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# 2007 Kentucky Survey Issue

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THE UNIFORM LIMITED PARTNERSHIP ACT (2001)  
COMES TO KENTUCKY: AN OWNER’S MANUAL

Dean Allan W. Vestal
Thomas E. Rutledge

I. INTRODUCTION

2006 saw Kentucky adopt two new partnership laws governing the general and the limited partnership. Based on, respectively, the Uniform Partnership Act (1997)\(^1\) ("RUPA")\(^2\) and the Uniform Limited Partnership Act (2001)\(^3\) ("ULPA")\(^4\), each of these laws is at minimum a modernization of and in certain...
respects a reconceptualization of these business structures as previously understood.

The objective of this article is not to provide an entirely comprehensive review of the new limited partnership act - such is beyond the scope of any article. Notwithstanding what may appear as surface simplicity, RULPA is and was a complicated statutory system; ULPA is a more complex statute building upon the prior law. We do not herein attempt to provide a complete exegesis of each provision or how it relates to all other provisions. Even were such possible, unanticipated fact situations will arise that we could not address. This article is meant to be an initial, and not the final, step in appreciating how this new statute functions. Our objectives are to introduce the structural themes that are used in the law, to highlight particular provisions that will dictate different consequences than what would apply under the predecessor laws, review the rules applicable when interfacing with the Secretary of State, and highlight departures from the uniform acts made in the Kentucky adoption.

As alluded to above, KyULPA contains non-uniform provisions; that non-uniform language is highlighted and discussed herein. In crafting KyULPA for submission to the Kentucky General Assembly, there was a continuing tension between the desire to adopt the uniform language and the realization that the uniform acts are not in any sense perfect. In fact, both academics and practitioners have "had a field day" criticizing the acts from standpoints of the structural decisions made in drafting to whether the language employed well suits the desired outcome. Generally speaking, departures were made from the uniform language where there was developing a consensus that it was deficient and a clearly better alternative was available. As discussed in greater detail below, non-uniform transition provisions that are in the end "non-transition" have been adopted as well. Other departures, most notably those dealing with

Limited Partnership Act (2006)," see KY. REV. STAT. ANN. § 362.2-1207 (LexisNexis 2006), sometimes referenced herein as "KyULPA."


6. The authors were the drafters of KyRUPA and KyULPA. The provisions dealing with Secretary of State filings were prepared initially in coordination with Maryellen B. Allen, general counsel to the office of the Secretary of State (1997-2002) and subsequently with Secretary of State Trey Grayson and Tracy Goff Herman, Director of the Division of Corporations. However, neither this article in general nor in particular the provisions addressing filings with the office of the Secretary of State have been reviewed or endorsed by that office.


8. For example, ULPA § 408 has been criticized, see, e.g., J. William Callison, "The Law Does Not Perfectly Comprehend ...": The Inadequacy of the Gross Negligence Duty of Care Standard in Unincorporated Business Organizations, 94 KY. L.J. 451 (2006), and has in KyULPA been replaced with an entirely different formula.

9. See infra notes 13 through 21 and accompanying text.
filings with the office of the Secretary of State, address matters unique to Kentucky law.

A. Are KyRUPA and KyULPA Worth the Trouble?

It is a valid question to ask whether the adoptions of KyRUPA and KyULPA are a worthwhile effort. The adoption of the new laws entails significant transaction costs in attorney education, client education, confusion during the transition period, and the modification of existing partnership agreements to comply with the new law while continuing to reflect party expectations. Still, the answer is a resounding “yes.” The new acts incorporate the current status of the law as it has grown through the common law and the continuing modernization of business organization law. Kentucky benefits from adopting uniform and model acts, especially in areas such as business organization law for which Kentucky courts issue few published decisions. Uniformity permits business men and women (and their attorney advisors) to look to other states as well as major treatises for guidance. Those other states and treatises are now focused on RUPA and are moving their focus to ULPA. Furthermore, failure to adopt updated business law simply makes Kentucky a less viable jurisdiction for out of state businesses when considering expansion and investment opportunities.

B. The Legislative Process

H.B. 234, containing both KyRUPA and KyULPA, was introduced by Representative Scott W. Brinkman to the 2006 General Assembly on January 5, 2006. The bill was assigned to the Judiciary Committee, and hearings were held on February 8. That day the bill was voted out of the Judiciary Committee with a favorable recommendation by a vote of 12 for and 1 against. The full House of Representatives voted 93 for and 6 against the bill on February 27, 2006, and it was referred to the Senate, where it was assigned to the Judiciary

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10. “Our dilemma is that we hate change and love it at the same time; what we really want is for things to remain the same but get better.” Statement of Sydney J. Harris, Wikipedia, available at http://en.wikipedia.org/wiki/Sydney_Harris (last visited June 22, 2007).

11. As of this writing, although it has been effective since July 15, 1994, no Kentucky state court has published an opinion interpreting any provision of the Kentucky Limited Liability Company Act (the “KyLLCA”), found at KY. REV. STAT. ch. 275.

12. Essentially identical legislation had been introduced to the 2005 General Assembly (H.B. 246, introduced February 2, 2005), the 2004 General Assembly (H.B. 190, introduced January 6, 2004), and the 2003 General Assembly (H.B. 558, introduced February 18, 2003). Each of these prior introductions has been by Representative Brinkman. Breaking the log-jam on the consideration and passage of RUPA and ULPA was HCR 113, passed by the House Judiciary Committee on February 16, 2005. This resolution directed the House Judiciary Committee, prior to December 1, 2005, to consider RUPA, ULPA, amendments to the LLC Act and amendments to the Kentucky Business Corporation Act (the “KyBCA”). Amendments to the KyLLCA and the KyBCA were submitted to the 2006 General Assembly in, respectively, H.B. 349 and H.B. 350, but no action was taken on either proposal.
Committee. It held hearings on March 16, and the bill was voted out of committee on a vote of 10 for and 0 against. The full Senate voted 38 for and 0 against the bill on March 22, 2006. The bill was signed by Governor Fletcher on April 5, 2006.

C. Codification and Effective Dates

The current partnership and limited partnership acts will remain in place and will continue to apply to certain partnerships formed prior to July 12, 2006.13 KyRUPA is codified in KRS ch. 362.1 and KyULPA is codified in KRS ch. 362.2.

The states have adopted a variety of approaches to the phase-in of ULPA.14 KyULPA has an initial effective date of July 12, 2006.15 As of that date, all newly formed limited partnerships are organized under and governed by the new act. KyRULPA will continue to govern all limited partnerships formed under KyRUPA, namely those formed on or after July 15, 1988 and prior to July 12, 2006.16 Limited partnerships formed prior to July 15, 1988 are not governed by KyRULPA unless they have elected to be so by filing an amended and restated  


15. KY. REV. STAT. ANN. § 362.2-1205(1)(a) (LexisNexis 2006). KyRUPA has the same initial effective date. § 362.1-1204; see also Op. Ky. Att’y Gen. (OAG) 06-001 (April 19, 2006).

A limited partnership existing on July 11, 2006, whether formed under KyRULPA or prior law, may elect to be governed by KyULPA by filing an amended and restated certificate of limited partnership. Many existing limited partnerships will want to do so in order to take advantage of the advances made in the new statutes including LLLP status. In the course of that amendment, a limited partnership desiring to be an LLLP must modify its name to meet the statutory requirements for the name of a LLLP.

Kentucky adopted the UPA in 1954, and the likelihood of any pre-UPA partnerships remaining in existence is quite low. Kentucky adopted RULPA in 1988, but with the proviso that it would not govern limited partnerships formed prior to its effective date absent an election by a limited partnership to be governed by the new law. From and after July 12, 2006, Kentucky will have:

- Partnerships formed prior to July 12, 2006 that remain governed by KyUPA;
- Partnerships formed on or after July 12, 2006 that are governed by KyRUPA;
- Partnerships formed prior to July 12, 2006 that have elected to be governed by KyRUPA;
- Limited partnerships formed prior to June 18, 1970 that remain governed by the then existing limited partnership law;
- Limited partnerships formed on or after June 18, 1970 and prior to July 15, 1988 that remain governed by the then existing limited partnership law;
- Limited partnerships formed prior to July 15, 1988 that elected to be governed by KyRULPA;
- Limited partnerships formed after July 15, 1988 and prior to July 12, 2006 that are governed by KyRULPA;
- Limited partnerships formed on or after July 12, 2006 that are governed by KyULPA;
- Limited partnerships formed prior to July 15, 1988 that elected to be governed by KyULPA; and

17. KY. REV. STAT. ANN. §§ 362.521(1)-(2) (LexisNexis 2006). The prior limited partnership act, §§ 362.410-362.710, an enactment of the Uniform Limited Partnership Act (1916), was effective June 18, 1970 and applied to limited partnerships formed through July 14, 1988.

18. KY. REV. STAT. ANN. § 362.2-1204(2) (LexisNexis 2006). From July 12, 2006, a limited partnership formed under pre-KyRULPA law may elect to be governed by KyULPA, but may not elect to be governed by KyRULPA. See KY. REV. STAT. ANN. § 362.521(2) (LexisNexis 2006) as amended by 2006 Acts, ch. 149, § 238.

19. See infra notes 218 through 222 and accompanying text.

20. See infra note 65 and accompanying text.

21. See supra notes 16-17 and accompanying text.
• Limited partnerships formed under KyRULPA that elect to be governed by KyULPA.

D. The Genesis of ULPA

As RUPA was being completed there were calls for a similar rewrite of RULPA.\(^22\) RUPA had been drafted with the intention that it no longer serve as the gap filler for limited partnership law.\(^23\) As such, it was not drafted to address the concerns of limited partnerships. Furthermore, if applied as the gap filler for state enactments of RULPA (in either the 1976 or 1985 versions)\(^24\) there would be fundamental shifts in the nature of the relationship between, on the one hand, the limited partnership and the limited partners and, on the other hand, the general partners. At the same time the limited partnership was itself facing a crisis of application. The widespread success of the LLC was usurping many of the traditional applications of the limited partnership, and new statutory mechanisms needed to be put in place to preserve the continuing utility of the structure in its most effective applications. A NCCUSL drafting committee was appointed in 1997, and in this project as contrasted with the earlier RUPA efforts, NCCUSL made greater use of, and in fact placed greater reliance upon, the various advisors appointed by the American Bar Association. ULPA was approved by NCCUSL in 2001, and was later in that year approved by the Committee on Partnerships and Unincorporated Business Organizations of the Section of Business Law, American Bar Association. Kentucky was the eighth jurisdiction to adopt ULPA.

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\(^{22}\) See, e.g., Allan W. Vestal, A Comprehensive Uniform Limited Partnership Act? The Time Has Come, 28 U.C. DAVIS L. REV. 1195, 1195-96 (1995) (“The Revised Uniform Partnership Act of 1994 (RUPA) is about to make the world of general partnerships chaotic. It promises to do the same to the world of limited partnerships. That chaos can be avoided if we move without delay to delink the law of limited partnerships from that of general partnerships by drafting and adopting a comprehensive uniform limited partnership act.”) (citations omitted).

\(^{23}\) See KY. REV. STAT. ANN. § 362.523 (LexisNexis 2006); see also § 362.447.

E. The End of Linkage

One crucial element in understanding ULPA is an appreciation of it as a free-standing organizational law not dependent upon any other act. Under RULPA, where it was silent, reference was made to UPA for the controlling rule, and from there to other principles of law. Delinkage of the law began with RUPA, which excluded from its scope the limited partnership. However, as the various state adoptions of RULPA continued to require a “gap filler,” references were continued to either the newly enacted RUPA or to the otherwise superseded UPA. ULPA was written to be an entirely self-contained. There is no mechanism by which a limited partnership formed under KyRULPA or the predecessor limited partnership act may elect to have KyRUPA serve as its “gap filler” statute.

II. A KYULPA OWNER’S MANUAL

ULPA is divided into twelve articles, and this discussion follows that same outline. In the course of drafting ULPA, the drafting committee was following on RUPA. As such, for reasons at times well reasoned and at other times inexorably dogmatic, the language used often tracks the language used earlier in RUPA.

25. See Kleinberger, User’s Guide, supra note 7, at 609 (“Of course, the new Act’s most fundamental change consists of replacing a linked statute with a stand alone statute.”). Professor Kleinberger served as the Reporter on ULPA.

26. RULPA § 1105 (1985); KY. REV. STAT. ANN. § 362.523 (LexisNexis 2006). Before that, under both the Uniform Limited Partnership Act (1976) and the Uniform Limited Partnership Act (1916), UPA served as a “gap filler,” providing the substantive law when the limited partnership law was silent. See RULPA § 1105 (1976); ULPA § 29 (1916); KY. REV. STAT. ANN. § 362.690 (repealed 1988); see also KY. REV. STAT. ANN. § 362.447 (LexisNexis 2006).

27. KY. REV. STAT. ANN. § 362.170 (LexisNexis 2006); UPA § 5 (1914).

28. RUPA § 202(b) (1997); KY. REV. STAT. § 362.1-202(2) (LexisNexis 2006). At that point, while RUPA “rejected” RULPA even as RULPA still referenced UPA. Such cases of unilateral linkage exist elsewhere in business organization law. For example, in Kentucky, the professional service corporation act, KY. REV. STAT. ch. 274, references the Kentucky Business Corporation Act, KY. REV. STAT. ch. 271B, where the PSC Act does not set forth a controlling rule. KY. REV. STAT. ANN. § 274.015(2) (LexisNexis 2006). Cooperative associations may elect to be governed, to the extent not set forth in KY. REV. STAT. ch. 272, by either the KyBCA, KY. REV. STAT. ch. 271B, or by the Non-Profit Corporation Act, KY. REV. STAT. ch. 273. See KY. REV. STAT. ANN. § 272.042.

29. While some states, in adopting RUPA, have then linked their existing limited partnership law, based upon RULPA, to RUPA, see, e.g., KAN. STAT. ANN. § 56-1a604 (2002), other states, while adopting RUPA, have retained the linkage of RULPA to the state adoption of UPA. See, e.g., DEL. CODE ANN. tit. 6, § 17-1105 (2006).

30. For a discussion of linkage and the process of delinking partnership and limited partnership law, see Elizabeth S. Miller, Linkage and Delinkage: A Funny Thing Happened to Limited Partnerships When the Revised Uniform Partnership Act Came Along, 37 SUFFOLK U. L. REV. 891 (2004).
A. KyULPA Article 1 – General Provisions

KyULPA’s definitions have been carried over from the uniform act with only one modification; a non-uniform definition of “sign/signature,” has been substituted.\(^{31}\) In addition, non-uniform definitions of “deliver/delivery,”\(^{32}\) “electronic transmission/electronic delivery,”\(^{33}\) “name of record with Secretary of State,”\(^{34}\) and “professional services”\(^{35}\) have been added.

ULPA § 103, dealing with knowledge and notice, has been carried over from the uniform act without modification. As such, it does not conform to the provision in KyRUPA, which modified the uniform act language of RUPA.\(^{36}\) As contrasted with the provisions under the KyBCA, KyULPA is focused upon when a person knows or should know of a fact, rather than upon the procedures by which information is delivered.\(^{37}\) This provision as well contains several deemed notice provisions, namely:

- That a certificate of limited partnership filed by the Secretary of State is notice that a partnership is a limited partnership and that those who are named therein as general partners are general partners;\(^{38}\)
- Notice that one has ceased to be a general partner ninety days after the filing of an amended certificate of limited partnership where the filing of the statement of dissociation;\(^{39}\)
- The dissolution of a limited partnership ninety days after filing of an amendment to the certificate of limited partnership stating that it is dissolved.\(^{40}\)

\(^{31}\) This non-uniform definition conforms to that in KY. REV. STAT. ANN. § 362.1-101(19) (LexisNexis 2006), which itself conforms to § 271B.1-400(24).

\(^{32}\) KY. REV. STAT. ANN. § 362.2-102(4) (LexisNexis 2006); accord § 271B.1-400(5); § 362.1-101(3).

\(^{33}\) KY. REV. STAT. ANN. § 362.2-102(7) (LexisNexis 2006); accord § 271B.1-400(8); § 362.1-101(5).

\(^{34}\) KY. REV. STAT. ANN. § 362.2-102(15) (LexisNexis 2006); accord § 362.1-101(9).

\(^{35}\) KY. REV. STAT. ANN. § 362.2-102(20) (LexisNexis 2006); accord § 275.005(3); § 275.015(20); § 362.1-101(16).

\(^{36}\) See KY. REV. STAT. ANN. § 362.1-103 (LexisNexis 2006).


\(^{38}\) KY. REV. STAT. ANN. § 362.2-103(3) (LexisNexis 2006). ULPA (1916) was silent as to the notice effect of the certificate of limited partnership. RULPA (1976) provided that the Certificate of Limited Partnership was notice of the existence of the limited partnership and that the persons listed therein as limited partners were limited partners, RULPA (1976) § 208, which treatment was consistent with interpretations of ULPA (1916). Conversely, RULPA (1985) provided that the certificate of limited partnership constituted the notice that the partnership is a limited partnership and of the identities of the general partners. RULPA (1985) § 208; KY. REV. STAT. ANN. § 362.429 (LexisNexis 2006).

\(^{39}\) KY. REV. STAT. ANN. § 362.2-103(4)(a) (LexisNexis 2006).

