.

82. WYO. STAT. ANN. § 17-21-1101(e) (Michie Supp. 1998). The RLLP is also required to pay \$100 each year. For some small partnerships this may impose a burden. *Id.*

83. WYO. STAT. ANN. § 17-21-1103 (Michie Supp. 1998).

84. *Id.* § 17-15-105 (Michie 1997).

for failure to include an LLC acronym,<sup>85</sup> the Wyoming RLLP statute contains no such provision.<sup>86</sup> This difference demonstrates the propriety of the RLLP as an entity providing a strong limited liability shield. Although the RLLP statute enumerates no consequences, the letters RLLP<sup>87</sup> should be included at all times to ensure retention of the limited liability shield.<sup>88</sup> Failure of an RLLP to assert itself as an RLLP is a misrepresentation and may lead to loss of limited liability protection.<sup>89</sup>

In addition to the registration fee, statement of renewal, and name formalities, a *professional* RLLP must observe additional formalities. Every state authorizes professionals to practice as partnerships.<sup>90</sup> Wyoming authorizes licensed professionals to form an RLLP, however, a professional RLLP must abide by the “rules, regulations, standards and requirements” of their licensing authority.<sup>91</sup> Thus, in a professional firm that organizes as an RLLP, the partners may remain vicariously liable depending on the rules and regulations of the licensing authority.<sup>92</sup> Along with liability for one’s own malpractice and possible vicarious liability, the professional RLLP partner may also be liable for employee actions.<sup>93</sup> In addition, the professional license must be in good standing at all times.<sup>94</sup> Failure to maintain a professional license will lead to malpractice liability, and may lead to a loss of RLLP liability protection.<sup>95</sup> It appears, however, that the faultless professional RLLP partner will enjoy limited liability from another partner’s wrongdoing.<sup>96</sup> The safeguards provided by professional licensing formalities indicate that corporate veil-piercing theories are not needed to impose li-

85. *Id.* § 17-15-105(b).

86. *Id.* §§17-21-1101 to -1105 (Michie Supp. 1998).

87. The registered partnership may choose the form of the RLLP name. *Id.* § 17-21-1103.

88. Consequences of failure to use the RLLP in all situations are not enumerated in the statute, however, one can speculate from the phrasing of the LLC name statute that the consequences could be loss of limited liability. Therefore, it is prudent to use the appropriate acronym at all times. *See supra* note 71 and accompanying text.

89. BROMBERG & RIBSTEIN, *supra* note 10, § 1.07(a)(7).

90. *See generally* ROBERT W. HILLMAN, HILLMAN ON LAWYER MOBILITY (1994); Stephen E. Kalish, *Lawyer Liability and Incorporation of the Law Firm*, 29 ARIZ. L. REV. 563 (1987).

91. WYO. STAT. ANN. § 17-21-1105 (Michie Supp. 1998). The American Bar association has authorized the use of the RLLP by lawyers. ABA Comm. on Ethics and Professional Responsibility, Formal Op. 96-401 (1996).

92. Jurisdictions that impose liability on lawyers for malpractice include Delaware and Illinois. *See* DEL. SUP. CT. R. 67(h); ILL. SUP. CT. R. 721(b).

93. Wyoming allows for this type of liability. WYOMING RULES OF PROFESSIONAL CONDUCT Rules 5.1-5.4 (1997). *See generally* John S. Dzienkowski, *Legal Malpractice and The Multistate Law Firm: Supervision of Multistate Offices; Firms as Limited Liability Partnership; and Predispute Agreements to Arbitrate Client Malpractice Claims*, 36 S. TEX. L. REV. 967, 972-79 (1995); Susan Saab Fortney, *Am I My Partner’s Keeper? Peer Review in Law Firms*, 66 U. COLO. L. REV. 329 (1995).

94. WYO. STAT. ANN. § 17-21-1105 (Michie Supp. 1998).

95. *Id.* § 17-21-306.

96. *Id.*

ability on a professional RLLP.<sup>97</sup>

Finally, the Wyoming RLLP statute offers no guidance on the applicability of corporate veil-piercing theories or the possible loss of the limited liability shield for statutory noncompliance.<sup>98</sup> However, noncompliance with registration guidelines could void any limited liability shield and provide an opportunity to apply corporate veil-piercing theories.<sup>99</sup> RLLP partners may argue that the lack of any statutory consequences for noncompliance should not limit their liability shield, but rather entitles the RLLP to limited liability protection even without strict statutory compliance.<sup>100</sup> However, prudence dictates that RLLPs do everything they can to comply strictly with the statute.

The limited liability feature of the Wyoming RLLP is extraordinarily broad compared to other states.<sup>101</sup> While Wyoming retains partner liability for personal malpractice or misconduct, the protections omitted from the statute create a dangerous amount of untempered limited liability.<sup>102</sup> Indiscreet limitations on liability, without proper safeguards, invite abuse.<sup>103</sup> The public needs some amount of protection from possible abuse by boundless RLLPs.<sup>104</sup> In the event that this statute is fully exercised, the limited liability protection provided could be dangerous for Wyoming citizens.<sup>105</sup>

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97. The wrongdoer will be liable regardless of the applicability of corporate veil-piercing theories. BROMBERG & RIBSTEIN, *supra* note 10, § 7.04(b).

