

Changes to PA Business Corp. Law may affect the way Commercial Real Estate is owned in PA

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For decades owners of commercial real estate in Pennsylvania took title in limited partnerships, not necessarily because it was the best entity to own and manage property, but because it minimized the effect of the Capital Stock Tax. The Capital Stock Tax utilized a formula to tax the assets of corporations and limited liability companies, including the equity of real estate owned by the business. Limited partnerships are generally composed of limited partners, who are essentially passive investors, and a general partner, who is tasked with the management of the partnership. The general partner is subject to liability for the partnership, and therefore, the general partner is often a corporation or limited liability company (meaning it was also subject to the Capital Stock Tax). Owners of commercial real estate traditionally were tasked with forming 2 entities, the limited partnership and the entity that would act as general partner, and therefore, incurred additional legal and accounting expenses.

The Capital Stock Tax was repealed effective December 31, 2015, and along with it, the primary reason for holding real estate in limited partnerships in Pennsylvania. Limited liability companies are generally favored by attorneys because of the flexibility they give members to manage the affairs of the company while still receiving liability protection. Many investors and developers will continue to use limited partnerships to own and develop real estate out of familiarity and habit, however, in the not too distant future banks, investors, title companies and attorneys will likely see limited partnerships as the exception, rather than the rule, when it comes to owning commercial real estate.

Limited liability companies are either member-managed or manager-managed. Often manager-managed limited liability companies are run in a similar manner to limited partnerships, with the manager acting like a general partner and the other members acting as passive limited partners. Real estate investors who were accustomed to the limited partnership structure may wish to continue utilizing the limited partnership-style of management and opt for manager-managed limited liability companies. Part of the reason attorneys prefer limited liability companies is because they offer a variety of options for clients. A member-managed limited liability company may appoint a managing-member who will act like a general partner, or the company may require all decisions to be made by a majority vote of the members. Limited liability companies offer greater flexibility than limited partnerships to real estate investors, and unlike limited partnerships in Pennsylvania, the individual members are not listed with the Corporation Bureau when the entity is formed.

In addition to the repeal of the Capital Stock Tax, Pennsylvania overhauled the Business Corporation Law ("BCL") in 2015. There were a number of significant changes relating to real estate, including an amendment to the definition of "doing business" in Pennsylvania. Previously, the statute provided that owning and leasing

real estate was not considered doing business in the Commonwealth of Pennsylvania. Following the amendment to the BCL, the act of leasing real estate is considered "doing business", which carries with it the requirement to register the entity with the state.

The amended BCL also permits entity conversions in Pennsylvania. This allows a corporation or a limited partnership to convert to a limited liability and vice versa. Real estate owners who formed limited partnerships as a result of the Capital Stock Tax may now want to convert to a limited liability company. If the requirements under the BCL and realty transfer tax regulations are satisfied, real estate owned by the entity can be re-titled following the conversion of the entity to a limited liability company without incurring transfer tax.

These changes will likely result in limited liability companies becoming the preferred entity choice of commercial real estate owners in Pennsylvania.

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