\(^{40}\) KY. REV. STAT. ANN. § 362.2-103(4)(b) (LexisNexis 2006).
\[ \text{The cancellation of a limited partnership ninety days after the effective date of the statement of cancellation;}^{41} \\
\text{The limited partnership’s conversion ninety days after the effective date of the conversion;}^{42} \text{ and} \\
\text{The merger of the limited partnership ninety days after the effective date of the merger.}^{43} \]

A limited partnership organized under KyULPA is a legal entity distinct from its partners.\textsuperscript{44} The adoption by a particular limited partnership of limited liability limited partnership status does not alter the entity, which is the same entity before and after any election into (or out of) that status.\textsuperscript{45} A limited partnership may be formed for any lawful purpose except for rendering professional services.\textsuperscript{46} The prohibition against a professional limited partnership is non-uniform; in the event that a limited partnership is formed to render professional services, it will likely be treated as a general partnership.\textsuperscript{47} The provision that a limited partnership may be organized for any lawful purpose does not restrict a limited partnership to a for-profit purpose.\textsuperscript{48} Still, the organization of a limited partnership other than with a for-profit motive will raise certain issues with respect to its structure and the application of ULPA.\textsuperscript{49}

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41. KY. REV. STAT. ANN. § 362.2-103(4)(c) (LexisNexis 2006).
42. KY. REV. STAT. ANN. § 362.2-103(4)(d) (LexisNexis 2006).
43. KY. REV. STAT. ANN. § 362.2-103(4)(e) (LexisNexis 2006).
44. KY. REV. STAT. ANN. § 362.2-104(1) (LexisNexis 2006). This provision puts the partnership on the same footing as a corporation, a limited liability company, and a RUPA partnership, see KY. REV. STAT. ANN. § 362.1-201(1), and eliminates any argument that a limited partnership is simply an aggregate of its partners. None of ULPA (1916), RULPA (1976), nor RULPA (1985) addressed whether a limited partnership is an entity or an aggregate.
45. KY. REV. STAT. ANN. § 362.2-104(1) (LexisNexis 2006); accord § 362.1-201(1) (parallel treatment of a partnership that elects LLP status).
46. KY. REV. STAT. ANN. § 362.2-104(2) (LexisNexis 2006). Cf. § 271B.3-010(1) (“any lawful business”); § 275.005 (“any lawful business, including the provision of one (1) or more professional services”); § 362.175(1) (“a business for profit”); § 362.411(“any business that a partnership without limited partners may carry on”); § 362.1-101(10) (“a business for profit”).
47. Various states have non-uniform limitations on the permissible purposes of a limited partnership. For example, Illinois, which has adopted ULPA, does not allow limited partnerships to be banks, operate railroads, or with certain exceptions write insurance. 805 ILL. COMP. STAT. 215/104(b) (2006); see also Gregg v. SR Investors, Ltd., 966 F. Supp. 746, 748 (N.D. Ill. 1997) (limited partnership formed under RULPA to operate railroad, which purpose was forbidden a limited partnership under the law of Illinois pursuant to which it was formed, rendered purported limited partnership a general partnership.).
48. Cf. KY. REV. STAT. ANN. § 362.411 (LexisNexis 2006) (“[A] limited partnership may carry out any business that a partnership without limited partners may carry on.”); § 362.175(1) (“a partnership is an association of two (2) or more persons to carry on as co-owners a business for-profit . . . .”).
49. See ULPA § 104 cmt subsec. (b) (2001)
In a change from RULPA, ULPA provides a default rule that each limited partnership will have perpetual duration.50

ULPA § 105 provides that a limited partnership has “the powers to do all things necessary or convenient to carry on its activities,” then goes on to expand this general grant, stating that the powers include “the power to sue, be sued, and defend in its own name and to maintain an action against a partner for harm caused to the limited partnership by a breach of the partnership agreement or violation of a duty to the partnership.”51 Referencing the power of the limited partnership to sue for injuries caused to it or to enforce the partnership agreement “is mentioned specifically to establish that the limited partnership itself has standing to enforce the partnership agreement.”52 The other basis for this language is that it needed to be made express in order that it could be provided that it could not be varied in the partnership agreement.53 ULPA § 105 has been modified in KyULPA to include as the basis upon which a limited partnership may bring suit against a partner “an actual or threatened injury to the limited partnership.”54 As such, no partner can defend against an action brought by the limited partnership on the basis that it involves only a prospective breach of the partnership agreement or violation of a duty to the partnership.55

With respect to each domestic limited partnership,56 KyULPA will govern (i) relations among the partners, (ii) relations between the partners and the limited partnership, and (iii) the liability of a partner as a partner for an obligation of the limited partnership. On this last component it is important to note the limitation

50. KY. REV. STAT. ANN. § 362.2-104(3) (LexisNexis 2006). This provision puts the limited partnership on a status equal to that of a corporation, § 271B.3-020(1), and a limited liability company, § 275.025(2). Cf. KY. REV. STAT. ANN. § 362.415(1)(e) (mandating that the certificate of limited partnership set forth “the latest date upon which the limited partnership is to dissolve.”).

51. KY. REV. STAT. § 362.2-105 (LexisNexis 2006); see also § 275.010. Cf. KY. REV. STAT. ANN. § 271B.3-020 (providing a “laundry list” of the powers of a corporation).


54. ULPA § 105 (2001), as modified in KyULPA, reads as follows:

A limited partnership has the powers to do all things necessary or convenient to carry on its activities, including the power to sue, be sued, and defend in its own name and to maintain an action against a partner for harm caused to the limited partnership by [a] an actual or threatened injury to the limited partnership, breach of the partnership agreement, or violation of a duty to the partnership.

See KY. REV. STAT. ANN. § 362.2-105 (LexisNexis 2006).

55. KY. REV. STAT. ANN. § 362.2-105 (LexisNexis 2006).

56. “Limited partnership” is a defined term in KY. REV. STAT. § 362.2-102(14) (LexisNexis 2006), and excludes a foreign limited partnership.
to partner liability as a partner;\(^{57}\) this provision does not modify liabilities imposed under independent contracts or other law.\(^{58}\) This governing law is not subject to modification by the partnership agreement.\(^ {59}\)

Law and equity supplement ULPA,\(^ {60}\) and interest will be determined in accordance with KRS § 362.010.\(^ {61}\) There has been added to the uniform language a non-uniform provision addressing the enforceability of agreements of limited partnership, which language is intended to place such agreement on even par with the limited liability company operating agreements.\(^ {62}\)

This provision, dealing with permissible names of limited partnerships, has been revised from the uniform language to track the provisions already in place in Kentucky for corporations and limited liability companies. Initially, any name must be distinguishable from any other name of record with the Kentucky Secretary of State.\(^ {63}\) Next, the name must include certain identifiers, and may not include certain terminology.

<table>
<thead>
<tr>
<th>LP that is not an LLLP(^ {64})</th>
<th>Must Contain</th>
<th>May Not Contain</th>
</tr>
</thead>
<tbody>
<tr>
<td>“limited” or “Ltd.”</td>
<td>“limited liability limited partnership” or “LLLP” or “L.L.L.P.”</td>
<td></td>
</tr>
<tr>
<td>or “limited partnership” or “L.P.” or “LP”</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

| LP that is an LLLP\(^ {65}\) | “limited liability limited partnership” or “LLLP” or “L.L.L.P.” | Only “limited partnership” or “L.P.” or “LP” |

The name of a limited partnership organized under KyULPA may contain the name of any partner.\(^ {66}\) Assumed names remain governed by the assumed name


\(^{62}\) Ky. Rev. Stat. Ann. § 362.2-107(3) (LexisNexis 2006); accord § 275.003. The same non-uniform language has been added to the Kentucky adoption of RUPA. See § 362.1-104(3).

\(^{63}\) Ky. Rev. Stat. Ann. § 362.2-108 (LexisNexis 2006); see also § 362.2-102(15) (definition of “name of record with the Secretary of State”); accord § 362.1-101(9). The “any name of record” includes the real name of any corporation, limited partnership, limited liability company, any name set forth on a registration as a limited liability partnership, see § 362.555, or Statement of Qualification, see § 362.1-1101, any fictitious name adopted for use in Kentucky, any reserved name, and any assumed name filed with the Secretary of State. It does not include trademark or service mark registrations, see § 365.571, or assumed name filings made by individuals.

\(^{64}\) Ky. Rev. Stat. Ann. § 362.2-108(2) (LexisNexis 2006). Under the prior law, the use of simply “L.P.” or “LP” was not acceptable as the identifier of a limited partnership. See § 362.403(1) (LexisNexis 1988).

statute\textsuperscript{67} and not by KyULPA.\textsuperscript{68} While the filing of a Certificate of Limited Partnership under a particular name will preclude the use of that name as the real, assumed, reserved, registered or fictitious name of another business entity in Kentucky, it does not preclude another use of that name by others.\textsuperscript{69} With certain additional requirements, these name requirements apply as well to foreign limited partnerships authorized to transact business in Kentucky under KyULPA.\textsuperscript{70}

ULPA § 109, dealing with name reservations, has been entirely rewritten in KyULPA to conform to practices and procedures already in place in Kentucky.\textsuperscript{71} A foreign limited partnership applying for a certificate of authority to transact business\textsuperscript{72} whose name is not distinguishable or does not meet the other statutory requirements may adopt a fictitious name and under that name qualify to and in fact transact business.\textsuperscript{73}

KyULPA § 110, equivalent in function to KyRUPA § 103, details the place of the partnership agreement and its ability to modify the otherwise applicable default rules of ULPA. It begins by providing that except as limited by KyULPA § 110(b), the partnership agreement\textsuperscript{74} shall govern “relations among the partners and between the partners and the partnership” and that where the

\textsuperscript{66} KY. REV. STAT. ANN. § 362.2-108(1) (LexisNexis 2006). \textit{Cf.} § 362.403(b) (prohibiting, subject to certain exceptions, the inclusion in the name of a limited partnership the name of a limited partner); § 362.050 (repealed 1988) (equivalent provision in Kentucky adoption of the ULPA (1916)).

\textsuperscript{67} KY. REV. STAT. ANN. § 365.015 (LexisNexis 2006). For a discussion of the amendments made to the assumed name statute in 2006 as they relate to limited partnerships and in general, see Maryellen B. Allen & Thomas E. Rutledge, \textit{The 2006 Amendments to the Assumed Name Statute: The Ongoing Task of Modernization and Clarification}, 70 KY. BENCH & BAR 62 (May 2006) [hereinafter Allen & Rutledge, Assumed Name].

\textsuperscript{68} KY. REV. STAT. ANN. § 362.2-108(6) (LexisNexis 2006) (this provision is non-uniform).

\textsuperscript{69} KY. REV. STAT. ANN. § 362.2-108(7) (LexisNexis 2006); \textit{accord} § 271B.4-010(6); § 275.100(6). Intellectual property protections in the form of trademark or service mark registrations may be appropriate. \textit{See also} Allen & Rutledge, Assumed Name, supra note 67, at 63.

\textsuperscript{70} KY. REV. STAT. ANN. § 362.2-108(8) (LexisNexis 2006). Those additional limitations are set forth in § 362.2-905. Foreign limited partnerships remain capable, even after the adoption of KyULPA, of qualifying to transact business under KyRULPA. \textit{See} § 362.497(1).

\textsuperscript{71} KY. REV. STAT. ANN. § 362.2-109 (LexisNexis 2006); \textit{accord} § 362.1-115. This provision substantially is based on § 271B.4-020; § 275.105. However, the provision allowing the cancellation or renewal of a reservation, § 362.2-109(3), does not appear in the KyBCA or the KyLLCA.

\textsuperscript{72} KY. REV. STAT. ANN. § 362.2-902 (LexisNexis 2006).

\textsuperscript{73} KY. REV. STAT. ANN. § 362.2-905 (LexisNexis 2006). A fictitious name will constitute, for purposes of the assumed name act, the real name of the foreign limited partnership. \textit{See} § 362.015(1)(c)(3); \textit{see also} Allen & Rutledge, Assumed Name, supra note 67, at 63. Unlike the KyBCA, which requires delivery to the Secretary of State of a resolution of the board of directors of a foreign corporation seeking to adopt a fictitious name for use in Kentucky, \textit{see} KY. REV. STAT. ANN. § 271B.15-060(1)(b) (LexisNexis 2006), no similar requirement applies to foreign limited partnerships.

\textsuperscript{74} The partnership agreement may be written or oral, may be implied from the facts, or may include a combination of written, oral and implied terms. KY. REV. STAT. ANN. § 362.2-102(17) (LexisNexis 2006).
partnership agreement does not otherwise provide, those relations shall be
governed by KyULPA.75 The provision then goes on to provide the other limits
as to the degree to which the partnership agreement may modify certain of the
otherwise applicable rules of ULPA. This exclusion was made because the
 provision both says too much and says too little. On the first point, the uniform
language states an axiom of contract law - a contract does not impact the rights
of persons who are strangers to the contract.76 As for its deficiencies, it fails to
define who are the “third parties” whose rights are being protected from
restriction. Is the partnership, a legal entity, a party to the partnership
agreement? What of persons who have express notice of the terms of the
partnership agreement and who with that knowledge proceed to do business with
the partnership?77 What of the authorities granted the Secretary of State, the
Attorney General, particular courts granted jurisdiction, and professional
regulatory boards? The failure to incorporate ULPA § 110(b)(13) in KyULPA is
not intended to be a substantive alteration. To the extent that it simply repeats an
axiom of contract law, it is unnecessary. As for its lack of specificity, its
absence does nothing to add to confusion, and principles of otherwise applicable
law, such as contract and agency, will apply. Those limitations on the
partnership agreement are that it may not:

- Vary the power of the limited partnership to sue, be sued or defend
  an action in its own name;78
- Vary the law applicable to the limited partnership;79
- Vary the requirements as to who may sign records on behalf of the
  limited partnership;80
- Vary the information that is required to be maintained under KRS
  141.407 or unreasonably restrict the right to information available to
general limited partners, it being made express, however, that the
partnership agreement may provide a different location for the
maintenance of the records, and reasonable limitations upon the

75. KY. REV. STAT. ANN. § 362.2-110(1) (LexisNexis 2006). As such, in forming a limited
partnership, even if there is no other conceptualization of the terms that will govern these
relationships, there exists a “partnership agreement,” namely to be bound by the rules set forth in
ULPA.

76. See also RUPA § 103 cmt 12 (1997) (“Although stating the obvious, subsection(b)(10)
provides expressly that the rights of a third party under the Act may not be restricted by an
agreement among the partners to which the third party has not agreed.”); Sexton v. Taylor County,
692 S.W.2d 808, 810 (Ky. Ct. App. 1985) (“It is the law in this jurisdiction that no stranger to a
contact may sue for its breach unless the contract was made for his benefit.”).

77. See generally Robert R. Keatinge, The Partnership Agreement and Third Parties:

78. KY. REV. STAT. ANN. § 362.2-110(a) (LexisNexis 2006); see also § 362.2-105.

79. KY. REV. STAT. ANN. § 362.2-110(b)(b) (LexisNexis 2006); see also § 362.2-106.

80. KY. REV. STAT. ANN. § 362.2-110(c) (LexisNexis 2006); see also § 362.2-204.
availability of use of records and appropriate remedies for breach of any reasonable restrictions on that use;

- Eliminate a partner’s duty of loyalty, but the partnership agreement may identify particular activities that do not violate the duty of loyalty, provided that such is not manifestly unreasonable, and may specify the voting threshold for the authorization or ratification, after full disclosure of all material facts, of a transaction that otherwise violate the duty of loyalty;

- Unreasonably reduce the duty of care;

- Eliminate the obligations of good faith and fair dealing, but may prescribe the standards by which the performance of these obligation will be measured provided that those defined standards may not be manifestly unreasonable;

- Vary the power of a general partner to dissociate, except that it may be required that the notice of withdrawal be in a record;

- Vary the right of a court to decree dissolution of the limited partnership in the circumstances described in the statute;

- Vary the requirement that the business of the limited partnership be wound up on the terms defined in the statute;

- Unreasonably restrict the right to bring an action; and

- Restrict the right of a partner to consent to a merger or conversion or restrict the consent of a general partner to an amendment to the certificate of limited partnership deleting the election to be a limited liability limited partnership.

The different formulations for the ULPA § 110(b) limitations, and their individual applications, have material consequences to the degree to which the partnership agreement may affect the applicable rules of ULPA - there is an uneven minimum “floor” to the partnership relationship, namely:

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81. KY. REV. STAT. ANN. § 362.2-110(2)(d) (LexisNexis 2006); see also § 362.2-111; § 362.2-304; § 362.2-407. The reference in this subparagraph to § 141.407 is a drafting mistake. § 141.407 addresses allowable income tax credits. The correct reference should be to § 362.2-111, information that must be maintained by a limited partnership.

82. KY. REV. STAT. ANN. § 362.2-110(2)(e) (LexisNexis 2006); see also § 362.2-408. With respect to the obligation of full disclosure in order for the authorization or ratification of an action otherwise involving a conflict of interest, see RESTATEMENT (THIRD) OF AGENCY § 8.06 (2006).

83. KY. REV. STAT. ANN. § 362.2-110(2)(f) (LexisNexis 2006); see also § 362.2-408(3).

84. KY. REV. STAT. ANN. § 362.2-110(2)(g) (LexisNexis 2006); see also § 362.2-1001; § 362.2-408(4).

85. KY. REV. STAT. ANN. § 362.2-110(2)(h) (LexisNexis 2006); see also § 362.2-604(1).

86. KY. REV. STAT. ANN. § 362.2-110(2)(i) (LexisNexis 2006); see also § 362.2-802.

87. KY. REV. STAT. ANN. § 362.2-110(2)(j) (LexisNexis 2006); see also § 362.2-803.

88. KY. REV. STAT. ANN. § 362.2-110(2)(k) (LexisNexis 2006); see also § 362.2-1001; § 362.2-1005.

89. KY. REV. STAT. ANN. § 362.2-110(2)(l) (LexisNexis 2006); see also § 362.2-1110(1); § 362.2-1110(2).
These various levels of limitation, for example what is the distinction between “unreasonably reduce” and “unreasonably restrict,” are not defined in ULPA, and the commentary provides scant guidance as to what was intended.