98. Several other state statutes provide for consequences in the event of noncompliance. These include: Arizona, Connecticut, Delaware, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Massachusetts, Missouri, Nevada, New Hampshire, New Jersey, New York, North Carolina, Rhode Island, South Carolina, Tennessee, Utah, and Wyoming. *See supra* note 1.

99. BROMBERG & RIBSTEIN, *supra* note 10, § 2.07(a). Alternatively the noncompliance with registration guidelines could lead to the nonexistence of the RLLP. *Id.*

100. RLLPs lacking strict compliance may argue that they are in substantial compliance. This means that the noncompliance was de minimis, or so minute that it should not affect liability. Partners can also argue that they acted as an RLLP by estoppel. This would be effective in a situation where the RLLP and a creditor transact business on the premise that the partnership is an RLLP. In the event that noncompliance led to a loss of RLLP limited liability, it would not affect the status of the firm as a partnership or limited partnership, therefore non-participating partners would likely retain limited liability. BROMBERG & RIBSTEIN, *supra* note 10, § 2.07(c).

101. WYO. STAT. ANN. § 17-21-306(b) (Michie Supp. 1998) provides protection for all types of claims including contract, tort, or otherwise. Twenty-one states do not provide the full limited liability shield provided by Wyoming. BROMBERG & RIBSTEIN, *supra* note 10, table 3-1 p. 160.

102. WYO. STAT. ANN. § 17-21-306 (c) (Michie Supp. 1998).

103. GELB, *supra* note 71, § 1.15.

104. *Id.*

105. A Wyoming RLLP with its large liability shield is relatively free to conduct business in any manner, secure in the knowledge that the partnership has a limited liability shield. There may be a case where an RLLP causes great harm to the general public but will be protected by the statute. To protect against this consequence, Delaware requires a one million dollar insurance policy. *See supra* note 16 and accompanying text. In Delaware, faultless partners remain protected while the public is protected from serious harm that may be caused by a partnership doing business as an RLLP. It is clear that the Delaware insurance requirement may be too extensive for Wyoming, however, some protection is important.

## Taxation

For federal income tax purposes, the Wyoming RLLP will be taxed as a partnership, unless the partners choose to “check-the-box.”<sup>106</sup> The “check-the-box” tax regulations allow unincorporated entities to choose between corporate or partnership tax status.<sup>107</sup> Knowledge of a client’s needs will be crucial in determining whether corporate or partnership taxation is preferable.<sup>108</sup>

The adoption of the “check-the-box” regulations simplified tax classification, particularly for partnerships.<sup>109</sup> Generally, all entities except the C corporation are taxed as partnerships unless they elect to “check-the-box.”<sup>110</sup> For federal tax purposes, every business entity not organized as a corporation that elects not to “check-the-box” will be treated as a partnership.<sup>111</sup> Pass-through taxation of partnerships provides several benefits to the partners in an RLLP not available to corporate shareholders.<sup>112</sup>

Partnerships are not taxable as an entity, but rather they are conduits for gains and losses to the partners.<sup>113</sup> Therefore, partnership income is taxed

The lack of an insurance requirement makes Wyoming’s RLLP an attractive entity for partnerships looking for limited liability, but it provides no protection to balance the large liability shield. See *infra* note 186 and accompanying text.

106. Treas. Reg. §301.7701-1 to -7 (as amended by T.D. 8697, 1997-2 I.R.B. 11).

107. All prior rulings and revenue procedures that used the old corporate classification rules are obsolete. See IRS Notice 97-1, 1997 IRB 22. If an entity fails to make an election the regulations provide for a default classification: partnership status if the entity has two or more owners and a sole proprietorship if the entity has one owner. Treas. Reg. § 301.7701-3(b)(2)(i)(ii)(1994). These regulations replaced the long-standing four-part *Kintner* test, and provided a simplified way to determine tax status. Treas. Reg. §§301.7701-1 to -7 (as amended by T.D. 8697, 1997-2 I.R.B. 11). *United States v. Kintner*, 216 F.2d 418 (9th Cir. 1954). The decision in this case resulted in the promulgation of a four-factor corporate characteristic test. The four-factor test is: (1) continuity of life, (2) centralization of management, (3) limited liability, and (4) free transferability of interest. *Id.* For a discussion on the *Kintner* test and its downfall, see generally Tassma A. Powers & Deby L. Forry, *Partnership Taxation & The Limited Liability Company: Check Out the Check-the-Box Entity Classification*, 32 LAND & WATER L. REV. 831 (1997) (discussing the impact the “check-the-box” rule had on business entities).

