

Big Changes in Pennsylvania for LLCs, LLPs, LPs, and GPs

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A major overhaul and modernization of the laws governing unincorporated associations in Pennsylvania took effect Tuesday.

[Act 170 of 2016](#), signed into law in November and currently being tracked by [Barley Snyder](#) attorneys, amends parts of the Pennsylvania Consolidated Statutes to repeal and replace laws governing unincorporated associations that haven't been updated in more than 25 years.

Pennsylvania-registered, unincorporated associations affected by the new law include:

- Limited liability partnerships
- General partnerships
- Limited partnerships
- Limited liability companies
- Unincorporated nonprofit associations
- Business trusts

Many of the new provisions are widely considered to be more management friendly, and amendments to existing LLC operating agreements and LP agreements may be appropriate for your business.

Notable changes include:

Statutory default rules for LLCs and contents of the operating agreement. The LLC is one of the most popular entity forms because it allows the owners broad governance flexibility. However, this flexibility is not limitless. The new law lists twenty items an operating agreement may NOT dictate, but also makes clear certain items it can. This added clarity increases the playing surface for LLC owners.

"Full shield" protection for general partners. General partners are still liable for all debts and obligations of the partnership. However, the new law provides a shield for general partners by requiring the partnership to reimburse and indemnify the general partner for all out of pocket costs incurred in the line of duty to his position so long as he acts within the appropriate standards of conduct.

Distribution tests. The new law provides two tests for measuring the legality of LLC distributions, which include transfers of cash or property to members:

1. "Insolvency Test" - a distribution is not allowed if the company couldn't pay its debts as they become due; and
2. "Balance Sheet Test" - a distribution is unlawful if, after the distribution is made, the company's total liabilities would exceed the company's total assets.

Under the new law, companies must satisfy both tests in order for the distribution to be lawful, and these tests apply to both interim and liquidating distributions. This is a much-needed change in LLC law as the prior law did not have a test for measuring the legality of distributions. As a practice tip, the Balance Sheet Test permits unrealized appreciation and depreciation of assets to be considered when measuring the legality of a distribution.

Governance rights vs. economic rights. Ownership interests in LLCs and partnerships can be divided into "governance rights" and "economic rights." The new law clarifies that a member can only transfer economic rights (the right to receive distributions) to persons outside the business, and governance rights are not transferrable unless the operating agreement provides otherwise. The result is that a creditor of only one member cannot execute upon that member's governance rights and thus cannot interfere with the management of the company. This clarification affords the company additional protection against creditors of its owners. However, this limitation does not apply to the interest of the sole member of an LLC, whose entire governance interest is subject to execution.

Don't get left in the Stone Age. Ensuring your governance documents are up to speed with today's legal climate and the latest changes in Pennsylvania law is critical to the continued success of your business. There's no better time than the present to conduct a careful review of your business's governance documents and the professionals at Barley Snyder are available to answer any questions. If you do have any questions on how these new laws affect you and your business, feel free to [reach out to me](#) at 717-208-8828 or by email at bkorman@barley.com.