What appears in the uniform act as ULPA § 110(b)(13) has not been carried over into KyULPA.90 A new subsection has been added to this section which, in non-uniform terms, provides specific enforcement for statute of fraud provisions set forth in partnership agreements.91

ULPA § 111 contains a detailed listing of records that are to be maintained by the limited partnership.92 The records are to be maintained at the designated office,93 but there is flexibility under a non-uniform addition to ULPA § 110 permitting the records to be maintained elsewhere.94 It is important to note that

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91. See KY. REV. STAT. ANN. § 362.2-110(3) (LexisNexis 2006); accord § 275.015(14); § 362.1-103(3).

92. KY. REV. STAT. ANN. § 362.2-111 (LexisNexis 2006). The limitations upon the degree to which the partnership agreement may depart from KyULPA, § 362.2-110(2), contains, as it relates to information rights, a glaring error: § 362.2-110(2)(d) makes reference to § 141.407 where there clearly should be a reference to § 362.2-111 instead.

93. Defined at KY. REV. STAT. ANN. § 362.2-102(5), the designated office is identified in the certificate of limited partnership. See also ULPA § 114 (2001), KY. REV. STAT. ANN. § 362.2-114 (LexisNexis 2006).

94. KY. REV. STAT. ANN. § 362.2-110(2)(d) (LexisNexis 2006) (“[T]he partnership agreement may provide a different location for the maintenance of the books and records . . . .”).
the partnership is required to maintain these records and that they differ from those required under KyRULPA. Note that these are the records that must be required as dictated by the limited partnership act; other law may require the maintenance of other records.

A partner dealing with the partnership other than as a partner will be on an equal footing with a stranger who is dealing with the partnership. In KyULPA the provision has been modified to expand the various relationships a partner may have with the partnership that fall within the scope of the protections afforded by this provision.

ULPA § 113 provides that a person may be both a general and a limited partner, and provides that in each capacity he or she is governed by the rules applicable to that capacity.

Unlike other business organization forms, which are required to maintain only a single office in Kentucky, that being the registered office, limited partnerships are obligated to maintain both a registered office and a designated office. There is no requirement that either of these offices be that at which the partnership actually maintains its business activities. In contrast, foreign limited partnerships qualify to transact business in Kentucky are required to maintain only a registered office in Kentucky. The registered agent must be an

95. KY. REV. STAT. ANN. § 362.2-110(2)(d) (LexisNexis 2006) (“A limited partnership shall maintain . . . .”) (emphasis added); ULPA § 111. The equivalent provision under KyRULPA is KY. REV. STAT. ANN. § 362.409.
97. For example, a partnership that is required to file a Form 1065 must furnish each partner with a Schedule K-1 that provides the partner’s distributive share of partnership income, gain, loss, deduction, or credit and any additional information that is necessary to enable the partner to determine the correct income tax treatment of a partnership item (Temporary Reg. §§ 1.6031(b)-1T(a)(3)). The Schedule K-1 must be furnished to each partner by the partnership on or before the due date of the partnership return (Form 1065) for the tax year (determined without regard to extensions). The partnership’s tax return is due on or before the 15th day of the fourth month following the end of the partnership’s tax year. For a calendar-year partnership, the partnership’s Form 1065 is due April 15 – the same date by which most individual partners must file their personal tax returns. See also Starting a Business and Keeping Records, Publication 583, Internal Revenue Service (Jan. 2007), available at http://www.irs.gov/pub/irs-pdf/p583.pdf.
98. ULPA § 112 has been modified in KyULPA, KY. REV. STAT. ANN. § 362.2-112 (LexisNexis 2006), as follows:

A partner may lend money to, borrow money from, act as a surety, guarantor or endorser for, guarantee or assume one or more specific obligations of, provide collateral for and transact other business with the limited partnership and has the same rights and obligations with respect to the loan or other transaction as a person that is not a partner.

The non-uniform language is drawn from Delaware, DEL. CODE ANN. tit. 6 § 15-119 (2006); a similar revision has been made in KyRUPA. See KY. REV. STAT. ANN. § 362.1-404(6) (LexisNexis 2006); see also § 362.413.
100. KY. REV. STAT. ANN. § 362.2-113 (LexisNexis 2006).
101. KY. REV. STAT. ANN. § 362.2-114(1) (LexisNexis 2006); see also § 362.407(1); § 362.415(1)(b) (maintenance of registered office and designated office under KyRULPA).
102. KY. REV. STAT. ANN. § 362.2-114(2) (LexisNexis 2006).
individual resident in Kentucky, a domestic corporation, LLC or non-profit corporation, or a foreign corporation, LLC or non-profit corporation authorized to transact business in Kentucky, any of which must have a business address which is identical with the registered office. \(^{103}\) Note that a limited partnership may not serve as the registered agent. The appointment of a registered agent, unless otherwise signing the record making that appointment, must be accepted in writing. \(^{104}\) Non-uniform provisions address the change of the designated office, the registered office or the agent for service of process and the resignation of the registered agent and office. \(^{105}\) The agent for service of process is the agent of the appointing limited partnership or foreign limited partnership for any process, notice or demand required or permitted by law. \(^{106}\) Service upon the registered agent is not the exclusive means by which service may be made, and other legally available options remain viable. \(^{107}\)

Partners in a limited partnership are expressly authorized to act without a meeting and to act by proxy. \(^{108}\) Note that in acting without a meeting there is no requirement of a writing to record any action taken and that there is no requirement of unanimity of the partners participating. \(^{109}\) Such requirements as to formality and procedures for meetings of the partners may be set forth in the partnership agreement. \(^{110}\) However, the appointment of a proxy for a partner must be in a signed record. A partnership agreement may eliminate the requirement that the designation of a proxy be in writing, eliminate voting by proxy or actions other than at a physical meeting, or otherwise alter these procedural rules.

The Secretary of State is authorized to create certain forms and has the authority to make their use mandatory. \(^{111}\) Other forms may be created and made available, but their use cannot be made mandatory. \(^{112}\)

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103. KY. REV. STAT. ANN. § 362.2-114(3) (LexisNexis 2006); accord § 271B.15-070(1)(b); § 275.415(2); § 362.407(1)(b); § 362.1-117(1)(b).
104. KY. REV. STAT. ANN. § 362.2-114(4) (LexisNexis 2006). This provision is non-uniform. Accord § 271B.15-070(2); § 275.415(3); § 362.407(2); § 362.1-117(2).
105. See KY. REV. STAT. §§ 362.1-115; 362.2-116 (LexisNexis 2006); accord § 271B.15-080(1); § 271B.15-090(1)-(3); § 275.420(1); § 275.425(1)-(3).
106. KY. REV. STAT. ANN. § 362.2-117(1) (LexisNexis 2006); accord § 271B.15-100(1); § 275.130(1); § 362.1-120(1).
107. KY. REV. STAT. ANN. § 362.2-117(6) (LexisNexis 2006); accord § 271B.15-100(4); § 275.130(3); § 362.1-120(4); see also KY. R. CIV. P. 4.04(4).
108. KY. REV. STAT. ANN. § 362.2-118 (LexisNexis 2006); accord § 271B.7-220.
109. Cf. KY. REV. STAT. ANN. § 271B.7-040(3) (LexisNexis 2002) (contemplating a writing to record any action taken outside of a meeting); § 271B.8-210 (allowing directors to act by consent only when the action is unanimous); § 271B.7-040(2) (allowing, absent provision in articles of incorporation allowing for shareholders to act by a voting threshold of not less than 80% of the shares issued and outstanding, the shareholders to act only by unanimous written consent).
111. KY. REV. STAT. ANN. § 362.2-119(1)-(2) (LexisNexis 2006). This provision is entirely non-uniform and is based on § 275.050 (LexisNexis 2002); see also § 271B.1-210; § 362.1-105(10)-(11) (LexisNexis 2002). Note that while § 362.2-119 contemplates forms for change of
Filings made under KyULPA are effective upon filing by the Secretary of State, except as there may be a delayed effective date, which the late effective date may be no more than ninety days after the date of delivery to the Secretary of State. While certain limited partnership filings made with the Secretary of State are to be made as well with a county clerk, the document’s effectiveness is not diminished by a failure to do so.

There then follow a series of provisions dealing with filing mechanics, the registration of foreign limited partnerships, certification of documents filed with the Secretary of State, and filing fees. These provisions are all non-uniform from ULPA and are based upon provisions in effect in the KyLLCA.

B. KyULPA Article 2 - Formation, Certificate of Limited Partnership and Other Filings

A limited partnership is formed by filing a certificate of limited partnership with the Secretary of State. The certificate must set forth:

- The name of the limited partnership (which name must comply with Ky. Rev. Stat. Ann. § 362.2-108);
- The street address of the initial designated office and the street address of the initial registered office and the name of the initial registered agent at that office; and
- The name and mailing address of each general partner.

the designated office, registered office, and agent for service of process as being optional, under § 362.2-115(4) their use is mandatory.

112. KY. REV. STAT. ANN. § 362.2-119(3) (LexisNexis 2006).
113. This non-uniform provision is based on KY. REV. STAT. § 271B.1-230(1)-(2); § 275.060; accord § 362.1-110(2).
114. KY. REV. STAT. ANN. § 362.2-120 (LexisNexis 2006). This non-uniform provision is based on KY. REV. STAT. ANN. § 271B.1-230(3) (LexisNexis 2002); § 275.060(3).
115. KY. REV. STAT. ANN. § 362.2-121(LexisNexis 2006); § 362.2-122; § 362.2-123 § 362.2-124; § 362.2-125.
117. KY. REV. STAT. ANN. § 362.2-201(a) (LexisNexis 2006). The effective time and date of the certificate is determined by § 362.2-120.
118. At times KyULPA uses the term “agent for service of process,” e.g., KY. REV. STAT. ANN. §§ 362.2-114(1)-(2) (LexisNexis 2006); §§ 362.2-115(1), (4), while at other times “registered agent,” e.g., §§ 362.2-114(3)-(4); §§ 362.2-115(3)-(4), is used. The terms are interchangeable, and no distinction is meant by the use of one label or the other.
119. KY. REV. STAT. ANN. §§ 362.2-201(1)(a)-(d) (LexisNexis 2006).
The certificate may set forth any other desired information. Also, if the limited partnership desires to be a limited liability limited partnership, it must so declare in the certificate of limited partnership. The certificate of limited partnership must be accompanied by a statement of the initial registered agent consenting to serve as such. The certificate of limited partnership must be signed by each general partner named therein. ULPA contains a provision requiring only substantial compliance with the requirements for the contents of a certificate of limited partnership. In light of the minimal requirements required as to the contents of a certificate of limited partnership, this provision has not been carried forward in KyULPA, and actual compliance with the requirements of the statute will be expected of those forming a limited partnership. The provision goes on to address the relative weight of the certificate of limited partnership versus the partnership agreement. As to third parties who reasonably and to their detriment rely on the filed record, the filed record controls, but as to partners and their transferees, the partnership agreement controls over the public record.

120. KY. REV. STAT. ANN. § 362.2-201(1)(e) (LexisNexis 2006). Note, however, that the additional information does not, by its filing with the Secretary of State, constitute notice to third parties, see § 362.2-103(3), and additional information may not be contained in the Certificate of Limited Partnership with the objective of overriding the limitations upon the partnership agreement set forth in § 362.2-110(2).

121. KY. REV. STAT. ANN. § 362.2-201(2) (LexisNexis 2006). This provision is non-uniform. Under ULPA § 201(1)(d), the certificate of limited partnership was required to state “whether the limited partnership is a limited liability limited partnership.” The movement and wording of this declaration is not intended as a change in the law, but rather to highlight the option of making the election and to clarify that the choice must be made by an affirmative statement. If limited liability limited partnership status is not elected, the liability of the general partners is determined under KY. REV. STAT. ANN. § 362.2-404(1) (LexisNexis 2006). If limited liability limited partnership status is elected, the liability of the general partners is determined under § 362.2-404(3). In the absence of an affirmative statement, the limited partnership will not be a limited liability limited partnership.

122. KY. REV. STAT. ANN. § 362.2-201(5) (LexisNexis 2006). This provision conforms to KY. REV. STAT. ANN. § 271B.5-010(2) (LexisNexis 2002); § 275.025(5); § 361.407(2).

123. KY. REV. STAT. ANN. § 262.2-204(1)(a) (LexisNexis 2006).

124. ULPA § 201(c) (2001) (“If there has been substantial compliance with subsection (a), subject to Section 206(c) a limited partnership is formed when the [Secretary of State] files the certificate of limited partnership.”). Proper payment of the filing fee is a prerequisite to the filing of a certificate of limited partnership or any other filing made with the office of the Secretary of State. KY. REV. STAT. ANN. § 362.2-122(1) (LexisNexis 2006); see also 30 KY. ADMIN. REGS. 1:050(1) (2006) (“Filing fees shall be paid when a document is filed in the Office of the Secretary of State.”). Limited partnerships are statutory creatures that do not exist at common law, and may be formed only by complying with the applicable statutory requirements. See Saulnier v. Fanaras Enters., Inc., 618 A.2d 841, 843 (N.H. 1992); Dominion Nat’l Bank v. Sundowner Joint Venture, 436 A.2d 501, 507-08 (Md. 1981). But see Winter v. Beale, Lynch & Co., 603 N.Y.S.2d 846 (N.Y. App. Div. 1993) (Carro, J., dissenting) (failure to record a limited partnership affects only the rights of the partners as to one another).

125. KY. REV. STAT. ANN. § 362.2-201(4) (LexisNexis 2006). Cf. KY. REV. STAT. ANN. § 271B.2-060(2) (LexisNexis 2002) (bylaws may contain any provision not inconsistent with law or the articles of incorporation).
A certificate of limited partnership may be amended as well as restated, and a certificate must be amended upon:

- The admission of a new general partner;
- The dissociation of a general partner; or
- The appointment of a person to wind up the limited partnership.127

Each general partner is under a personal obligation to see that the information in the certificate of limited partnership is and remains current and accurate.128 Articles of Correction filed with respect to a certificate of limited partnership, while generally relating back to the date of the original filing, do not relate back for purposes of constructive notice of the contents of the certificate as corrected or as to persons who have relied upon the information set forth in the certificate prior to its correction and who would be adversely affected by the correction.129

The notices filed upon the dissolution of a KyULPA limited partnership differ from those existing under existing corporate and LLC law. Initially, at the time of dissolution, the Certificate of Limited Partnership may need to be amended to make of record that a person other than a general partner has been appointed to oversee the winding up of the limited partnership’s activities.130 At the end of the winding up process, there is then delivered a Statement of Cancellation setting forth the name of the limited partnership, the date of the filing of its initial Certificate of Limited Partnership, and such other information as is determined appropriate.131 This process differs from that under the corporate and LLC acts under which Articles of Dissolution are filed at the beginning of the winding up process, and there is no public filing indicating that the winding up has been completed.132 This filing must be signed by the person so named.133

The provisions dealing with who must sign various filings made by or on behalf of the limited partnership are addressed in an integrated provision. The initial Certificate of Limited Partnership must be signed by each general partner, while any amendment designating an additional general partner must be signed by that new general partner.134 An amendment to a Certificate of Limited Partnership by which the partnership either elects or terminates an election to be

128. KY. REV. STAT. ANN. § 362.2-202(3) (LexisNexis 2006). As this provision is not listed in ULPA § 110(b), presumably it could be restricted or eliminated in the partnership agreement. However, this is at best a rather questionable reading.
130. KY. REV. STAT. ANN. § 362.2-202(2)(c) (LexisNexis 2006).
131. KY. REV. STAT. ANN. § 362.2-203 (LexisNexis 2006).
133. KY. REV. STAT. ANN. § 362.2-204(1)(d) (LexisNexis 2006).
134. KY. REV. STAT. ANN. §§ 362.2-204(1)(a), (c) (LexisNexis 2006).
a limited liability limited partnership must be signed by all general partners.\textsuperscript{135} Certain other amendments need be signed only by one general partner.\textsuperscript{136} Except where a general partner has dissociated by reason of death or incompetency, or there has been filed a Statement of Dissociation with respect to that general partner,\textsuperscript{137} the Amendment to the Certificate of Limited Partnership recording the dissociation of that general partner needs to be as well signed by that dissociated general partner.\textsuperscript{138} Filings made by a foreign limited partnership must be signed by at least one general partner.\textsuperscript{139} Legal action to compel the execution of the document that needs to be signed may be brought in the circuit court in which the limited partnership maintains its registered office, and the court may order either that the responsible person execute the record or that the Secretary of State accept the document without signature.\textsuperscript{140} The statute defines to whom the Secretary of State should return copies of filed documents.\textsuperscript{141} A non-uniform provision addresses the filing of corrections to documents already filed.\textsuperscript{142} There may exist personal liability with respect to filed documents containing information that was incorrect at the time of filing or that became incorrect with the passage of time and for which corrective filings have not been made.\textsuperscript{143}

A Certificate of Existence for a domestic limited partnership, or a Certificate of Authorization for a foreign limited partnership, may be issued by the Secretary of State. In contrast with the declarations made in Certificates of Existence/Qualification under the KyBCA or the KyLLCA, the Secretary of State certifies that the last due annual report has been “filed” as contrasted with having been “delivered.”\textsuperscript{144}

In a change from the practice under KyRULPA, limited partnerships governed by KyULPA and foreign limited partnerships qualified to transact business in Kentucky under KyULPA are required to file an annual report with the Secretary of State.\textsuperscript{145} This requirement will apply as well to each limited partnership formed under KyRULPA or predecessor limited partnership law that

by voluntary election becomes subject to KyULPA. The annual report will require each limited partnership to set forth:

- Its name and jurisdiction of organization;
- For domestic limited partnerships, the street address of the designated office;
- For foreign limited partnerships, the street address of its principal office; and
- The registered office and the name of the registered agent at that office.146

A change in the designated or registered office, or in the registered agent, will be accomplished by a separate filing and not by means of amending the annual report.147 Changes in the general partners need to be disclosed by an amendment to the certificate of limited partnership and are not made of record in the annual report.148

A limited partnership that does not file its annual report within sixty days of the due date149 is subject to administrative dissolution.150 This non-uniform provision conforms to existing law under the KyBCA and KyLLCA, as well as law adopted for KyRUPA limited liability partnerships.151 It should be noted that upon administrative dissolution, the limited partnership “continues in existence but may not carry on any business except that necessary to wind up and liquidate its business and affairs.”152 A limited partnership that has been administratively dissolved may apply for reinstatement, which reinstatement, if granted, will relate back to the original administrative dissolution.153 A refusal by the Secretary of State to reinstate a limited partnership may be appealed.154

The revocation of a certificate of authority granted a foreign limited

146. KY. REV. STAT. ANN. § 362.2-210(1)(a)-(c) (LexisNexis 2006). The filing fee for the annual report is $15.00, § 362.2-122(1)(t); accord KY. REV. STAT. ANN. § 271B.1-220(s) (LexisNexis 2002); § 275.055(u).
147. KY. REV. STAT. ANN. § 362.2-115(4) (LexisNexis 2006); see also § 362.2-210(4); accord KY. REV. STAT. ANN. § 275.040 (LexisNexis 2002); § 275.120.
148. KY. REV. STAT. ANN. § 362.2-202(2) (LexisNexis 2006).
149. See KY. REV. STAT. ANN. § 362.2-210(3) (LexisNexis 2006) (annual report is due by June 30 of the calendar year after which the limited partnership is formed and by June 30 of each year thereafter). For these purposes, the election by an existing KyRULPA or pre-KyRULPA partnership to be governed by KyULPA will constitute its date of formation.
150. KY. REV. STAT. ANN. § 362.2-809(1)(a) (LexisNexis 2006).
152. KY. REV. STAT. ANN. § 362.2-809(4) (LexisNexis 2006); accord KY. REV. STAT. ANN. § 271B.14-210(3) (LexisNexis 2002 & Supp. 2006); § 275.300(2).
154. KY. REV. STAT. ANN. § 362.2-811(2) (LexisNexis 2006); accord KY. REV. STAT. ANN. §§ 271B.14-230 (LexisNexis 2002); § 275.450.
partnership results in the revocation of its authority to transact business in Kentucky. The revocation of the certificate of authority may be appealed. Absent a successful appeal, a revocation is not subject to cure. Rather, a new application for certificate of authority must be filed, and for the period between the revocation of the Certificate of Authority and the issuance of a new Certificate of Authority, the foreign limited partnership was not qualified to transact business in Kentucky.