108. A practitioner dealing with a conversion from one entity to another should consult the applicable tax codes. See I.R.C. § 336 (1994).

109. See generally Powers & Forry, *supra* note 107.

110. See *supra* note 106 and accompanying text.

111. See Powers & Forry, *supra* note 107, at 845; Treas. Reg. § 301.7701-3 (1994).

112. See JAMES A. DOUGLAS & ROBERT E. HALEY, PARTNERSHIP TAX DIGEST (Cum. Supp. 1987); J. WILLIAM CALLISON, PARTNERSHIP LAW AND PRACTICE (Cum. Supp. 1997).

113. I.R.C. § 701 (1994). Individual partners are liable for their respective distributive share of the partnership’s taxable income. See *Longmire v. Indiana Dep’t. of State Revenue*, 638 N.E.2d 894 (Ind. Tax 1994). S corporations, on the other hand, limit the pass-through of losses because they have only one class of stock. However, voting and non-voting shares are not considered different classes of stock. I.R.C. § 1361(b)(1)(d) (1994). This one class of stock rule inhibits flexibility regarding allocation of income and loss. Unlike other pass-through entities, the income and losses of an S corporation pass through on a pro rata basis to the owners of the single class of stock. See I.R.C. § 1361(b)(1)(d) (1994). Unlike a C corporation, an S corporation is not allowed to have stock with different economic interests. Additionally, other pass-through type entities may allocate specific items of income attributable to specific operations in a manner different from other profit and loss sharing ratios. I.R.C. § 704(b) (1994);

at an individual rate and not at corporate rates.<sup>114</sup> Partnerships avoid double taxation, and partnership losses may offset the partners' ordinary income of the same year, subject to passive activity, adjusted basis, and at risk limitations.<sup>115</sup> These outcomes provide beneficial tax results for those choosing to do business in a partnership or RLLP form. However, many determinations must be made before choosing the appropriate tax classification.<sup>116</sup> In some circumstances a business might want to elect to be taxed as a corporation.<sup>117</sup> Conversion from one entity to another may also have a large impact on choice of entity determinations.<sup>118</sup>

When a Wyoming partnership registers as an RLLP, the original partnership is not terminated in the eyes of the I.R.S., as long as the entity remains essentially the same.<sup>119</sup> For example, when a general partnership converts to a limited partnership under Wyoming statute section 17-21-901, the resultant limited partnership is "for all purposes the same entity that existed before the conversion."<sup>120</sup> The I.R.S. considers the conversion from a general partnership to a limited partnership an exchange.<sup>121</sup> No gain or loss is recognized, as long as each partner's total percentage interest in the partnership's profits, losses, and capital remains the same after the conversion, and the business of the general partnership is continued after the conversion.<sup>122</sup> The

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Treas. Reg. § 1.704-1(b) (1994). Generally, as long as the allocations have "substantial economic effect" (i.e., they have real bottom-line financial meaning) partners can receive tax-favorable special allocations of tax items. Christopher M. Riser, *Tax Choice of Entity for a New Small Business*, LIMITED LIABILITY COMPANY REP., Vol. 6, No. 4 (July/August 1998).

114. The partnership files an informational return to the I.R.S., then the individual partners claim he gains and losses from the partnership on their I.R.S. form 1040 Schedule C. I.R.C. § 701 (1994).

115. A loss in an activity in which a person does not materially participate (passive activity) is not allowed to offset ordinary income. I.R.C. § 469 (1994). The share of loss is only allowed to the extent of the partner's adjusted basis in the partnership. *Id.* § 704(d). Section 465 limits deductions of loss from a partnership to losses suffered to capital that is actually at risk. *Id.* § 465.

116. *See supra* note 76.

117. A business that will generate income from its inception would exemplify a business that may prefer to be taxed as a C corporation because no losses would be available to pass-through. The business may also take advantage of corporate taxation by retaining or reinvesting the earnings rather than distributing to shareholders. This type of business is more suitable to a corporate form than a pass-through type entity.

118. In the event of a conversion, a corporation may still benefit more from converting to an S-corporation rather than converting to a partnership. A shift from C corporation status to partnership status requires a liquidation of the corporation, which may result in a significant current corporate and shareholder tax liability. The immediate tax cost of moving to a partnership format may be significant enough to tip the balance in favor of a Subchapter S election. *See* I.R.C. §§ 331(a), 336, 1001 (1994).

119. If the RLLP stays essentially the same as the original partnership then the original partnership is deemed to continue as the new RLLP. The RLLP will remain a partnership as long as it does not "check-the-box." I.R.C. § 708 (1994). *See also*, WYO. STAT. ANN. § 17-21-1102 (Michie Supp. 1998).

120. All the property remains in the new entity, all obligations are also transferred to the new entity, and an action or proceeding pending may be continued as if conversion had not occurred. WYO. STAT. ANN. § 17-21-903 (Michie 1997).

