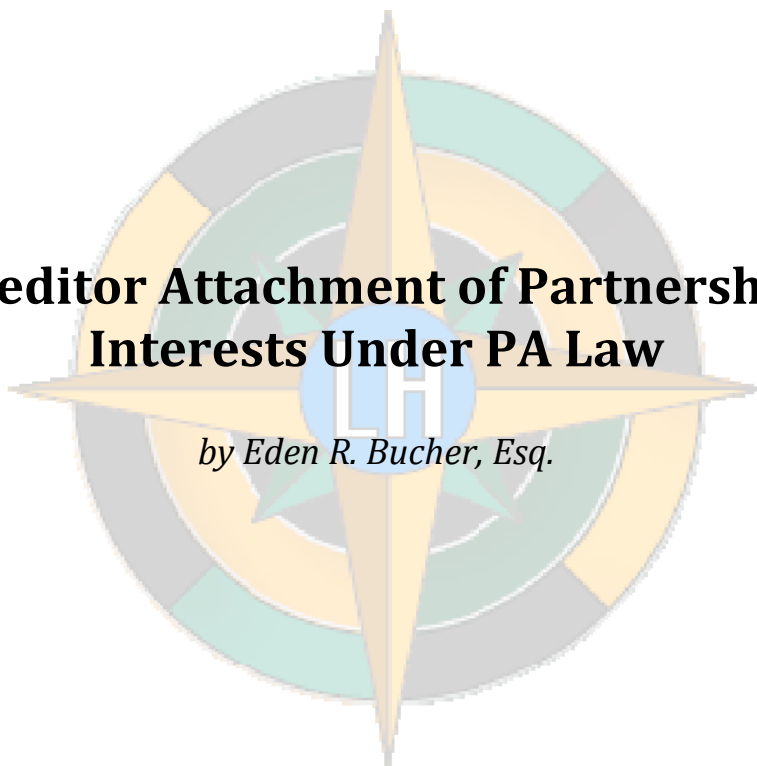


A Leisawitz Heller White Paper

Creditor Attachment of Partnership Interests Under PA Law

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When partners in business enterprises are faced with unexpected creditor claims, they often wonder if their ownership interest in their partnership can be seized. Shareholders in closely held corporations face similar concerns, but the law of stock transfers is generally better understood than the rules for partnerships. Consequently, this white paper will attempt to shed light on the attachment of partnership interests.

Ultimately the question becomes, “How far can a creditor go to execute a borrower’s ownership interest in a limited partnership agreement?” Section 8563 of the Pennsylvania Revised Uniform Limited Partnership Act (15 Pa. USCA 8501, *et seq.*) offers some insight:

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. This chapter does not deprive any partner of the benefit of any exemption laws applicable to his partnership interest.

In other words, this law allows creditors to be paid from partnership distributions, but it does not allow seizure of the actual partnership interests.

The courts have ruled repeatedly that a creditor of an individual partner cannot reach partnership property in execution (see *e.g.* Wiseman v. Martorano, 405 Pa. 369, 175 A.2d 873 (1961) and Shirk v. Caterbone, 201 Pa. Super. 544, 193 A.2d 664 (1963). Such a creditor can be paid only out of what is due to the individual partner from the partnership by way of distributions after all partnership obligations, including those of any judgment creditor of the partnership as a whole, have been satisfied.

It should also be noted that partnerships may be general partnership or limited partnerships. The latter help insulate limited partners from personal liability for debts of the partnership. It is important to note, however, that the creditor protections afforded by limited partnerships protect the limited partners, not their partnership interests. Consequently, many limited partnership agreements contain provisions similar to the following:

a) In the event a Partner’s interest is taken or disturbed by levy, foreclosure, charging order, execution or other similar proceeding, the Partnership shall not dissolve; b) the assignee of any Partner’s interest shall in no event have the right to interfere in the management or the administration of the Partnership business or affairs, or to act as a Partner in the Partnership. The assignee shall have only the right to receive distributions, profits and losses attributable to the assignor Partner’s interest in the Partnership; c) an

assignee of any partnership interest, whether of a General Partner or a Limited Partner, shall receive the federal K-1 form and all relative state forms and report all income and loss on his or her income tax returns each year in accordance with Rev. Rul. 77-137; and

d) Notwithstanding anything to the contrary contained in this Agreement, (i) an assignee who has not become a substituted Limited Partner in accordance with the terms and provisions of this Agreement, or (ii) an assignee who acquired an interest in the Partnership by virtue of levy, foreclosure, charging order or other similar procedure shall not have the right to vote in the capacity of a "Limited Partner"; the only rights of such assignees shall be an allocation of income, gain, loss, deduction, credit and distributions to which his or her assignor would otherwise be entitled to receive.

Unlike the Uniform Limited Partnership Act, the Revised Uniform Limited Partnership Act does not provide for foreclosure and sale of Limited Partnership interests. The holder of a judgment against an individual partner can issue a writ of execution directed to the partnership as garnishee pursuant to Pa. R.C.P. 3108. The judgment entered against the garnishee on the writ would be in the form of a charging order in the case of attachment against a partnership interest pursuant to Pa. R.C.P. 3148. The charging order does not allow the judgment creditor to force the dissolution or otherwise interfere with the management of the partnership or reach the partnership assets, but merely allows the judgment creditor to reach the debtor's income stream from the partnership. The case law on charging orders and partnership interests is very limited in Pennsylvania. However, pursuant to the rules and statutes referred to above, it is the proper remedy for a judgment creditor who wishes to execute on the partnership interest of the judgment debtor.

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