C. KyULPA Article 3 - Limited Partners

A person becomes a limited partner (i) as provided in the partnership agreement, (ii) pursuant to a merger or conversion, or (iii) with the approval of all partners (both limited and general). This is the same rule that applies under KyRULPA. Not being referenced in ULPA § 110(b), the partnership agreement may provide other rules for admission of a limited partner, a fact contemplated by KRS § 362.2-301(1).

A limited partner, in that capacity, has no authority to serve as an agent of and bind the limited partnership. However, this provision does not preclude one who is a limited partner from acting as an agent of the limited partnership. Such authority may be afforded them in the partnership agreement or by a specific delegation of authority by the limited partnership. A general partner who is as well a limited partner has the agency authority of a general partner.

Limited partners, as such, are afforded limited liability, and are not liable, including by reason of “indemnification, contribution, assessment or otherwise,”

155. In addition to failure to file a required annual report, a foreign limited partnership may have its certificate of authority revoked if (i) it is without an registered office or agent for sixty days, (ii) it fails to advise the Secretary of State of certain changes in the registered office or agent, or (iii) the Secretary of State receives notice of the disappearance of the limited partnership by reason of a merger. See KY. REV. STAT. ANN. §§ 362.2-906(1)-(4) (LexisNexis 2006).

156. KY. REV. STAT. ANN. § 362.2-907(3) (LexisNexis 2006); accord KY. REV. STAT. ANN. § 271B.15-310(3) (LexisNexis 2002); § 275.445(3).

157. KY. REV. STAT. ANN. § 362.2-907(6)-(8) (LexisNexis 2006); accord KY. REV. STAT. ANN. § 271B.15-310 (LexisNexis 2002); § 275.450.

158. KY. REV. STAT. ANN. §§ 362.2-301(1)-(3) (LexisNexis 2006).

159. See KY. REV. STAT. ANN. § 362.2-301(1)-(3) (LexisNexis 2002); § 362.531.

160. KY. REV. STAT. ANN. § 362.2-302 (LexisNexis 2006). As noted in the Official Comment to ULPA § 302:

In this respect a limited partner is analogous to a shareholder in a corporation; status as owner provides neither the right to manage nor a reasonable appearance of that right.

See also KY. REV. STAT. ANN. § 275.135(2) (LexisNexis 2002). A limited partner who without authority acts to bind the limited partnership will have violated the warranty of authority and is exposed to personal liability on the obligation created. See RESTATEMENT (THIRD) OF AGENCY § 6.10 (2006); see also RESTATEMENT (SECOND) OF AGENCY §§ 140, 219 (1958).


162. KY. REV. STAT. ANN. § 362.2-113 (LexisNexis 2006); see also ULPA § 302 cmt. (2001).
for the debts and obligations of the limited partnership.\textsuperscript{163} This limited liability
is not lost if the limited partner “participates in the management and control of
the limited partnership.”\textsuperscript{164} This is a material departure from the prior law under
which a limited partner who participated in the management and control of the
limited partnership did so at the risk of waiving the limited liability otherwise
afforded to them.\textsuperscript{165} As is always the case when considering a business entity
that affords its members limited liability it is important to keep in mind the outer
limits of that protection.\textsuperscript{166}

A limited partner, upon ten days notice in a record, may inspect and copy at
the designated office of the limited partnership the information required to be
maintained.\textsuperscript{167} The limited partner is not required to set forth any purpose for
seeking this information.\textsuperscript{168} Assuming a series of conditions are satisfied, a
limited partner is as well entitled to receive from the limited partnership “true
and full information regarding the state of the activities and financial condition.
. . and other information regarding the activities of the limited partnership.”\textsuperscript{169}
Those conditions are:

\textsuperscript{163} KY. REV. STAT. ANN. § 362.2-303 (LexisNexis 2006). The terms “indemnification” and
“assessment” are not uniform, and were added to KyULPA to conform to KY. REV. STAT. ANN.
§ 362.220(2) (LexisNexis 2002); see also KY. REV. STAT. ANN. § 326.1-306(3) (LexisNexis 2006).
\textsuperscript{164} KY. REV. STAT. ANN. § 362.2-303 (LexisNexis 2006).
\textsuperscript{165} See KY. REV. STAT. ANN. § 362.437 (LexisNexis 2002). Under traditional limited
partnership law, limited partners were shielded from general liability for the debts and obligations
for the limited partnership only so long as they did not take part in the active management of
partnership. See, e.g., KY. REV. STAT. ANN. § 362.437(1) (LexisNexis 2002); see also §
362.437(4). Partnership law, over the course of its development from the original 1916 Uniform
Act through RULPA (1985), has increased the scope of activities in which limited partnership may
engage without foregoing limited liability. See J. WILLIAM CALLISON & MAUREEN A. SULLIVAN,
PARTNERSHIP LAW AND PRACTICE: GENERAL AND LIMITED PARTNERSHIPS § 23:1 (2005). Still, the
application of these numerous safe harbor provisions has in many particular cases been a question
of fact, and therefore limited broad reliance thereon. See id. at § 23:4; compare Alzado v. Blinder,
Robinson & Co., 752 P. 2d 544, 552-53 (Colo. 1988) (control of expense distribution formula of
partnership did not give limited partner control such that it could be liable to partnership creditors),
with Brooke v. M.T. Hood Meadows Or., Ltd., 725 P.2d 925, 929 (Or. Cl. App. 1986) (control by
limited partner over distribution of limited partnership’s profits constituted control), aff’d on reh’g,
732 P.2d 36 (Or. Cl. App. 1986). See generally, Annotation, Liability of Limited Partner Arising
from Taking Part in Control of Business under Uniform Limited Partnership Act, 79 A.L.R. 4th
427 (1990); see also ULPA § 303 cmt. (2001). With respect to the control rule and criticism
thereof, see generally Joseph Basile, Jr., Limited Liability for Limited Partners: An Argument for
the Abolition of the Control Rule, 38 VAND. L. REV. 1199 (1985); George W. Coleman & David A.
Weatherbie, Special Problems in Limited Partnership Planning, 30 SW. L.J. 887, 897-909 (1976);
Alan Feld, Comment, The “Control” Test for Limited Partnerships, 82 HARV. L. REV. 1471

\textsuperscript{166} See generally Rutledge, Holy Grail, supra note 58.
\textsuperscript{167} KY. REV. STAT. ANN. § 362.2-304 (LexisNexis 2006); see also § 362.2-111 (LexisNexis 2006).
\textsuperscript{168} KY. REV. STAT. ANN. § 362.2-304(1) (LexisNexis 2006); accord KY. REV. STAT. ANN.
§ 271B.16-020(1) (LexisNexis 2002); § 275.185(2).
\textsuperscript{169} KY. REV. STAT. ANN. § 362.2-304 (LexisNexis 2006).
• The disclosure will be during regular business hours and at a
reasonable location specified by the limited partnership;
• The information must be sought “for a purpose reasonably related to
the partner’s interest as a limited partner”;[12]
• The demand for the information must be in a record received by the
limited partnership;
• The demand must describe “with reasonable particularity the
information sought and the purpose for seeking the information”;[13]
• The information sought must be “directly connected” to the limited
partner’s purpose; and
• The request must be “just and reasonable.”[14]

The “just and reasonable” requirement modifies both the limited partner’s
request as well as the information provided in response thereto.[15] Upon receipt
of a request for information, the limited partnership is obligated to respond,
stating either what information it will provide and when, or its reason for
deploying to provide any of the information sought.[16]

A dissociated limited partner has continuing information rights, but only for
information pertaining to the period they were a limited partner.[17] The
information must be sought utilizing the same procedures as those applicable to
an incumbent limited partner, with the added obligation that they act in good
faith.[18]

A limited partnership has the right to impose reasonable restrictions upon the
use of information provided to limited partners, and should there be a question as
to whether a proposed limitation is reasonable, the limited partnership will bear
the burden of proof of demonstrating that they are so.[19] Should the incumbent
or former limited partner seek to inspect information through an agent, that agent
is equally bound by those limitations on use.[20] The limited partnership has the
right to recover from either a current or a former limited partner for the
information requested.

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170. KY. REV. STAT. ANN. § 362.2-304(2) (LexisNexis 2006); accord KY. REV. STAT. ANN.
§ 271B.16-020(3) (LexisNexis 2002).
171. Telephone conference between Thomas E. Rutledge and Daniel J. Kleinberger, ULPA
Reporter (January 30, 2005).
172. KY. REV. STAT. ANN. § 362.2-304(3) (LexisNexis 2006). KyULPA does not contain a
provision equivalent to KY. REV. STAT. § 271B.16-040 for a court ordered inspection of records.
Still, a court’s equitable powers will undoubtedly reach the inspection of documents of a domestic
limited partnership.
175. KY. REV. STAT. ANN. § 362.2-304(7) (LexisNexis 2006). This provision applies to
limitations imposed unilaterally by the limited partnership ex post the limited partner’s request for
information. If limitations on the use of information are imposed by the partnership agreement, the
limited partnership should not be subject to a burden of proving reasonableness.
176. KY. REV. STAT. ANN. § 362.2-304(10) (LexisNexis 2006).
“reasonable costs of copying, limited to the costs of labor and material” 177 incurred in responding to the request.

While the estate of a deceased limited partner has limited information rights, 178 the transferee of a limited partner does not have information rights. 179

In addition to these obligations to respond to requests for information, there is an affirmative obligation to provide information to limited partners whenever a limited partner is:

- to give or withhold consent on a matter, before the consent is given or withheld, the limited partnership shall, without demand, provide the limited partner with all information that the limited partnership knows and is material to the limited partner’s decision. 180

The actions upon which a limited partner may be asked to give or withhold consent, unless modified by the partnership agreement, are:

- Admission of a limited partner; 181
- Admission of a general partner; 182
- Amendment of the partnership agreement; 183
- The decision to amend the certificate of limited partnership so as to obtain or relinquish LLP status; 184
- The disposition of all or substantially all of the limited partnership’s property outside the ordinary course; 185
- The compromise of a partner’s obligation to make a contribution or return an improper distribution; 186
- Expulsion of a limited partner by consent of the other partners; 187
- Expulsion of a general partner by consent of the other partners; 188
- Redemption of a transferable interest subject to charging order using limited partnership property; 189
- Causing dissolution by consent; 190
- Causing dissolution by consent following the dissociation of a general partner, when at least one general partner remains; 191

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177. KY. REV. STAT. ANN. § 362.2-304(8) (LexisNexis 2006); accord KY. REV. STAT. ANN. § 271B.16-030(3) (LexisNexis 2002); § 275.185(2).
178. KY. REV. STAT. ANN. § 362.2-704 (LexisNexis 2006).
180. KY. REV. STAT. ANN. § 362.2-304(9) (LexisNexis 2006).
181. KY. REV. STAT. ANN. § 362.2-301(3) (LexisNexis 2006).
182. KY. REV. STAT. ANN. § 362.2-401 (LexisNexis 2006).
188. KY. REV. STAT. ANN. § 362.2-502(1) (LexisNexis 2006).
190. KY. REV. STAT. ANN. § 362.2-703(3)(c) (LexisNexis 2006).
191. KY. REV. STAT. ANN. § 362.2-801(2) (LexisNexis 2006).
• Avoiding dissolution and appointing a successor general partner, following the dissociation of the sole general partner;\textsuperscript{192}
• Appointing a person to wind up the limited partnership when there is no general partner;\textsuperscript{193}
• Approving, amending or abandoning a plan of conversion;\textsuperscript{194} and
• Approving, amending or abandoning a plan of merger.\textsuperscript{195}

The affirmative disclosure obligation prior to soliciting the views of the limited partners with respect to any of these actions applies as well to as any other actions upon which, pursuant to the partnership agreement, the limited partners are to consent. As noted in the Official Comment to ULPA § 304, “The duty stated in this subsection is at the core of the duties owed the limited partners by a limited partnership and its general partners.”

RULPA did not expressly address the degree to which the fiduciary duties applicable to partners would apply to limited partners.\textsuperscript{196} ULPA addresses this oversight by clearly providing what obligations do attach to the limited partnership status. Initially, it is provided that, “A limited partner does not have any fiduciary duty to the limited partnership or to any other partner solely by reason of being a limited partner.”\textsuperscript{197} With this provision, it is clear that limited partners as such do not owe fiduciary duties, a rule that accords with the lack of control and lack of agency authority that limited partners have in the limited partnership.\textsuperscript{198} Note, however, that if the Agreement of Limited Partnership allocates managerial authority to a limited partner, they will have obligations, which may be fiduciary in nature, but in that situation the obligations are undertaken pursuant to contract and not by reason of status.\textsuperscript{199} Limited partners are obligated to act consistent with an obligation of good faith and fair

\textsuperscript{191} KY. REV. STAT. ANN. § 362.2-801(3)(a) (LexisNexis 2006).
\textsuperscript{192} KY. REV. STAT. ANN. § 362.2-801(3)(b) (LexisNexis 2006).
\textsuperscript{193} KY. REV. STAT. ANN. § 362.2-803(3) (LexisNexis 2006).
\textsuperscript{194} KY. REV. STAT. ANN. § 362.2-1103(1) (LexisNexis 2006); § 362.2-1103(2)(b).
\textsuperscript{195} KY. REV. STAT. ANN. §§ 362.2-1107(1)-(4) (LexisNexis 2006).
\textsuperscript{196} Under KY. REV. STAT. ANN. § 362.523 (LexisNexis 2006), the fiduciary duties set forth at § 362.250 and at common law are applied to the general partners of a limited partnership, while § 362.447 further provides that a partner in a general partnership has the same rights and powers, is subject to the same restrictions, and shall have the same liabilities, as is a partner in a partnership without limited partners. Under RULPA, limited partners were generally not held to have fiduciary duties, see, e.g., In re Villa W. Associates, 146 F.3d 798, 807 (10th Cir. 1998); Cantor Fitzgerald, L.P. v. Cantor, No. 16297, 2000 WL 307370, at *20 (Del. Ch. Mar. 13, 2000) ; Bond Purchase, L.L.C. v. Patriot Tax Credit Props., L.P., 746 A.2d 842, 864 (Del. Ch. 1999), notwithstanding the linkage of limited partnership law to general partnership law and the fiduciary duties obligations of both UPA § 21, KY. REV. STAT. ANN. § 362.250(1) (LexisNexis 2002), and at common law.
\textsuperscript{197} KY. REV. STAT. ANN. § 362.2-305(1) (LexisNexis 2006).
\textsuperscript{198} See ULPA § 305 cmt. (2001).
\textsuperscript{199} Id.; see also KE Prop. Mgmt. Inc. v. 275 Madison Mgmt. Corp., No. 12683, 1993 WL 285900, at *10 (Del. Ch. Jul. 21, 1993) (limited partner to whom partnership agreement delegated authority affecting management may be subject to fiduciary obligations).
dealing.\textsuperscript{200} As, in this formulation, good faith and fair dealing are contractual obligations, and are not fiduciary in nature, they do not mandate self-abnegation or preclude a limited partner from, in the exercise of the rights and discharge of their duties, acting in their own self-interest.\textsuperscript{201}

ULPA § 306 addresses the situation in which one becomes a general partner when he intended to be a limited partner and what steps they must be taken to avoid liability as a general partner.\textsuperscript{202} A person finding himself in this situation is obligated to either cause the Certificate of Limited Partnership to be amended/corrected to state that they are not a general partner, or to withdraw from future participation in the venture.\textsuperscript{203} In the event he chooses to withdraw, there exists no obligation to return previously received distributions; the focus is upon the avoidance of future distributions.\textsuperscript{204} A person who endeavors to have the Certificate of Limited Partnership amended/corrected, but who is not able to do so, is able to withdraw from future participation in the venture even if that withdrawal would otherwise constitute a violation of the partnership agreement.\textsuperscript{205} Still, that person, as a general partner, has personal liability for the debts and obligations of the limited partnership to any third party who believed in good faith that the person was a general partner.\textsuperscript{206} While the statute requires that third party to have believed that person to have been a general partner, there is no statutory requirement that he otherwise relied upon that person in order that the liability be imposed.