121. No gain or loss is recognized by a partnership or to any of its partners in the case of a contribution of property to the partnership in exchange for an interest in the partnership. I.R.C. § 721 (1994).

122. *See* Rev. Rul. 84-52, 1984-1 C.B. 157.

same reasoning applies when converting from a general partnership to a registered limited liability partnership. I.R.S. Private Letter Rulings have said that the conversion from a general partnership to a limited partnership is analogous to the conversion from a general partnership to a registered limited liability partnership.<sup>123</sup> Consequently, registration as an RLLP will have no adverse tax consequences for the partners in a partnership. A business planner should also consider method of accounting and the self-employment tax when registering a Wyoming general partnership as an RLLP.<sup>124</sup>

A Wyoming RLLP enjoys the dual benefit of federal pass-through taxation and no Wyoming state income tax. However, if the Wyoming RLLP does business in a neighboring state, the income tax statute of that state will apply.<sup>125</sup>

#### OUT OF STATE TREATMENT OF WYOMING RLLPS

Similar to the out of state tax consequences of doing business, out of state treatment of Wyoming RLLP limited liability warrants consideration. Many Wyoming entities conduct business in other states. However, other states may not recognize the liability shield provided by the Wyoming RLLP statute.<sup>126</sup>

A Wyoming RLLP may "conduct its business, carry on its operations and have and exercise the powers granted by [the Wyoming statutes] in any state, territory, district or possession of the United States or in any foreign country."<sup>127</sup> Most state limited liability partnership statutes have similar pro-

123. Priv. Ltr. Rul. 9229016 (Apr. 16, 1992) (LLP converting to LLC); Priv. Ltr. Rul. 9420028 (Feb. 18, 1994) (formation of Delaware LLP); Priv. Ltr. Rul. 9420028 (Feb. 18, 1994) (conversion of New York general partnership to Delaware LLP); Priv. Ltr. Rul. 9423037 (Mar. 16, 1994) (conversion of New York general partnership to Delaware LLP); Priv. Ltr. Rul. 9423040 (Mar. 18, 1994) (conversion of New York general partnership to Delaware LLP); Priv. Ltr. Rul. 9424036 (Mar. 21, 1994) (conversion of Illinois general partnership to Delaware LLP).

124. An important consideration is whether a general partnership's registration as an RLLP would force the firm to switch from the cash method to the accrual method of tax accounting. This could force a sudden acceleration of income into the conversion year. For a complete discussion, see BROMBERG & RIBSTEIN, *supra* note 10, § 705(d). Avoiding substantial self-employment tax is another consideration regarding converting to an RLLP. *See id.* § 705(c).

125. COLO. REV. STAT. ANN. § 39-22-203 (West 1997); IDAHO CODE §§ 63-3022L, 63-3082 (Michie Supp. 1998); MONT. CODE ANN. § 15-30-105 (1997); NEB. REV. STAT. ANN. § 77-2773 (Michie 1996); UTAH CODE ANN. § 59-10-303 (1996).

126. *See infra* note 129 and accompanying text.

127. WYO. STAT. ANN. § 17-21-1104(a) (Michie Supp. 1998). Also, the Wyoming legislature intended the

legal existence of registered limited liability partnerships formed pursuant to an agreement governed by [WUPA] be recognized outside the boundaries of this state and that the laws of this state governing such registered limited liability partnerships

visions, allowing the laws of the state of formation to apply to the organization, internal affairs, and the liability of the partners of the RLLP.<sup>128</sup> The states surrounding Wyoming each have provisions that allow for a Wyoming RLLP to do business in those states and still maintain the protection of the Wyoming RLLP statutes with regard to internal partnership management and limited liability.<sup>129</sup>

In those states without a statute specifically providing that the Wyoming RLLP statute will govern a Wyoming RLLP, an RLLP will face uncertain choice-of-law questions.<sup>130</sup> In such an event, a practitioner should consult the statute of that state and approach doing business there with caution.

#### APPLICABILITY OF WYOMING PARTNERSHIP LAW

The Wyoming RLLP and the WUPA statutes leave unsettled several issues surrounding the application of partnership law to Wyoming RLLPs. These issues include the level of partner management and control, partner agency powers, partner financial rights, and partner fiduciary duties.<sup>131</sup> The following discussion attempts to determine if partnership law should apply to Wyoming RLLPs.

First, in a Wyoming general partnership, each partner has equal management rights.<sup>132</sup> These rights are particularly important to general partners because it is through proper management that they protect themselves from liability.<sup>133</sup> The limited liability shield available in RLLPs raises the issue of how management rights should be distributed. Partners with limited liability will be less likely to suffer the consequences of someone else's misman-

transacting business outside this state be granted the protection of full faith and credit under the constitution of the United States.

*Id.* § 17-21-1104(b).

128. BROMBERG & RIBSTEIN, *supra* note 10, § 6.02(d).

129. COLO. REV. STAT. ANN. §§ 7-64-1006 to -1008, -1010 (West 1997) (section 7-64-1010 expressly provides that Colorado does not permit a foreign RLLP to engage in business from which a domestic RLLP is barred); IDAHO CODE § 53-343C (Michie Supp. 1998); MONT. CODE ANN. § 35-10-710 (1997); NEB. REV. STAT. ANN. § 67-457 (Michie 1996); UTAH CODE ANN. §§ 48-1-43, -44(1) (1998).

130. Some commentators suggest that the Commerce Clause, Due Process Clause and Full Faith and Credit Clause of the United States Constitution may require a foreign jurisdiction to recognize the limited liability status of a defendant under the laws of the state of organization. See Deborah A. DeMott, *Perspectives of Choice of Law for Corporate Internal Affairs*, 48 LAW & CONTEMP. PROBS. 161, 187-98 (1985); Arthur T. Von Mehren & Donald T. Trautman, *Constitutional Control of Choice of Law: Some Reflections on Hague*, 10 HOFSTRA L. REV. 35 (1981).

131. BROMBERG & RIBSTEIN, *supra* note 10, §4.01.

132. WYO. STAT. ANN. § 17-21-401(f) (Michie 1997).

133. General partners can essentially protect themselves from added liability by proper management. They do not rely on another to protect them; they are responsible for their own liability through management decisions.



agement.<sup>134</sup> In an RLLP situation it is not necessary to allow for equal management in an RLLP because all partners are protected from the mismanagement of other partners.<sup>135</sup> Therefore, the default partnership rule of equal management rights, in all likelihood, will not be strictly applied to an RLLP by the courts.<sup>136</sup> RLLP partners can determine the management rules of their RLLP by agreement, allowing for equal management or some other combination.

However, when partners are employed by the RLLP, management rights become more important.<sup>137</sup> Management decisions have an impact on employed partners even when protected by the RLLP limited liability shield.<sup>138</sup> Therefore, in an RLLP partner employment situation, the default partnership management rule should apply. This would protect the employed partner, whose livelihood is subject to RLLP control, by allowing that partner to participate equally in management decisions.

Second, in a Wyoming partnership, each partner is an agent of the partnership and has the power to bind it.<sup>139</sup> The WUPA provides for a statement of partnership authority in which partners can deal with agency issues.<sup>140</sup> Determining which partners will act as agents for the partnership will aid an RLLP in maintaining limited liability.<sup>141</sup> This determination provides notice to the public that only certain partners are agents of the partnership, which decreases the chance that limited liability will be lost. In order to put the public on notice, an RLLP could file the statement of partnership authority with the RLLP registration.<sup>142</sup> If this issue is not resolved by the RLLP, a court could impose liability on the partnership for a wrongful act

134. Mismanagement is the catalyst for liability in a partnership. In an RLLP, when all partners have limited liability, the mismanagement by one will not make all partners liable. This limit on liability provides an incentive to those partners who would not manage in a general partnership, to provide management in an RLLP. The result will be a better quality of management and possibly a better business. BROMBERG & RIBSTEIN, *supra* note 10, §3.00.

135. WYO. STAT. ANN. § 17-21-306 (Michie Supp. 1998).

136. This argument is a double-edged sword. The partner in an RLLP also knows that whether he participates in the management or not, he will be protected from liability. This can provide an incentive for the partners to become apathetic to mismanagement.

137. BROMBERG & RIBSTEIN, *supra* note 10, § 4.02(a).

138. Poor management decisions may cause loss of employment or other economic problems for the employed partner. BROMBERG & RIBSTEIN, *supra* note 10, § 4.02.

139. WYO. STAT. ANN. § 17-21-301(a)(i) (Michie 1997) (providing that each partner may bind the partnership unless that partner has no authority and the person with whom the partner is dealing knows or has received notice that the partner lacks such authority).

140. *Id.* § 17-21-303 (providing for the inclusion of a statement of authority or a statement limiting the authority of some or all partners).

141. Those partners who are authorized to act as agents for the RLLP should be clearly identified so that others doing business with the RLLP will know if they are dealing with the proper person. This protects both sides. The creditor can bind the partnership, and the partnership is protected from the creditor claiming that the deal is invalid.

142. WYO. STAT. ANN. § 17-21-105(a) (Michie 1997).

or misapplication of funds by a partner who is not authorized as an agent.<sup>143</sup>

Third, equal profit and loss sharing is the default rule for partnerships.<sup>144</sup> Partnership income and loss may be allocated in any form the partners agree upon, provided that the allocation has substantial economic effect.<sup>145</sup> Equal profit and loss sharing may not be fair to those partners who choose to contract for liability on behalf of the RLLP.<sup>146</sup> This anomaly may lead to the application of a different rule.<sup>147</sup> A form of equalized profit and loss allocation may be appropriate and can be incorporated into the partnership agreement, providing that the profit amount would increase as partner risk increased.<sup>148</sup>