D. KyULPA Article 4 - General Partners

A person becomes a general partner (i) as provided in the partnership agreement, (ii) upon admission as a replacement general partner after the dissociation of the last incumbent general partner, (iii) pursuant to a merger or conversion, or (iv) with the approval of all of the partners.\textsuperscript{207} Note that the filing

\begin{itemize}
\item \textsuperscript{200} KY. REV. STAT. ANN. § 362.2-305(2) (LexisNexis 2006).
\item \textsuperscript{201} KY. REV. STAT. ANN. § 362.2-305(3) (LexisNexis 2006); see also ULPA § 305 cmt. (2001).
\item \textsuperscript{202} KY. REV. STAT. ANN. § 362.2-306 (LexisNexis 2006); accord KY. REV. STAT. ANN. § 362.439 (LexisNexis 2002).
\item \textsuperscript{203} What constitutes a prompt renunciation of future participation in the activities of the limited partnership is not addressed in the statute. See Ritzau v. Warm Springs W., 589 F.2d 1370, 1376-77 (9th Cir. 1979); Vidriksen v. Grover, 363 F.2d 372, 373 (9th Cir. 1966); Voudouris v. Walter E. Heller & Co., 560 S.W.2d 202, 208 (Tex. App. 1997).
\item \textsuperscript{204} ULPA § 306 cmt. (2001).
\item \textsuperscript{205} KY. REV. STAT. ANN. § 362.2-306(3) (LexisNexis 2006).
\item \textsuperscript{206} KY. REV. STAT. ANN. § 362.2-306(2) (LexisNexis 2006); see also KY. REV. STAT. ANN. § 362.2-606(2)(b) (LexisNexis 2002).
\item \textsuperscript{207} KY. REV. STAT. ANN. § 362.2-401 (LexisNexis 2006). The admission of a general partner subsequent to the dissociation of the last general partner is addressed in § 362.2-801. The consent of “all of the partners” addresses both the general and the limited partners, and may be modified in the partnership agreement. As this provision is not addressed in ULPA § 110(b)/KY. REV. STAT. ANN. § 362.2-110(1) (LexisNexis 2006), the “as provided by the partnership agreement” is
or amendment of the Certificate of Limited Partnership is not a pre-condition to one becoming a general partner.\footnote{208} Although the Certificate of Limited Partnership is required to name each general partner, general partner status is not dependent upon being so named in the certificate. Rather, upon admission as a general partner, that role is held, and there exists an obligation to amend the Certificate of Limited Partnership to so record the holding of that position. While each person named in the Certificate of Limited Partnership is as to third parties a general partner, the fact that one is not so listed in the Certificate of Limited Partnership is not conclusive that they are not a general partner.\footnote{209}

Each general partner, by virtue of that status, is an agent of the limited partnership for the purpose of its activities.\footnote{210} A limited partnership is bound by the acts of a general partner, including the signing of a record in the name of the partnership “for apparently carrying on in the ordinary course the limited partnership’s activities or activities of the kind carried on by the limited partnership.”\footnote{211} The exception to this rule is when (i) the general partner did not have the authority to act and (ii) the third party “knew, had received a notification, or had notice” that the general partner lacked authority to bind the limited partnership.\footnote{212} A private ordering, such as in the partnership agreement,
limiting the general partner’s agency authority does not preclude a partner from binding the partnership in violation of the limitation. A general partner violating the private ordering will be subject to the partnership’s claim for damages.

A general partner cannot bind the limited partnership by an action “which is not apparently for carrying on in the ordinary course the limited partnership’s activities or activities of the kind carried on by the limited partnership” unless the general partner is so authorized to act by all of the partners.213

The limited partnership is liable for the consequences of the actions of a general partner who (i) is “acting in the ordinary course of activities of the limited partnership” or (ii) is acting “with the authority of the limited partnership.”214 Further, if a general partner acting in either capacity receives or causes the limited partnership to receive the money or property of one who is not a partner, and that money or property is then misapplied by a (not necessarily the same) general partner, the limited partnership is liable to that third party for the loss.215 These provisions state generally applicable rules of agency, namely that the principal (i.e., the limited partnership) is liable for the actions of its agent (i.e., the general partner) when the agent is acting in the course of the activities for which the principal has designated the agent to act.216

The general partners are jointly and severally liable for all liabilities of the limited partnership unless otherwise agreed by the claimant or provided by law.217 However, a general partner is not personally liable for an obligation of the limited partnership incurred before that person’s admission as a general partner.218 The rule of joint and several liability is not applicable, however, if the issue arises when the limited partnership has elected to be a limited liability limited partnership. In that situation:

An obligation of a limited partnership incurred while the limited partnership is a limited liability limited partnership, whether arising in contract, tort, or otherwise, is solely the obligation of the limited partnership. A general partner is not personally liable, directly or indirectly, by way of indemnification, contribution, assessment, or


216. See Restatement (Third) of Agency § 6.01 (2006); Restatement (Second) of Agency §§ 140, 219 (1958).

217. KyULPA did not contain a rule regarding the liability of the general partners for the debts and obligations of the general partnership. Rather, the liability was determined by reference to KyUPA. See Ky. Rev. Stat. Ann. § 362.523 (LexisNexis 2006); § 362.220.

otherwise, for such an obligation solely by reason of being or acting as a general partner.\(^{219}\)

This rule applies once the LLLP election is made.\(^{220}\) If the partnership agreement is in effect before the LLLP election contained indemnification, contribution, assessment or other obligations inconsistent with limited liability, those provisions are ineffective\(^{221}\) unless again adopted contemporaneous with or subsequent to the election to become an LLLP.\(^{222}\)

KyULPA does not contain a provision similar to those that appear in the KyBCA and the KyLLCA providing that those acting on behalf of an entity before its organization are personally liable on all debts and obligations undertaken.\(^{223}\) However, as this rule repeats generally applicable agency law, its absence does not indicate a different result.\(^{224}\)

The question may be asked as to why the LLLP option was added to ULPA, and it may be asked as well why it was made an elective status rather than a default rule. As to the first question, the creation of the LLLP is parallel with the development of the LLP under the RUPA.\(^{225}\) Certain states, prior to ULPA, permitted limited partnerships to elect limited liability partnership status,\(^{226}\) and

\(^{219}\) KY. REV. STAT. ANN. § 362.2-404(3) (LexisNexis 2006). “Indemnification” and “assessment” are not uniform and conform to § 362.1-306(3) itself adopting the terms from § 362.220(3). § 138.183 was amended to address the general partners in a limited liability limited partnership, imposing upon them, and in parallel with the managers of an LLC and the partners in an LLC, liability for the taxes imposed under §§ 138.130-.205. Similar revisions were made in § 138.440 with respect to those taxes imposed by §§ 138.210-.446 and in § 139.185 § 142.404 was amended to include as responsible persons for those taxes imposed under § 142.400 general partners in a limited liability limited partnership, and as well to address the dissolution or withdrawal of a limited liability company, limited liability partnership, or limited liability limited partnership.

\(^{220}\) The issue of whether a claim arose before or after an election to be an LLLP is not addressed in the ULPA and is left to other law. Note that the election to become a limited liability limited partnership will not protect the general partners from liability on claims that arose prior to the time of filing of the LLLP election in the certificate of limited partnership. See also supra note 218 and accompanying text.

\(^{221}\) KY. REV. STAT. ANN. § 362.2-404(3) (LexisNexis 2006).

\(^{222}\) Accord KY. REV. STAT. ANN. § 362.1-306(3) (LexisNexis 2006).

\(^{223}\) See KY. REV. STAT. ANN. § 271B.2-040; § 275.095 (LexisNexis 2006).


\(^{225}\) Still, “[a] foolish consistency is the hobgoblin of little minds.” Ralph Waldo Emerson, Self-Reliance, Essays: First Series (1841).

the potential for doing so existed under most UPA-RULPA statutory schemes.\textsuperscript{227} Furthermore, notwithstanding certain tax complexities that arose prior to the adoption of the current tax classification regulations,\textsuperscript{228} it has been the common practice to organize a corporation, and more recently a limited liability company, to serve as the general partner of a limited partnership.\textsuperscript{229} By doing so, as to third parties, the general partner was a limited liability entity, and the creditors, after exhausting the assets of the limited partnership, could look no further than the assets of that corporation/limited liability company. Those actually promoting/controlling the limited partnership would typically have owned the business entity that was the general partner, and through it enjoyed the economic benefits of control, without placing their personal assets, beyond those contributed to the general partner, at risk. For all intents and purposes, by satisfying the transactional costs of organizing and maintaining a special purpose corporation or limited liability company, making attendant tax filings and at times bearing a quite de minimus increase in the effective overall tax rate, limited liability was achieved. With the LLLP, complete limited liability can be achieved within the limited partnership, alleviating the need to create and maintain the special purpose corporation/limited liability company. Essentially, it was a matter of efficiency. At one point in the drafting process, ULPA would have provided a default rule of limited liability for all partners, whether they be general or limited. This option, however, was rejected for a variety of reasons including its degree of departure from what was commonly understood as the limited partnership, concerns regarding enactability among the states, and issues with respect to altering the rule for pre-ULPA limited partnerships that would at some point become subject to its rules either by affirmative election or a drag-in effective date. As a concession to these concerns, LLLP status was made elective and not mandatory.\textsuperscript{230}

A general partner in a limited partnership that is not a LLLP or was not at the time the claim at issue arose may be joined in an action against a limited

\textsuperscript{227} Whether in any instance it was possible depended upon the state’s formulation of the largely non-uniform LLP language adopted as an amendment to the state adoption of the UPA and whether a limited partnership was a “partnership” thereunder that could elect LLP status.

\textsuperscript{228} See Thomas E. Rutledge & Thomas Earl Geu, \textit{A Practical Guide to the Limited Liability Limited Partnerships} § 2.2, in \textit{1 STATE LIMITED PARTNERSHIP LAWS} (Elizabeth S. Miller et al. eds., Aspen 2007).

\textsuperscript{229} For a history of the use of a corporate general partner in a limited partnership, see Robert W. Hamilton, \textit{Corporate General Partners of Limited Partnerships}, 1 \textit{J. SMALL & EMERGING BUS. L.} 73, 77-86 (1997).

\textsuperscript{230} See Kleinberger, \textit{User’s Guide}, supra note 7, at 621.
partnership or named in a separate action. A judgment against the limited partnership is not a judgment against any general partner, and no judgment against the limited partnership may be satisfied from assets of a general partner unless there is as well a judgment against the general partner. A suit and a judgment against only the limited partnership will involve fewer costs to both the plaintiff and what would otherwise be the defendants and may be entirely appropriate where the claim can be satisfied from the limited partnership’s assets. Where the plaintiff is not comfortable that limited partnership assets will be sufficient, some or all of the general partners will need to be made defendants.

Still, even where there is a judgment against a limited partner for an obligation of the limited partnership, that judgment may not be satisfied out of the general partner’s personal property unless:

- A writ of execution against the limited partnership has been returned unsatisfied;
- The limited partnership is a debtor in bankruptcy;
- The general partner has agreed that the creditor need not exhaust the assets of the limited partnership;
- A court permits the judgment creditor to move first against the general partner because the assets of the limited partnership will clearly be insufficient to satisfy the judgment, the exhaustion of limited partnership assets will be excessively burdensome, or it is equitable; or
- The general partner is as well liable by law or contract independent of the existence of the limited partnership.

ULPA § 406 is a central provision of the act, detailing certain rights of the general partners, detailing other rights of all partners, and reciting certain rights the general partners have against the limited partnership.

Initially, each general partner has an equal (per capita) right to participate in the management and conduct of the limited partnership’s activities. Except where the consent of the limited partners is required by either the ULPA or by the partnership agreement, a decision may be made by either the single general partner or by a decision of the remaining general partners.

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231. KY. REV. STAT. ANN. § 362.2-405(1) (LexisNexis 2006); accord § 362.1-307(3). Naming the general partner of a LLLP when the sole basis of asserting liability against them is the status as a general partner may subject plaintiff’s counsel to sanctions under Rule 11. See Page v. Roscoe, LLC, 497 S.E.2d 422 (N.C. Ct. App. 1998) (involving a suit in which members of LLC were named as parties notwithstanding statute providing that members are not proper parties to a suit against LLC). Naming an LLLP general partner based upon some other basis of liability, such as the personal guarantee of a debt or having been the actor that caused a tort, is not status based.

232. KY. REV. STAT. ANN. § 362.2-405(2) (LexisNexis 2006).

233. KY. REV. STAT. ANN. § 362.2-405(3) (LexisNexis 2006); accord § 362.1-307(4).

234. KY. REV. STAT. ANN. § 362.2-406 (LexisNexis 2006); accord § 362.1-404.

235. KY. REV. STAT. ANN. § 362.2-406(1) (LexisNexis 2006); accord § 362.1-401(6).
partner or, where there is more than one general partner, by a majority of the general partners. There is flexibility to alter this default management structure. For example, the partnership agreement may invest in the limited partners the right to participate in management decisions that would otherwise rest within the exclusive province of the general partners. Another option is to provide for differentiations among the general partners in either the partnership agreement or in a private agreement amongst themselves as to who has particular authority over particular aspects of operations and activities. The act does not specifically reference the ability of a general partner to employ an agent or to otherwise delegate managerial authority over the limited partnership, although the commentary indicates that such is permitted. While under the prior law a delegation would not relieve the general partner of fiduciary obligations with respect to the performance (or not) of that agent, the commentary to the ULPA indicates that the inquiry would be into the care employed in selecting the agent, the scope of the delegation and the supervision thereafter given to the agent’s performance.

Subject to the partnership agreement, the approval of all partners, general and limited, is required to amend the partnership agreement, amend the certificate of limited partnership to add or delete an election of limited liability limited partnership status, or dispose of all or substantially all of the limited partnership’s assets outside the ordinary course of business. Again, the partnership agreement may increase or decrease the number of actions requiring the approval of all partners.

From the limited partnership, general partners are entitled to (i) reimbursement by the limited partnership for payments made on behalf of the limited partnership in the course of its activities or to preserve its assets, (ii) indemnification by the limited partnership for liabilities incurred in the course of its activities or to preserve its assets, and (iii) reimbursement of advances made in excess of the general partner’s agreed capital contribution.

236. In the former case, the differentiations are binding upon the limited partners, while in the latter they are not.
241. KY. REV. STAT. ANN. § 362.2-406(2)(a)-(c) (LexisNexis 2006). This list of items requiring, absent a contrary provision in the partnership agreement, the consent of the limited partners, is partial; there are other actions that, all else being equal, will require their consent. See supra notes 181 through 195 and accompanying text.
242. KY. REV. STAT. ANN. § 362.2-406(6) (LexisNexis 2006); accord § 362.1-401(3).
243. KY. REV. STAT. ANN. § 362.2-406(4) (LexisNexis 2006); accord § 362.1-401(4). Payments on behalf of or advanced to the limited partnership are treated as loans that accrue interest as determined under § 362.2-107(2). See § 362.2-406(5).
Unless agreed in the partnership agreement, general partners are not entitled to remuneration for services rendered to the limited partnership. It is important to note that this default rule is similar to, but departs in a material way, from the rule under the KyRUPA. In a general partnership, partners are not entitled to remuneration except in connection with the winding up and termination of the partnership. In KyULPA there is no different treatment of the winding up and termination phase of the limited partnership.

Unlike the information rights of limited partners, which are specific and circumscribed, the information rights of general partners are near plenary. Each general partner may access the information that the limited partnership is required to maintain, and may as well access, “any other records maintained by the limited partnership regarding the limited partnership’s activities and financial condition.” As such, there is no requirement of a statement as to why information is wanted or the opportunity for the limited partnership to determine that the requested information will not be provided.

Each general partner as well as the limited partnership itself is obligated to furnish to each general partner:

- Without demand, “any information concerning the limited partnership’s activities reasonably required for the proper exercise of the general partner’s rights and duties under the partnership agreement or” KyULPA; and
- On demand, “any other information concerning the limited partnership’s activities, except to the extent the demand or the information demanded is unreasonable or otherwise improper under the circumstances.”

A dissociated general partner has certain rights to information for the period they were a general partner on terms similar to those applicable to a current limited partner. A dissociated general partner may be charged the costs of producing requested information; there is no similar cost shifting mechanism for information sought by and provided to an incumbent general partner. As was the case with information provided to a limited partner, the limited partnership may impose “reasonable limitations” on the use of information provided a current or

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former general partner, and bears the burden of proving that proposed limitations are reasonable. The limitations are binding as well on any agent or attorney through whom a current or former general partner inspects records. Except with respect to a dissociated general partner, no transferee has rights under this section.

Few topics have caused the spillage of as much ink as the fiduciary obligations of partners. The initial recommendation for the revision of UPA proposed that the fiduciary formulation of UPA § 21(1) be reviewed and updated. With the end of linkage of limited partnership to general partnership law, it became necessary for the limited partnership act to independently address the standards imposed upon the general partners. Following as it was on the heels of RUPA, ULPA adopted, as to the general partners, the same formulations for the fiduciary obligations of care and loyalty and the contractual obligations of good faith and fair dealing as had been recently approved. Depending upon your frame of reference, RUPA either accurately codifies the common law as developed under UPA or adopts an entirely new regime that departs from the previously developed common law. For practitioners in Kentucky there is as well an additional complexity – the provisions adopted in KyULPA are not uniform. This discussion will review the fiduciary and other obligations of ULPA § 408, then review the limited modifiability of those provisions under ULPA § 110, then review the impact of the non-uniform revisions made to KyULPA § 408 in KyULPA.