Fourth, indemnification and contribution issues also affect the financial rights of the RLLP partner.<sup>149</sup> The default rule in the WUPA is that a partner who pays a partnership debt is entitled to indemnification by the partnership.<sup>150</sup> Indemnification will arise in an RLLP when a partner is directly liable for his own misconduct or the supervisory misconduct of an employee.<sup>151</sup> The RLLP liability shield may be interpreted to preclude partners from having to contribute to a deficit in partnership assets that occurs because of an indemnification proceeding.<sup>152</sup> This situation could mean the end of the partnership. However, a pre-registration agreement stating that all partners will contribute in the event of an indemnification deficit could reduce the risk of termination of the partnership.<sup>153</sup>

Fifth, under the WUPA partners are fiduciaries with a general duty of loyalty and care.<sup>154</sup> Courts may interpret RLLP status as having an effect on the duty of loyalty and care in the partnership.<sup>155</sup> A fiduciary duty of loyalty includes the duty to refrain from self-benefit with respect to partnership

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143. BROMBERG & RIBSTEIN, *supra* note 10, § 4.03(a).

144. WYO. STAT. ANN. § 17-21-401(b) (Michie 1997).

145. I.R.C. § 704(b) (1994).

146. *See supra* note 69 and accompanying text.

147. Profit and loss sharing may have to be discussed and delineated in a partnership agreement to ensure that the partner who takes on more liability will be duly compensated for the risk.

148. Equalized profit sharing would compensate the partner that contracts for liability with greater profits.

149. *See* Rubin, Quinn, Moss, Heaney, & Patterson, P.C. v. Kennel, 832 F. Supp. 922 (E.D. Pa. 1993) (holding that law firm was entitled to indemnification from a partner for funds the firm paid to clients on account of the partner's misappropriation of client funds); Gramercy Equities Corp. v. DuMont, 531 N.E.2d 629, (1988) (denying indemnification to joint venturer who alone defrauded third parties); Flynn v. Reeves, 218 S.E. 2d 661 (1975) (wrongdoing partner not entitled to indemnification).

150. WYO. STAT. ANN. § 17-21-401(c) (Michie Supp. 1998).

151. *Id.* § 17-21-306(c).

152. *Id.* § 17-21-306(b).

153. BROMBERG & RIBSTEIN, *supra* note 10, § 4.00.

154. GELB, *supra* note 71, § 7.4.

155. BROMBERG & RIBSTEIN, *supra* note 10, § 4.05.

property, dealing, and opportunity.<sup>156</sup> In the RLLP setting, there may be a conflict of interest, for example, when a liable partner attempts to prevent a distribution of earnings in order to allow the partnership to pay the claim. This would limit the liable partner's personal responsibility for wrongdoing, implicating the duty of loyalty. The RLLP partnership agreement can deal with this conflict by allowing the RLLP partners to determine how the partnership will handle situations when the duty of loyalty will be involved.

RLLP limited liability also reduces the incentive to exercise caution in supervising the partnership and therefore implicates the duty of care. Partners in an RLLP also have an increased incentive to remove themselves from participation in the RLLP in order to further insulate themselves from liability.<sup>157</sup> This issue is particularly important in small firms that are unable to pay large judgments, because these firms will likely require substantial management participation from all partners.<sup>158</sup> In larger firms the risk is small enough that it may not affect the incentives related to duty of care.<sup>159</sup>

The courts or the legislature will eventually resolve each of the issues discussed above. However, an artfully drafted partnership agreement may avoid most obstacles and provide a properly functioning RLLP.

#### COMPARISON TO OTHER WYOMING ENTITIES

The following section compares the RLLP to other Wyoming business entities, including: the Wyoming Business Corporation;<sup>160</sup> the Wyoming Limited Liability Company;<sup>161</sup> and the Limited Partnership (LP).<sup>162</sup>

##### *Formation*

The RLLP entity is simple to form.<sup>163</sup> Conversely, the corporation requires a great deal of planning and paperwork, including articles of incorporation, shareholder agreements, issuance of shares, corporate records and reports, and bylaws.<sup>164</sup> The LLC also requires extensive planning and pa-

156. *Id.*

157. See *supra* notes 132-136 and accompanying text.

158. A particular problem may occur where professional RLLP partners have to discuss partnership business with one another, particularly in a law firm. This may lead to the loss of limited liability for all partners involved, however, the actual result remains unresolved by the RLLP statute.

159. See generally Edward M. McNally & John H. Small, *Alternative Entities: The Multiple Choices Available in Delaware*, 12 DEL. LAW. 27 (1994); Steven A. Waters & Walt Miller, *Partnerships*, 51 SMU L. REV. 1245 (1998).

160. WYO. STAT. ANN. §§ 17-16-101 to -1804 (Michie 1997).

161. *Id.* §§ 17-15-101 to -144.

162. *Id.* §§ 17-14-101 to -1104.

163. See *supra* notes 38-54 and accompanying text.

164. WYO. STAT. ANN. §§ 17-16-101 to -105 (Michie 1997).

perwork.<sup>165</sup> In the LP, a statement of limited partners is required before limited liability is available, making the LP a time intensive entity to form.<sup>166</sup> However, forming the RLLP is neither time nor labor intensive. Since partnerships can be formed inadvertently, a business that is actually using a partnership form would simply have to register to become an RLLP.<sup>167</sup> Ostensibly, anyone operating a business for profit may register as an RLLP in Wyoming.<sup>168</sup>

### *Limited Liability*

The Wyoming RLLP, the Wyoming Business Corporation, the LLC, and the LP each provide some form of limited liability.<sup>169</sup> The level and availability of the limited liability varies with each entity. The RLLP statute limits partner liability for personal wrongdoing,<sup>170</sup> while the corporation and the LLC provide limited liability to shareholders and directors, or members and managers.<sup>171</sup> The LP provides a limited partner with limited liability, but that partner is also unable to participate in the management of the LP.<sup>172</sup>

Constraints on shareholders of a corporation and members of an LLC also impact limited liability. Ordinarily, corporate shareholders are unable to participate in the management of the corporation, although they may do so in other capacities.<sup>173</sup> LLC members, if so authorized by the operating agreement, may participate in management while retaining limited

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165. Along with filing requirements, the operating agreement governs the internal operation of the LLC. While this form is flexible, proper planning is necessary to preclude problems from arising. The LLC form requires extensive planning and consideration. However, unlike the RLLP statute, the flexible LLC statute allows for single member LLCs, which can be a valuable planning tool. WYO. STAT. ANN. §§ 17-15-106 to -112 (Michie 1997).

166. WYO. STAT. ANN. § 17-14-301 (Michie 1997).

167. *Id.* §§ 17-16-101 to -105.

168. *See supra* note 39 and accompanying text.

169. WYO. STAT. ANN. §§ 17-21-306; -16-622; -15-113; -14-403 (Michie 1997).

170. *Id.* § 17-21-306.

171. However, the shareholders or members may become liable for personal wrongdoing or upon piercing of the corporate veil. *See supra* note 71 and accompanying text.

172. In the LP, the limited partners do not materially participate in the partnership by definition. However, one could set up an RLLP similar to an LP, where the partnership agreement waives the limited liability for some partners. *See supra* note 69. Those partners who maintain limited liability may still participate and not be subject to the passive activity limitations. I.R.C. § 469(h) (1994).

173. WYO. STAT. ANN. § 17-16-801 (Michie 1997) provides that management responsibilities rest with the board of directors who are elected by the shareholders. However, under the Wyoming Business Corporation Act a general business corporation can be formed in a manner that does not resemble a typical corporation. Several provisions that allow for this less formal type of entity are: *Id.* § 17-16-732(a)(i) (dispensing with or limiting the board of directors); *Id.* § 17-16-840 (allowing a single officer to perform all of the duties of president, vice-president, treasurer, and secretary); *Id.* § 17-16-701(a),(c) (not requiring annual meetings); and *Id.* § 17-16-206(c) (dispensing with bylaws). Default provisions are provided if there are no bylaws adopted, including: (i) an annual meeting shall be held within three (3) months after the close of the corporation's fiscal year; (ii) the required officers shall be the president, the secretary and the treasurer; and (iii) bylaws may be adopted at any director or shareholder meeting. *Id.*

liability.<sup>174</sup> RLLP partners participate directly in the management of the RLLP and are agents and fiduciaries of the partnership.<sup>175</sup> This agency relationship endows the RLLP partner with actual and apparent authority to bind the partnership.<sup>176</sup> Under the WUPA a partnership may file a statement of partnership authority,<sup>177</sup> which can limit or expand the authority of any partner.<sup>178</sup> This ability makes the RLLP the entity with the most limited liability and the most partner freedom.

### *Taxation*

The taxation of a limited partnership is essentially the same as the general partnership. Either may choose to “check-the-box” and be taxed as a C corporation.<sup>179</sup> Unlike in an LP, all RLLP partners are treated as general partners for tax purposes.<sup>180</sup> The partner may enjoy limited liability and still materially participate enough to avoid having the loss treated as a passive activity loss.<sup>181</sup> While partnerships avoid the double taxation of corporations, which is often desirable, the LLC also now enjoys partnership classification by the I.R.S., allowing it to utilize the pass-through taxation method. Thus, the RLLP and the LLC provide similar availability to the benefit of pass-through taxation.<sup>182</sup>

The Wyoming RLLP can be an advantageous form for doing business. However, the Wyoming RLLP, unlike other Wyoming entities, has few safeguards to help protect the public.

174. *Id.* § 17-15-116.