A discussion of fiduciary obligations under partnership law must begin with UPA § 21(1), which provides:

258. See RUPA § 404 (1997); see also ULPA § 408 (2001), in which the official comment identifies RUPA § 404 as its source.
Every partner must account to the partnership for any benefit, and hold as trustee for it any profits derived by him without the consent of the other partners from any transaction connected with the formation, conduct, or liquidation of the partnership or from any use by him of its property.261

Just as often cited for the fiduciary obligations of partners are the words of Justice Cardozo in *Meinhard v. Salmon*,262 to wit:

> Joint adventurers, like copartners, owe to one another, while the enterprise continues, the duty of the finest loyalty. Many forms of conduct permissible in a workaday world for those acting at arm’s length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the marketplace. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior.263

Several points are worth noting. First, the language of RUPA § 21(1) and of *Meinhard* address what we think of today as the “duty of loyalty”; the “duty of care” is not addressed.264 Second, while UPA speaks of the obligations of each partner to the partnership, *Meinhard* speaks of obligations among the partners.

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261. UPA § 21(1) (1914); KY. REV. STAT. ANN. § 362.250(1) (LexisNexis 2006).
263. *Id* at 546. This language has been criticized as overstating partner obligations. See, e.g., Robert W. Hillman, *Private Ordering Within Partnerships*, 41 U. MIAMI L. REV. 425, 458 (1987), which observed:

> Although colorful, the judicial rhetoric inevitably overstates the standard of conduct the law actually imposes on partners. If partners truly are fiduciaries, they are a unique species of this group and cannot be subjected to traditional standards applicable to other types of fiduciaries. . . . Partners . . . are always joint owners. . . . Partners are not disinterested trustees, and the likelihood that most partners operate under a “punctilio of an honor the most sensitive” standard is remote.

A description of the fiduciary duties of the partners in a partnership predating UPA and likely informing the drafting of UPA § 21 was the Supreme Court’s ruling in *Latta v. Kilbourn*, which provided:

> [It is] well settled that one partner cannot, directly or indirectly, use partnership assets for his own benefit; that he cannot in conducting the business of a partnership, take any profit clandestinely for himself; that he cannot carry on the business of the partnership for his private advantage; that he cannot carry on another business in competition or rivalry with that of the firm, thereby depriving it of the benefit of his time, skill, and fidelity, without being accountable to his copartners for any profit that may accrue to him therefrom; that he cannot be permitted to secure for himself that which it is his duty to obtain, if at all, for the firm of which he is a member; nor can he avail himself of knowledge or information which may be properly regarded as the property of the partnership, in the sense that it is available or useful to the firm for any purpose within the scope of the partnership business.

264. See also RUPA § 404(c) cmt 3 (1997) (“There is no statutory duty of care under the UPA . . . ”).
without reference to the partnership. Third, while Meinhard’s lofty language, whether normative or aspirational, uses the term “fiduciary” and references the law of trusts, the term “fiduciary” does not appear in UPA § 21(1). Still, there developed a broad body of decisional law addressing the twin fulcrums of fiduciary duty law, the duty of care and the duty of loyalty.

Whether the common law as developed under UPA for the standard of care was that of an ordinarily prudent person, some standard more relaxed than ordinary care, or merely good faith, has long been the subject of debate, as has whether the relaxed standard of review of the business judgment rule is applicable in the partnership context. Indeed, one may conclude that the relative paucity of case law (and the varying language employed by the courts in the case law) has not yielded the necessary critical mass of decisional law necessary to derive and impose a consistent standard. Regardless of the formulation of the standard of care employed, the question of whether such standard could be prospectively modified by the partners’ agreement has also been the subject of some debate.

ULPA addresses the fiduciary obligations in a manner entirely different than that set forth in UPA, providing:

265. “Fiduciary” does appear in the heading to RUPA § 21(1). The standard of a “trustee” appears in both UPA § 21(1), KY. REV. STAT. § 362.250(1), and in Meinhard.

266. See generally II ALAN R. BROMBERG & LARRY E. RIBSTEIN, BROMBERG AND RIBSTEIN ON PARTNERSHIP § 6.07 (2007).


268. BROMBERG AND RIBSTEIN, supra note 266, at § 6.07(f).

269. CALLISON AND SULLIVAN, supra note 165, at § 12.02.

270. See, e.g., Gerard C. Martin, Duties of Care Under the Revised Uniform Partnership Act, 65 U. CHI. L. REV. 1307, 1309-10 (1998) (“While most courts and scholars agree that partners owe each other some duty of care under the UPA, there are some who argue the partners owe each other no duty of care whatsoever. Additionally, others disagree strongly about what that duty is.”).


The most fundamental duty owed by partners to one another is a fiduciary duty. Partners may, however, believe that by mutual consent they can restrict or virtually eliminate these mutual obligations. Under current partnership law, this belief is probably mistaken; under most present judicial interpretations of the Uniform Partnership Act (UPA), fiduciary duties are mandatory provisions waivable only with informed consent, on a case-by-case basis. (footnotes omitted).

273. UPA § 21(1), adopted in Kentucky at KY. REV. STAT. ANN. § 362.250(1) (LexisNexis 2006), provides:

Every partner must account to the partnership for any benefit, and hold as trustee for it any profits derived by him without the consent of the other partners from any transactions connected with the formation, conduct, or liquidation of the partnership or from any use by him of its property.
(a) The only fiduciary duties a general partner has to the limited partnership and the other partners are the duties of loyalty and care under subsections (b) and (c).

(b) A general partner’s duty of loyalty to the limited partnership and the other partners is limited to the following:

(1) to account to the limited partnership and hold as trustee for it any property, profit, or benefit derived by the general partner in the conduct and winding up of the limited partnership’s activities or derived from a use by the general partner of limited partnership property, including the appropriation of a limited partnership opportunity;

(2) to refrain from dealing with the limited partnership in the conduct or winding up of the limited partnership’s activities as or on behalf of a party having an interest adverse to the limited partnership; and

(3) to refrain from competing with the limited partnership in the conduct or winding up of the limited partnership’s activities.

(c) A general partner’s duty of care to the limited partnership and the other partners in the conduct and winding up of the limited partnership’s activities is limited to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law.274

ULPA § 408(d) imposes upon each general partner, in the discharge of their obligations to the limited partnership and the other partners, and in the exercise of their rights vis-à-vis the other partners, whether arising under ULPA or the partnership agreement, obligations of good faith and fair dealing.275 Referenced in ULPA § 110(b)(5), the obligation of good faith and fair dealing may not be eliminated, but reasonable standards of measurement may be imposed.276

What is meant by the imposition of the obligations of good faith and fair dealing upon partners has been subject to significant dispute. Good faith has traditionally been seen as an aspect of the partners’ fiduciary obligations under

274. ULPA §§ 408(a)-(c) (2001). ULPA § 408(c) has not been adopted in KyRUPA, and a unique and non-uniform provision appears in place thereof. See infra notes 304-05 and accompanying text.
275. KY. REV. STAT. § 362.2-408(4) (LexisNexis 2006); ULPA § 408(d) (2001).
276. KY. REV. STAT. § 362.2-110(2)(g) (LexisNexis 2006).
UPA, and the ABA-UPA Paper sought incorporation into a revised UPA of a fiduciary duty of good faith. Whether good faith is itself a fiduciary duty or a component of the enumerated duties is disputed in both the cases and the commentary, and there is at least dicta in Kentucky indicating that the obligation is fiduciary in nature.

Under ULPA, good faith is addressed not as a fiduciary concept, but as a contractual issue akin to that utilized under the Uniform Commercial Code. At the same time, RUPA acknowledges that the definitions of good faith as the terms are utilized in the UCC as “too narrow or not applicable.” Not referenced in the commentary to RUPA is the definition of “good faith” set forth in the RESTATEMENT OF CONTRACTS § 205, namely “good faith performance of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party.” With respect to these obligations, the official commentary to RUPA provides:

The meaning of “good faith and fair dealing” is not firmly fixed under present law. “Good faith” clearly suggests a subjective element, while “fair dealing” implies an objective component. It was decided to leave

277. See, e.g., Newberger, Loeb’s Co. v. Gross, 563 F.2d 1057, 1078 (2nd Cir. 1977), cert. denied, 434 U.S. 1035 (1978) (primary elements of a partner’s fiduciary obligations are “utmost good faith, fairness [and] loyalty”) (citations and quotation marks omitted).
278. UPA Revision Subcommittee, supra note 257, at 151.

Next, Lach argues that the general partners breached their fiduciary duty by transferring partnership assets to the LLC. Partners have the duty to act with the utmost good faith to all other partners.


281. See RUPA § 404 cmt. 4 (1997) (referring to the Uniform Commercial Code while acknowledging that its definitions are too narrow for application in the partnership context).
282. “Honesty in fact” and “the observance of reasonable commercial standards of fair dealing in the trade.”

283. RUPA § 404 cmt. 4 (1997).
the terms undefined in the Act and allow the courts to develop their meaning based on the experience of real cases. Some commentators, moreover, believe that good faith is more properly understood by what it excludes than by what it includes.

Good faith, as judges generally use the term in matters contractual, is best understood as an “excluder” – a phrase with no general meaning or meanings of its own. Instead, it functions to rule out many different forms of bad faith. It is hard to get this point across to persons used to thinking that every word must have one or more general meanings of its own – must be either univocal or ambiguous.284

The commentary to RUPA § 404(d) states that “in some situations the obligation of good faith includes a disclosure component. Depending upon the circumstances, a partner may have an affirmative disclosure obligation that supplements the Section 403 duty to render information.”

ULPA § 408(e)285 provides:

A general partner does not violate a duty or obligation under this [Act] or under the partnership agreement merely because the general partner’s conduct furthers the general partner’s own interests.

This provision and the official commentary thereto for the language as adopted in RUPA are deceptively brief considering the alteration in partnership law that follows, or at least may follow, from this language. Certain commentary states that the new language is meant to make clear that “a partner as such is not a trustee and is not held to the same standards as a trustee.”286 If and to the extent that UPA and the common law hold a partner to the standards of a trustee, this provision is a material change in the law.287 It is not clear, however, that the standard of a trustee was the applicable rule under UPA. Rather, the UPA statutory scheme dictated that “partners renounce the immediate, non-consensual pursuit of self interesting favor of the long term pursuit of self-interest through the collective mechanism of the partnership.”288 There exist at least three alternative explanations to ULPA § 408(e). Under the first it is in the nature of

284. RUPA § 404 cmt. 4 (1997) (citation omitted).
285. KY. REV. STAT. ANN. § 362.2-408(5) (LexisNexis 2006); accord § 362.1-404(5).
286. RUPA § 404 cmt 5 (1997). Cf. Meinhard, 164 N.E. at 546 (discussing a partner’s obligations by reference to those of a “trustee”); see also Enjoy Snax Vending, Inc. v. Williams Food Serv., No. 2003-CA-000717-MR, 2004 WL 2149193, at *2 (Ky. Ct. App. Sept. 24, 2004) (“In Kentucky, it is well established that every contract has an implied covenant that imposes upon the parties a duty to conduct itself in a ‘bona fide’ manner. That duty requires the parties to act ‘in good faith; honestly, openly, and sincerely; without deceit or fraud.’") (citations omitted).
287. See Donald J. Weidner, RUPA And Fiduciary Duty: The Texture Of Relationship, 58 L. & CONTEMP. PROBS. 81, 88 (1995) (“To emphasize: this language changes the basic statement of the default rule among partners. RUPA section 404(e) sets aside both partnership case law and basic agency doctrine requiring abnegation of self.”) [hereinafter Weidner, RUPA and Fiduciary Duty].
an evidentiary rule that “the fact that a partner directly personally benefits from the partner’s conduct in the partnership context does not, without more, establish a violation of the partner’s duties or obligations under ULPA or the partnership agreement.” 289 An alternative reading is that so long as the limitations of the duty of loyalty as set forth in ULPA § 408(b), as perhaps modified within the constraints of ULPA § 110(b)(3), are satisfied, no action of a general partner, even if undertaken without notice or informed consent, will constitute a violation of the duty of loyalty or the obligations of good faith and fair dealing. 290 At the same time, it cannot be read as permitting a partner to act adversely to or in conflict with the partnership; such a reading would nullify ULPA § 408(b)(2). 291 A third possible interpretation is that ULPA § 408(e) incorporated a “fairness” test pursuant to which, in assessing a self-interested act by a partner, the examination is two-fold: Was there benefit to the partner and was there detriment to the partnership and/or the other partners? Absent the second element, the partner’s action does not violate the obligation of loyalty. 292 This interpretation gives effective meaning to the otherwise curious term “merely” as utilized in the statute.

Factors distinguishing ULPA § 408 from UPA § 21(1) include the former’s:

- Exclusion of the common law from further informing the fiduciary duties among the partners; 293
- Effort of comprehensively codify both the standard of care and the standard of loyalty; 294

289. See Weidner, RUPA And Fiduciary Duty, supra note 287, at 88.
291. KY. REV. STAT. § 362.1-404(2)(b) (LexisNexis 2006) (a partner’s duty of loyalty includes refraining “from dealing with the partnership in the conduct or winding up of the partnership business as or on behalf of a party having an interest adverse to the partnership.”).
292. Mitchell, Naked Emperor, supra note 259, at 473-76.
293. See RUPA § 404 cmt. 1 (1997) (“Section 404 is both comprehensive and exclusive. In that regard, it is structurally different from the UPA which touches only sparingly on a partner’s duty of loyalty and leaves further development of the fiduciary duties of partners to the common law of agency.”); see also HILLMAN ET AL., supra note 288, at § 404 cmt. 1 (“First, RUPA presents an exclusive statutory treatment of partners’ fiduciary duties. Unlike the UPA, which co-exists with the common law, RUPA attempts to displace the common law and define the fiduciary duties of partners entirely by statute.”). Consequent to statutory departure from RUPA, neither of these comments reflects the law in Kentucky.
294. See, e.g., RUPA § 404 cmt. 2 (1997) (“Section 404(b) provides three specific rules that comprise a partner’s duty of loyalty. These rules are exclusive and encompass the entire duty of loyalty.”); HILLMAN ET AL., supra note 288, at § 404 cmt. 2 (“By its terms, RUPA comprises an exclusive statement of the fiduciary duties of partners among themselves and to the partnership. The formulation is exclusive in two ways; the duties of loyalty and care are the only components of the partners’ fiduciary duties, and the duties themselves are exclusively defined.”). Consequent to statutory departure from ULPA, neither of these comments reflects the law in Kentucky.
• Limitation of the fiduciary obligations to those of care and loyalty;295
• Temporal limitation of the duty of loyalty that excludes pre-
formation activities;296
• Exclusion of an obligation to provide information from the fiduciary
framework;297
• Incorporation of the contractual obligations of good faith and fair
dealing as modifiers of the discharge of the fiduciary obligations;298
and
• Provision that, by means of ULPA § 110(b), subject to defined
limitations, the fiduciary obligations may be modified by private
ordering.299

KyULPA has modified the uniform language to eliminate the exclusivity of
the fiduciary obligations to those of care and loyalty and further eliminated the
exclusivity of the formula employed for each. This elimination of exclusivity is
accomplished by three modifications: (i) the deletion of the statement that care
and loyalty are the “only” fiduciary duties and the substitution of a statement
that the fiduciary duties “include” care and loyalty;300 (ii) the deletion of a
statement that the duty of loyalty is “limited to” and the substitution of a
statement that the duty of loyalty is “limited to” and the substitution of a
statement that the duty of loyalty “includes, but is not limited to”;301 and (iii) the

295. See Hillman et al., supra note 288, at § 404 cmt. 3 (“First, RUPA excludes from the
fiduciary duties formulation the common-law obligation of disclosure, and places the disclosure
provisions in another section. Second, RUPA downgrades the common-law fiduciary duty of good
faith to the status of a non-fiduciary ‘obligation.’”).
296. UPA § 21(1), Ky. Rev. Stat. § 362.250(1) (LexisNexis 2006), applies to the “formation,
conduct, or liquidation of the partnership,” while ULPA §§ 408(b) and 408(c) apply to the conduct
and the winding up of the partnership. “Reference to the ‘formation’ of the partnership has been
eliminated from RUPA because of concern that the duty of loyalty could be inappropriately
extended to the pre-formation period when that parties are really negotiating at arm’s length.”
RUPA § 404 cmt. 2 (1997). This is a significant departure from UPA as the common law has
imposed fiduciary obligations during the formation period. See, e.g., Waite ex rel. Bretton Woods
Acquisition Co. v. Sylvester, 560 A.2d 619, 625 (N.H. 1989). The obligations of good faith and
fair dealing do not apply during the formation period as they modify obligations under ULPA and
the partnership agreement, neither of which is applicable until the partnership comes into existence.
297. See Hillman et al., supra note 288, at § 404 cmt. 3a(i) (“Defining the disclosure
obligation as non-fiduciary is a significant departure from existing law, since the present [UPA]
regime affirmatively requires that partners make disclosures under certain well-defined
circumstances such as upon transactions with the partnership, the purchase of a partnership interest
from a partner or sale of a partnership interest to a partner.”).
298. Hillman et al., supra note 288, at § 404 cmt. 3b. Note that the ABA-UPA Paper
suggested that the new formulation include good faith as a fiduciary obligation. See UPA Revision
Subcommittee, supra note 257, at 151.
299. This addition was requested in the ABA-UPA Paper. See UPA Revision Subcommittee,
supra note 257, at 126.
deletion of a statement that the duty of care “is limited to” and the substitution of a statement that the duty of care “includes, but is not limited to.” 302 These modifications will allow a greater scope for the development of the common law than would be anticipated under the uniform language, and is a change that has been supported in the academic literature.303 In addition, an entirely non-uniform formula for the duty of care has been adopted. While ULPA recited the standard of care as being refraining from “grossly negligent or reckless conduct, intentional misconduct or a knowing violation of the law,” KyULPA adopts an aspirational model for the standard of care, expecting of the partners that they act “with the care that a reasonable person in a like position would exercise under similar circumstances and in a manner the partner believes to be in the best interests of the partnership.304 This aspirational standard avoids the “socially impoverished message” of the RUPA/ULPA duty of care formula305 and preserves an expectancy in partners that, while perhaps not that of Cardozo’s “trustee,” is still meaningful.

The provisions of ULPA § 408 are subject to modification in the partnership agreement only within the constraints of ULPA §§ 110(b)(5), (6), and (7).306 These limits on modification as set forth in KyULPA are the same as those in ULPA notwithstanding the fact that the standards themselves are different between KyULPA and ULPA. It is not possible to eliminate the duty of loyalty307 or unreasonably reduce the duty of care.308 So long as they are not manifestly unreasonable, specific types or categories of activities may be identified as not violating the duty of loyalty.309 What constitutes “manifestly unreasonable” is not defined. Similarly, while the duty of care may not be “unreasonably reduced,”310 that threshold is not defined. The obligation of good faith and fair dealing may not be eliminated, but subject to a requirement that

306. KY. REV. STAT. ANN. §§ 362.2-110(2)(e)-(g) (LexisNexis 2006).
307. KY. REV. STAT. ANN. § 362.2-110(2)(e); accord § 362.1-103(2)(e). Cf. DEL. CODE tit. 6 § 15-103(f) (2006) (allowing the prospective elimination of the duty of loyalty and/or the duty of care). The KyLLCA permits the elimination of personal liability for monetary damages for a breach of the duties set forth in KY. REV. STAT. ANN. § 275.170. See KY. REV. STAT. ANN. § 275.180(1) (LexisNexis 2006). Under the KyBCA, the Articles of Incorporation may eliminate or limit a director’s personal liability so long as the elimination or limitation does not extend to certain categories of conduct including those in which the director has a personal financial interest or personal benefit, the approval of an improper distribution, or “for acts or omissions not in good faith or which involve intentional misconduct or are known to the director to be a violation of law.” § 271B.2-020(2)(d); see also § 271B.8-300(5)(b).
308. KY. REV. STAT. ANN. § 362.2-110(2)(d) (LexisNexis 2006); accord § 362.1-103(2)(d).
they not be manifestly unreasonable, the standards by which good faith and fair dealing will be applied are permitted.\textsuperscript{311}

The provision authorizing for an ex post facto approval, upon full disclosure, of an action otherwise violating the standard of loyalty is confirmatory as, under generally applicable contract and agency law, the partners would have the capacity to authorize such actions.\textsuperscript{312} Therefore, this aspect of ULPA merely confirms that prevailing law.\textsuperscript{313}

Whether the business judgment rule is applicable to the duty of care analysis under KyULPA is debatable.\textsuperscript{314}

E. KyULPA Article 5 – Contributions and Distributions

A partner’s contribution to the limited partnership may be in the form of tangible or intangible property, including a promissory note.\textsuperscript{315} The obligation to contribute, as undertaken, is not excused by the partner’s death, disability, or other inability to perform.\textsuperscript{316} In the event of a failure to make a contribution of services or other property, the partner is obligated to contribute cash of equal value.\textsuperscript{317} The compromise of an obligation to make a contribution may be only by all of the partners.\textsuperscript{318} However, if a creditor has extended credit based upon a contribution obligation, they may enforce the original contribution, notwithstanding any inter-se compromise thereof.\textsuperscript{319}

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\item[311.] KY. REV. STAT. ANN. § 362.2-110(2)(g) (LexisNexis 2006); \textit{accord} § 362.1-103(2)(e).
\item[312.] KY. REV. STAT. ANN. § 362.2-110(2)(e)(2) (LexisNexis 2006); \textit{accord} § 362.1-103(2)(e)(2).
\item[313.] See RUPA § 103 cmt 5 (1997) (“Subsection (b)(3)(ii) is intended to clarify the right of partners, recognized under general law, to consent to a known past or anticipated violation of duty and to waive their legal remedies for redress of that violation.”) (emphasis added); \textit{see also} RESTATEMENT (THIRD) OF AGENCY § 8.06 (2006).
\item[314.] \textit{See} Miller & Rutledge, \textit{The Business Judgment Rule}, \textit{supra} note 271.
\item[315.] Note that, unlike the rule under the KyLLCA, KY. REV. STAT. ANN. § 275.200(1) (LexisNexis 2006), there is no requirement in KyULPA that the agreement to make a contribution to a limited partnership be in writing. Prior to the 2002 amendment to the Kentucky Constitution, there existed a requirement that “stock” be issued only for services performed or value paid. \textit{See} KY. CONST. § 193 (repealed 2002). This provision had not been made expressly applicable to limited partnerships organized pursuant to KyRULPA notwithstanding that the Kentucky Constitution defined “corporation” to include joint stock companies and associations, KY. CONST. § 208 (repealed 2002), and that “corporation” may include a “partnership, joint stock company or association.” KY. REV. STAT. ANN. § 446.010(8) (LexisNexis 2006); \textit{see also} Rutledge & Booth, \textit{LLC Act}, \textit{supra} note 228, at 25.
\item[316.] KY. REV. STAT ANN. § 362.2-502(1) (LexisNexis 2006); \textit{accord} § 275.200(2).
\item[317.] KY. REV. STAT. ANN. § 362.2-503(2) (LexisNexis 2006); \textit{accord} § 275.200(3). The agreed cash value of the contribution that was to have been in services or property other than cash is required to be agreed to and maintained in the limited partnership’s records. § 362.2-502(2); § 362.2-111(9)(a).
\item[318.] As this provision is not referenced in KY. REV. STAT ANN. § 362.2-110(2) (LexisNexis 2006), the unanimity threshold may be modified in the partnership agreement.
\item[319.] KY. REV. STAT. ANN. § 362.2-502(3) (LexisNexis 2006); \textit{accord} § 275.200(5). Still, a recovery brought about by a suit by a creditor of the limited partnership to enforce a limited
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The general rule for distributions from a limited partnership, whether they be interim or liquidating, is that they be made among the partners in proportion to the respective values of the contributions received from the partners.\textsuperscript{320} In a change from prior law, “[T]his section apportions distributions in relation to the value of contributions received from each partner without regard to whether the limited partnership has returned any of those contributions.”\textsuperscript{321} This alteration conforms the ULPA to the practice under which the limited partnership agreement provides the initial distributions will be a return of the amount contributed, thereby avoiding taxable income to the extent of the contribution returned.\textsuperscript{322} Many limited partnership agreements will provide alternative measures for the ratio of sharing distributions. However, care must be taken when doing so as the sharing ratios have additional impacts such as the allocation of certain voting rights.\textsuperscript{323}

Partners are not entitled to any distribution from the limited partnership except upon dissolution and winding up unless the limited partnership should decide to make an interim distribution.\textsuperscript{324} In many instances this rule will be altered in the partnership agreement, compelling distributions, if otherwise permissible, to meet the tax obligations of the partners or upon reaching certain pre-determined targets. The dissociation of a partner does not itself give rise to a right to a distribution.\textsuperscript{325}

ULPA § 506, addressing distributions in kind as adopted in the KyULPA, has been modified and supplemented. The first provision has been supplemented to make clear that irrespective of the nature of a partner’s contribution to the limited partnership, there is no right to demand that any distribution be in any form other than cash.\textsuperscript{326} There are, as well, alterations to the wording regarding

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\item The revision to this sentence in KyULPA is “A partner, regardless of the nature of the partner’s contribution, has no right to demand or receive any distribution from a limited partnership in any form other than cash.” \textit{Accord} § 362.1-402(1); § 362.469; § 275.220(1).
\end{itemize}
the propriety of distributions in kind. While the uniform language and KyULPA are parallel in eliminating any right to receive a distribution in kind, they differ as to the ability to compel a partner to receive a distribution in kind. Under ULPA § 506, the decision as to whether a distribution in kind will be acceptable is made by the recipient partner and preserves in the recipient partner the right to reject a distribution in kind even when the distribution is pro-rata among the partners. KyULPA preserves the partner’s right to reject an in kind distribution only if the distribution is on a basis other than pro-rata among all of the partners. So long as the in kind distribution is pro-rata among all of the partners in proportion to their respective interests in the limited partnership, no individual partner has the right to reject the distribution.327 With the non-uniform revisions, there is greater flexibility with respect to distributions in kind, including as part of a liquidating distribution.328

Once the determination is made that a distribution will be made, each partner, to the extent entitled to participate therein, has the status of and is entitled to the rights of a creditor of the limited partnership.329 If, however, the partner (including a dissociated partner) to whom a distribution is to be made owes an amount to the limited partnership, an example being to satisfy a contribution obligation, the distribution may be held back by the limited partnership as an offset.330

Distributions, whether interim or liquidating, may not be made by a limited partnership when either of two statutory tests is not satisfied. First, a distribution may not be made if it violates the partnership agreement.331 Second, a limited partnership is prohibited from making distributions that would render

329. Ky. Rev. Stat. Ann. § 362.2-507 (LexisNexis 2006); accord § 362.471 (granting to each partner or limited partner the status and remedies available to general creditors of the limited partnership with respect to any right to receive a distribution); § 275.225(4); § 275.235 (granting to each member the status of and remedies available to creditors of an LLC with respect to any right to receive a distribution); § 271B.6-400(6) (granting shareholders the status and remedies of creditors of a corporation with respect to declared but unpaid dividends); Taylor v. Axton-Fisher Tobacco Co., 173 S.W.2d 377 (Ky. Ct. App. 1943); see also Ky. Rev. Stat. Ann. § 362.2-508(5) (LexisNexis 2006).
331. Ky. Rev. Stat. Ann. § 362.2-508(1) (LexisNexis 2006). This curious provision is the only instance in which ULPA states that a limited partnership may not do something “in violation of the partnership agreement.” Even were it entirely absent, the same outcome would follow by virtue of ULPA § 110(a)/Ky. Rev. Stat. Ann. § 362.2-110(1) (LexisNexis 2006). In that the “partnership agreement” constitutes the agreement of the partners with respect to the operation of the partnership, see § 362.2-102(17), where a distribution is made and all partners consent thereto, it could be said that there is an amendment to the partnership agreement either permitting or ratifying that distribution and therefore that not only is not in violation of the partnership agreement, but rather that it is in compliance with the partnership agreement.
the limited partnership insolvent or otherwise impair its capital. A distribution is forbidden if, after it is made:

- The limited partnership would not be able to pay its debts as they became due in the ordinary course of business; or
- The total assets of the limited partnership would be exceeded by the sum of its total liabilities and the amount necessary to satisfy the dissolution rights of any interests which are superior to the dissolution rights of the partner(s) receiving the distribution.

A limited partnership is permitted to determine that a distribution is not prohibited by reference to financial statements prepared under practices and principals reasonable under the circumstances or a fair valuation or other methods reasonable under the circumstances. Therefore, it is not necessary that the limited partnership prepare its financial statements in accordance with generally accepted accounting principles consistently applied (“GAAP”). This flexibility in the preparation of financial statements will accommodate many small businesses that prepare their financial statements on a cash basis or otherwise do not follow GAAP.

The impact of a distribution upon the capital of a limited partnership is measured:

- In the case of a “purchase, redemption, or other acquisition of a transferable interest” as of the date the limited partnership’s assets are transferred or the debt is incurred; and
- In all other instances as of the date the distribution is authorized, provided payment is to occur within 120 days after the date of the authorization of the payment, or the actual date of distribution, if such occurs more than 120 days after the date of authorization.

334. Note that this determination is made by the limited partnership, not by the general partners.
335. Ky. Rev. Stat. Ann. § 362.2-508(3) (LexisNexis 2006); accord § 271B.6-400(4); § 275.225(2); see also Imperial Trading Co., Inc. v. Uter, 837 So.2d 663, 675 (La. Ct. App. 2002) (affirming trial court’s finding that manager was personally liable, along with member, for assenting, without reasonable care or inquiry, to distribution to member while LLC was unable to pay its debts as they came due and that other manager was not liable where evidence supported his lack of knowledge of distribution, but reversing trial court’s finding on other payments on basis record did not support imposing liability for checks payable to manager without evidence that they were distributions or that such a distribution violated the statutory restrictions). Even though a proposed distribution does not violate these provisions, further investigation of the effect of the distribution under fraudulent conveyance law is in order. See, e.g., In re Brentwood Lexford Partners, LLC, 292 B.R. 255, 264-65 (Bankr. N.D. Tex. 2003).
A distribution may be made contingent upon the ability of the limited partnership to make such payments, in which instance that contingent liability will not be used to assess the propriety of the distribution, but the effect of the payment on that obligation is measured anew as of the date each payment is actually made.

In a non-uniform provision, the limitations upon “distributions” are not applicable to compensatory payments made by the limited partnership to its partners. This is accomplished by excluding from the definition of a “distribution” compensatory payments made for services rendered to or on behalf of the LLC or as part of a retirement or other benefits program. The issue that arises is that while corporate officers and employees will typically receive salaries that are not construed as “distributions,” payments to partners for services rendered are treated as “distributions” under both state and tax law. This can give rise to a fundamentally unfair distinction in treatment. Imagine two entities ABC, Inc. and XYZ, LLLP. Mary is a shareholder and an employee of ABC, Inc. and is a general partner of XYZ, LLLP, for which she performs services. ABC, Inc. pays to Mary $1,000 in salary when the corporation is insolvent as determined under KRS § 271B.6-400(3). XYZ, LLLP makes a $1,000 “distribution” to Mary for services rendered when the LLLP is insolvent. Absent this non-uniform provision, the $1,000 paid Mary by ABC, Inc. is not subject to recovery as a wrongful distribution, while the $1,000 paid Mary by XYZ, LLLP may be subject to recovery as a wrongful distribution. The non-uniform provision precludes this inequitable result.

If a general partner consents to a distribution that violates the limitations imposed by ULPA § 508 and it is demonstrated that in doing so the general partner failed to satisfy the duty of care, the general partner is liable to the limited partnership for the excess of distribution over the permissible amount. The recipient of a distribution, knowing it to have been improperly declared, is liable to the limited partnership to the extent the distribution made exceeded the distribution that could properly have been made. A general partner against

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337. KY. REV. STAT. § 362.2-508(6) (LexisNexis 2006); accord § 275.225(5).
338. KY. REV. STAT. ANN. § 362.2-508(6) (LexisNexis 2006); accord § 275.225(1).
339. KY. REV. STAT. ANN. § 362.2-508(7) (LexisNexis 2006); accord § 275.225(6).
341. A broader review of this issue appears in Marshall Paul, Stuart Levine & Joyce Kuhns, Righting the Wrong Approach to Wrongful Distributions in Limited Liability Entities, 3 J. OF LIMITED LIABILITY COMPANIES 164 (Spring 1997); see also Allan G. Donn, Limited Liability Entities for Law Firms - 10 Years Later, 7 PASSTHROUGH ENTITIES 19, 23 (Aug. 2004).
342. The statute is silent as to any liability of a limited partner to whom a right to consent to a distribution has been allocated in the limited partnership agreement.
343. KY. REV. STAT. ANN. § 362.2-509(1) (LexisNexis 2006). While this provision is similar to that set forth for limited liability companies, see § 275.230(1), the KyLLCA does not condition personal liability upon a breach of duty by the member/manager approving the improper distribution.
344. KY. REV. STAT. ANN. § 362.2-509(2) (LexisNexis 2006).
whom recovery of the improper portion of a distribution is sought may implead and seek contribution from (i) any other general partner who participated in violating the standard of care in declaring the distribution and (ii) to the extent the distribution was improper, any other partner who received the distribution.  

An action for recovery of an improper distribution, or to require contribution from those who approved or received the impermissible distribution, may not be brought except within the two years the distribution. A waiver of the partnership’s right to seek recovery of an improper distribution is effective only if approved by all of the partners, and no waiver is binding upon a third party who without notice of a compromise has extended credit to the limited partnership based upon the recovery of an improper distribution.

F. **KyULPA Article 6 - Dissociation**

The ULPA §§ 601 through 604 address the dissociation of partners, either limited or general, from a limited partnership.