175. *See Lutz v. Schmillen*, 899 P.2d 861 (Wyo. 1995). When a partner acquires property contrary to his fiduciary duty, he is held to be a trustee of the property for the partnership’s benefit. Also, while it is acknowledged that the partnership relationship does not preclude a partner’s procurement of realty interests in his own right and with his own funds, the partner can do so only as long as the partnership does not suffer any disadvantage and the partner who is making the purchase does not reap any individual advantage from his position as a partner. *Id.* at 864. When a partner obtains financing for the development of real property in the course of a plan which had been originally pursued by the partnership for the same purpose, excluding other partners from participating further in the originally intended project, the partner has intercepted a partnership opportunity in breach of his fiduciary duty to the partnership. *Id.* at 865.

176. No authority is deemed to exist if the partner has no authority to act for the partnership in a particular matter, and the person with whom the partner is dealing knows or has received notice that the partner lacks authority. Otherwise apparent authority exists. WYO. STAT. ANN. § 17-21-301 (Michie 1997).

177. *Id.* § 17-21-303.

178. *Id.*

179. *See supra* note 109 and accompanying text.

180. This indicates that the I.R.S. will assume a partner in an RLLP materially participates in the RLLP. *See supra* notes 132-136 and accompanying text.

181. *See supra* note 115 and accompanying text.

182. *See supra* notes 105-107 and accompanying text.

## PROPOSED AMENDMENTS TO THE WYOMING RLLP STATUTE

Wyoming's version of the registered limited liability partnership raises several concerns. The concerns include the lack of an insurance requirement,<sup>183</sup> the lack of certain formalities,<sup>184</sup> and the lack of enumerated consequences for breach of the included formalities.<sup>185</sup> When coupled with the large liability shield provided by the Wyoming RLLP statute, these shortcomings are the catalyst for concern that the Wyoming RLLP statute is dangerous. Amendments to the Wyoming RLLP will protect Wyoming and the public.

An insurance requirement for a Wyoming RLLP would temper the wide reaching limited liability shield. However, none of the other Wyoming business entity statutes contain any type of insurance requirement.<sup>186</sup> If the Wyoming legislature were to amend the Wyoming RLLP to require even a small insurance policy, the utility of the RLLP in Wyoming would be diminished. Business people would choose other forms that do not include an insurance requirement. Comparing the number of Delaware RLLPs formed since 1993 to the number of Wyoming RLLPs formed since inception substantiates this argument.<sup>187</sup> Without an insurance requirement, Wyoming may also attract out of state business ventures to form a Wyoming RLLP. An insurance requirement is not a viable option for tempering the broad limited liability shield offered by the Wyoming RLLP statute.

The application of corporate veil-piercing theories by statute may be a viable option for tempering the broad limited liability shield of the Wyoming RLLP. Requiring corporate formalities such as annual meetings insures proper business conduct, and provides courts with a way to impose liability on an RLLP. However, corporate style formalities are not tailored to the RLLP form. For instance, the requirement of an annual meeting or other corporate formality may be redundant in an RLLP situation where the partners meet on a daily basis. Therefore, the solution to a formality requirement lies in enumerating the consequences of a breach of the requirements already listed in the RLLP statute.

The Wyoming Legislature should amend the RLLP statute to include stated consequences for the failure to use the proper name form. Inclusion of "RLLP," or "LLP" to the name of the entity gives the public proper information regarding the type of entity they are dealing with. The failure to

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183. See *supra* notes 15-16 and accompanying text.

184. See *supra* notes 78-81 and accompanying text.

185. See *supra* notes 83-89 and accompanying text.

186. See generally WYO. STAT. ANN. §§ 17-3-101 to -23-302 (Michie 1997).

187. See *supra* notes 31-36 and accompanying text.

enumerate the consequences of noncompliance in this regard provides the entity with an argument that noncompliance should not lead to loss of limited liability by reason of analogy to the LLC statute. The Wyoming LLC statute specifically enumerates loss of limited liability as a consequence of failure to use the appropriate acronym.<sup>188</sup> The addition of a similar phrase to the Wyoming RLLP statute does not detract from the utility of the Wyoming RLLP, like an insurance requirement might, yet it provides the public with a substantial benefit. Knowledge of the type of entity allows the public to make an informed determination about dealing with an RLLP.

The inclusion of enumerated consequences for failure to use the appropriate acronym is the only addition that, initially, should be made to the Wyoming RLLP statute. With this addition, the Wyoming RLLP will remain an extremely valuable entity, but not at the cost of Wyoming or its' public.

#### CONCLUSION

The Wyoming RLLP is a valuable entity.<sup>189</sup> A partnership wishing to utilize limited liability should consider the RLLP form. However, the broad limited liability shield that is untempered by consequences for noncompliance may be dangerous to the public and the State. The Wyoming legislature should review the Wyoming RLLP statute in light of any adjudication that may arise. In the meantime, the Wyoming legislature should amend the RLLP statute to include enumerated consequences for non-compliance with the name requirements. But for now, the Wyoming Legislature has provided partnerships with a powerful entity.

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188. WYO. STAT. ANN. § 17-15-105(b) (Michie 1997).

189. See *supra* note 101 and accompanying text.