KyULPA provides that a limited partner has no right to disassociate from the partnership prior to its termination. Still, while lacking the right to dissociate, and subject to a contrary provision in the partnership agreement, a limited partner may dissociate, by giving notice of its “express will” to do so, even though that dissociation may be wrongful. Under the KyRULPA as originally adopted, absent the partnership agreement specifying a time or event upon which a limited partner could properly withdraw from the partnership, or in the absence of a definite time for the dissolution of the partnership, a limited partner had the statutory right to withdraw from the partnership six months following the giving of notice of withdrawal to each general partner. Having withdrawn, the limited partner was entitled to receive whatever payment certificate or, in the agreement of limited partnership or, in the absence of any such provision, the “fair value” of the limited partner’s interest in the partnership as of the date of

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348. Ky. Rev. Stat. Ann. § 362.2-601(1) (LexisNexis 2006). As originally adopted in Kentucky, KyRULPA provided that a limited partner could withdraw from the partnership on six months prior written notice, and thereafter receive a distribution of the fair value of the limited partner’s interest in the partnership. See § 362.465; § 362.467, each as prior to 1998 amendments. In 1998 these provisions were amended, see 1998 Ky. Acts ch. 341, §§ 50-51, to eliminate both any right of withdrawal, absent an enabling provision in the partnership agreement or the unanimous approval of the other partners, and of a liquidating payment upon withdrawal, unless such are set forth in a written partnership agreement.


withdrawal, which fair value was to be determined “based upon his right to share in distributions from the limited partnership.” 351

In addition to withdrawal by express will of a limited partner, a limited partner will be dissociated from the limited partnership upon:

- An event specified in the partnership agreement as causing a dissociation of a person as a limited partner, 352
- The expulsion of a limited partner by the unanimous consent of the other partners if it is unlawful to carry on the activities of the limited partnership with that person as a limited partner, if all of that limited partners transferable interest in the partnership has been transferred other than for purposes of giving security of pursuant to an unforeclosed charging order, in the case of a limited partner that is a corporation, 90 days after delivery by the limited partnership to the limited partnership that it will be expelled consequent to the filing of a certificate of dissolution, the revocation of its charter, or in the case of a limited partnership that is a limited liability company or a partnership, it being dissolved and its business wound up, 353
- A judicial determination pursuant to an application by the limited partnership that a person should be expelled as a limited partner because they have engaged in conduct that is wrongful and that adversely and materially affects the limited partnership, willful or pursuant material breaches of the partnership agreement or the obligations of good faith and fair dealing thereunder or they have engaged in conduct relating to the activities of the limited partnership such that it is not reasonably practical to thereafter carry on its activities with that person as a limited partnership. 354

351. KY. REV. STAT. ANN § 362.467 (LexisNexis 2006) (prior to 1998 amendment by 1998 Ky. Acts ch. 341, § 51). These provisions of KyRULPA were amended in 1998 with the objective of eliminating the right of withdrawal and in so doing making limited partnerships formed a KyRUPA more viable as estate planning vehicles.

352. KY. REV. STAT. ANN § 362.2-601(2)(b) (LexisNexis 2006). In contrast with the rule requiring that there be maintained in a record a listing of the events that would cause the dissolution of the limited partnership, 362.2-111(9)(d), there exists no statutory requirement that the event or events that would cause the dissociation of a limited partner be set forth in a record.

353. KY. REV. STAT. ANN. § 362.2-601(2)(d) (LexisNexis 2006). With respect to the treatment of a corporation and the suspension of its right to conduct business, such could take place by reason of an administrative dissolution that is remedied, with that remedy relating back, after the effective date of its expulsion as a limited partner. In that instance, the expulsion from the limited partnership will be effective notwithstanding the subsequent reinstatement. Note as well that, in the case of a limited liability company, there is not similar treatment in the event of administrative dissolution as its expulsion is conditioned upon the business being wound up; where administrative dissolution leads only to reinstatement within the applicable time period, and no actions toward the winding up are taken, expulsion from the limited partnership will not automatically happen.

• The death of a limited partner who is an individual;\textsuperscript{355}
• In the case of a limited partner that is a trust or trustee, a distribution of the trust entire transferable interest other than by reason of the substitution of a successor trustee;\textsuperscript{356}
• In the case of the limited partnership that is an estate or the personal representative of an estate, distribution of its entire transferable interest in the limited partnership other than by reason of the appointment of a successor personal representative;\textsuperscript{357}
• Other termination of a limited partner who is not an individual partnership, limited liability company, corporation, trust or estate;\textsuperscript{358}
or
• Upon the merger and conversion of the limited partnership if either limited partnership is not the surviving entity or if, in the course of the merger and conversion, that person does not become a limited partner in the successor entity.\textsuperscript{359}

Upon dissociation, the limited partner is not entitled to a buyout of their interest in the partnership.\textsuperscript{360} Rather, the limited partner retains only their transferable interest in the partnership, becoming, in effect, a transferee of their own interest.\textsuperscript{361} A limited partner so dissociated has no rights as a limited partner, is no longer bound by obligations of good faith and fair dealing, except with respect to those matters that have arisen prior to the dissociation, and at the same time is not discharged from any obligations of the limited partnership or other partners incurred prior to the dissociation, which obligations may include those of contribution.\textsuperscript{362} Furthermore, in that the limited partner has altered their status, on an economic basis, to that of a mere transferee, they are no longer owed fiduciary duties.\textsuperscript{363}

ULPA § 603\textsuperscript{364} addresses those events that cause the dissociation of a general partner from the partnership, a term functionally defined in ULPA §

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\item \textsuperscript{361} Ky. Rev. Stat. Ann. § 362.2-602(1)(c) (LexisNexis 2006). A limited partner so dissociated has no rights as a limited partner, is no longer bound by obligations of good faith and fair dealing, except with respect to those matters that have arisen prior to the dissociation, and at the same time is not discharged from any obligations of the limited partnership or other partners incurred prior to the dissociation, which obligations may include those of contribution.
\item \textsuperscript{362} Ky. Rev. Stat. Ann. § 362.2-602(1) (LexisNexis 2006); § 362.2-602(2).
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by its effect. However, dissociation does not in and of itself terminate a partner’s economic relationship with the partnership.366

Under ULPA § 603, a partner will be dissociated upon any of a series of events, events that are in part dependent upon the type (e.g., individual, corporation) of partner.367 ULPA § 110(b) limits modification of ULPA § 603 in only one aspect. The only permissible limit on a voluntary withdrawal under ULPA § 603(b)(1) is to require that the notice provided the partnership be in writing.368 It is worth noting that the right of a court to order a ULPA § 603(5) judicial expulsion of a partner may be varied in the partnership agreement.369

ULPA § 802 is referenced in ULPA § 110(b)(9), which provides that the partnership agreement may not “vary the power of a court to decree dissolution in the circumstances specified in Section 802.”370 Reasonable minds can differ as to the proper interpretation of ULPA § 110(b)(9) and its preclusive effects. Under one reading, there remains open the opportunity for the partnership agreement to impose additional procedural requirements, such as requiring collective action by the partners in order to initiate an action for expulsion, on the theory that such requirements neither vary the “power of a court”371 nor the “circumstances specified in Section 802.”372 By way of contrast, the Official Comment to RUPA § 103(b)(7), upon which ULPA § 110(b)(8) is based, appears to be broader than the text of the provision itself,373 and precludes such procedural limitations upon the unilateral right of a partner to initiate an expulsion action under RUPA § 601(5), stating in part “Under subsection (b)(7), the right of a partner to seek court expulsion of another partner under 601(5) can not be waived or varied (e.g., requiring a 90-day notice) by agreement.”374 In order that RUPA § 103(b)(7) may conform to its commentary, it has been amended in KyRUPA to provide that the partnership agreement may not “Vary the right of a partner or the partnership to seek a partner’s expulsion by judicial determination or vary the right of a court to expel a partner in the events specified in KRS 362.1-601(5).”375

365. KY. REV. STAT. ANN. § 362.2-605 (LexisNexis 2006).
367. The events causing the dissociation of a partner are in part generic to all partners irrespective of type, KY. REV. STAT. ANN. §§ 362.2-603(1)-(6) (LexisNexis 2006), and in part are dependent upon the nature of the partner. §§ 362.1-602 (7)-(10).
368. ULPA § 110(b)(8) (2001); KY. REV. STAT. ANN. § 362.2-110(2)(h) (LexisNexis 2006).
373. However, NCCUSL’s own rules preclude the expansion of the substantive text of a uniform act by the commentary. See National Conference of Commissioners on Uniform State Laws, Procedural and Drafting Manual 10 (1997) (“Comments should not be used as a substitute for or to modify any substantive provision in the Act.”).
374. RUPA § 103(b)(7) cmt. 9 (1997).
375. KY. REV. STAT. ANN. § 362.1-103(2)(g) (LexisNexis 2006).
The dissociation of a partner by reason of being a debtor in bankruptcy is problematic, especially if the partnership is a limited liability limited partnership. The Bankruptcy Code, at sections 365 and 541, disfavors so-called “ipso facto” provisions, namely those that are triggered by the bankruptcy filing and which have the effect of reducing the value of the interest in the hands of the debtor. Traditionally, partnership agreements have been viewed as executory agreements, namely those requiring continuing performance and obligations from all of the partners and the partnership. On this basis, the dissociation of a partner by reason of bankruptcy was deemed appropriate. One aspect of those continuing obligations was the shared obligations of the partners to contribute toward the satisfaction of partnership obligations. This rationale may not exist in a LLLP absent a contrary provision in the partnership agreement; not only are the general partners not liable for the debts and obligations of the partnership, but also they have no obligations to contribute toward obligations satisfied by other partners.

ULPA § 604 addresses when a general partner’s dissociation from the partnership is wrongful. Note that even if wrongful, the partner has the right to dissociate. Hence, “A person has the power to dissociate at any time as a general partner, rightfully or wrongfully, by express will pursuant to KRS 362.2-603(1).” As such, the distinction between the power and the right to dissociate (withdraw from the partnership) is retained. This power may not be varied in the partnership agreement. A dissociation that is wrongful exposes the dissociating partner to liability to the partnership and to the other partners for


377. As of this writing there is no published ruling assessing whether an LLLP agreement is or is not an executory agreement and the impact of limited liability upon the traditional analysis of partnership agreements. See also In re Ehmann, 319 B.R. 200 (Bankr. D. Ariz. 2005), aff’d, 334 B.R. 437, withdrawn, 337 B.R. 228 (Bankr. D. Ariz. 2006); In re Baldwin, No. 04-72919, 2006 WL 2034217 (B.A.P. 10th Cir. July 11, 2006); Thomas E. Geu & Thomas E. Rutledge, Guess Who’s Coming to Dinner?: The Bankruptcy Trustee’s Ability to Become a Member and the Ehmann Decision, 7 BUS. ENTITIES 32 (2005); Thomas E. Rutledge & Thomas Earl Geu, In re Ehmann II: Now You See It, Now You Don’t, 8 BUS. ENTITIES 44 (2006); James J. Wheaton, Current Status of Bankruptcy Issues (Mar. 16, 2006), in ALI-ABA VIDEO L. REV. (2006); Susan Kalinka, In re Ehmann: Bankruptcy Court Decision Portends Problems for Manager-Managed LLCs, 84 TAXES 5 (2006).


379. KY. REV. STAT. ANN. § 362.2-604(2) (“A person’s dissociation as a general partner is wrongful only if . . . .”) (emphasis added); see also § 362.300(2).

damages caused by the dissociation.\textsuperscript{381} Furthermore, if a wrongful dissociation results in the dissolution of the partnership, the wrongfully dissociating partner is not entitled to participate in the winding up.\textsuperscript{382} A dissociation is wrongful if:

(a) It is in breach of an express provision of the partnership agreement; or

(b) In the case of a partnership for a definite term or particular undertaking, before the expiration of the term or the completion of the undertaking if any of the following apply:

1. The partner withdraws by express will;

2. The partner is expelled by judicial determination under KRS 362.2-603(5);

3. The partner is dissociated by becoming a debtor in a bankruptcy; or

4. In the case of a partner who is not an individual, trust other than a business trust, or estate, the partner is expelled or otherwise dissociated because it willfully dissolved or terminated.\textsuperscript{383}

ULPA § 605 addresses the consequences of a dissociation, whether proper or wrongful, of a general partner. As to the dissociated partner:

- The partner’s right to participate in the management and conduct of the partnership’s business terminates;\textsuperscript{384}
- Certain aspects of the partner’s duty of loyalty terminate;\textsuperscript{385} and
- The general partner’s duty of care and other aspects of the duty of loyalty continue only as to matters and events occurring before the dissociation.\textsuperscript{386}

Interestingly, and for understandable reasons, ULPA § 605 does not expressly address the continuation, subsequent to dissociation, of a partner’s obligations of good faith and fair dealing. These obligations modify other obligations of the partners under the Act and the partnership agreement. As such, to the extent that obligations continue subsequent to dissociation, which question is in part dependent upon whether the dissociation will be followed

\textsuperscript{381} KY. REV. STAT. ANN. § 362.1-604(3) (LexisNexis 2006); see also § 362.2-605(6).
\textsuperscript{382} KY. REV. STAT. ANN. § 362.2-605(1) (LexisNexis 2006).
\textsuperscript{383} KY. REV. STAT. ANN. § 362.2-604(2)(b) (LexisNexis 2006).
\textsuperscript{384} See KY. REV. STAT. ANN. § 362.2-605(1) (LexisNexis 2006).
\textsuperscript{385} See KY. REV. STAT. ANN. § 362.2-605(2); see also § 362.2-404(2)(c).
\textsuperscript{386} KY. REV. STAT. ANN. § 362.2-605(3) (LexisNexis 2006); see also § 362.2-408(2)(a); § 362.2-408(2)(b); § 362.2-408(3).
with winding up and termination, the obligations of good faith and fair dealing will continue in force. As obligations, including fiduciary obligations, diminish or terminate, the contractual obligations of good faith and fair dealing will as well diminish and terminate.

ULPA § 606 addresses the ongoing agency authority of a general partner subsequent to the general partner’s dissociation. Assuming the partnership has not otherwise ceased to exist, the former general partner may still bind the limited partnership if:

- The action would have been within the authority of a general partner who is not dissociated;
- It has been less than two years since the general partner’s dissociation; and
- The third party did not have notice of the dissociation and reasonably believed that the person was still a general partner.387

While the limited partnership may be bound to the third party by a dissociated general partner, the dissociated general partner is liable to the limited partnership and to any general partner for any damage caused to the limited partnership or them by that obligation.388 In light of the continuing authority of a dissociated general partner, it is advised that the statement of dissociation and the amendment of the certificate of limited partnership, both recording the dissociation, be filed as soon as is possible, and that steps be taken to put third-parties on notice of these filings.389

ULPA § 607 addresses the continuing obligations of a general partner, as a general partner, for the obligations of the limited partnership subsequent to dissociation. Initially, dissociation does not relieve a general partner of an obligation incurred by the limited partnership prior to the dissociation.390 While a general partner is not exposed on obligations of the limited partnership accrued after dissociation, there are two exceptions to the rule. First, if the general

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387. KY. REV. STAT. ANN. § 362.2-606(1) (LexisNexis 2006). Note that the final clause requires both components; they are not alternatives.
388. KY. REV. STAT. ANN. § 362.2-606(2) (LexisNexis 2006). The term used is “damage,” and not “cost,” because the limited partnership may in fact benefit from the transaction to which it was improperly bound. Accord § 362.1-702(2).
389. The dissociated general partner is obligated, at the request of the limited partnership, to sign an amendment to the certificate of limited partnership stating that they have dissociated. See KY. REV. STAT. ANN. § 362.2-605(4) (LexisNexis 2006). As well, a statement of dissociation may be filed with the Secretary of State. The notice effect of the two filings is the same. See § 362.2-103(4)(a). While filing a statement of dissociation is optional, amending the certificate of limited partnership to delete the dissociated general partner is mandatory. See § 362.2-202(2)(b).
390. KY. REV. STAT. ANN. § 362.2-607(1) (LexisNexis 2006). For the period that the limited partnership is a limited liability limited partnership, the general partner will not have liability for the obligations of the limited partnership. As was the case under ULPA § 404, KY. REV. STAT. ANN. § 362.2-404, other law will determine when an obligation was “incurred.”
partner’s dissociation results in the limited partnership’s dissolution, the otherwise dissociated partner is liable as is any other general partner under ULPA 404 for an obligation undertaken under ULPA 804.\footnote{391} Second, if the dissociation does not result in the dissolution of the limited partnership, the general partner is liable for obligations of the limited partnership if:

- A general partner would be liable on the obligation; and
- At the time the third party enters into the transaction: it has been less than two years since the general partner’s dissociation; the third party did not have notice of the dissociation and reasonably believed that the person was still a general partner.\footnote{392}

A creditor of the limited partnership may release a dissociated general partner from liability on an obligation, but the release requires the consent of the limited partnership.\footnote{393} Alternatively, a dissociated general partner is automatically released if the creditor, with notice of the dissociation and without seeking and receiving the consent of the dissociated general partner, agrees to a material alteration of the obligation.\footnote{394}

G. KyULPA Article 7 - Transferable Interests and Rights of Transferees and Creditors

ULPA § 701 defines a partner’s transferable interest in the limited partnership as the right to receive distributions, and further provides that the transferable interest is personal property.\footnote{395} The transfer of a transferable interest is permissible, does not dissociate the transferor, and does not cause the dissolution of the limited partnership.\footnote{396} A transferee is entitled to receive distributions made with respect to the transferable interest, whether periodic or liquidating.\footnote{397} The receipt of a transferable interest does not entitle the transferee to participate in the management of the limited partnership or to access information except upon the winding-up of the partnership and then only from the date of dissolution.\footnote{398} Still, the transferee has no right to participate in the management of the limited partnership and is not owed fiduciary obligations or obligations of good faith and fair dealing. The transfer of a transferable

\footnote{392. Ky. Rev. Stat. Ann. § 362.2-607(3) (LexisNexis 2006). Note that both components are required; they are not alternatives.}
\footnote{396. Ky. Rev. Stat. Ann. §§ 362.2-702(1)(a)-(b); accord §§ 362.1-503(1)(a)-(b); see also § 275.255(1).}
interest does not deprive the transferor of the rights not encompassed within the transferable interest, including the right to participate in management, to inspect records, and to benefit from the fiduciary obligations of the general partners. As such, barring expulsion, the transferor limited partner retains those rights. The partnership agreement may contain limitations upon the transferability of a transferable interest, but those limitations are effective only as to a third party that has notice thereof. The addition of non-uniform new subsection (8) to ULPA § 702 serves to preempt KRS §§ 355.9-406 and 355.9-408, which may themselves be interpreted to preempt limitations upon the transfer of the transferable interest contained in the limited partnership agreement.

ULPA § 703 details the rights of a judgment creditor vis-à-vis a partner’s transferable interest. Essentially, a charging order is a lien on the transferable interest entitling the holder to receive all distributions that would be otherwise made to the partner until such time as the judgment is satisfied. That lien is subject to foreclosure, and the purchaser of the lien will have the rights of a transferee. The charged interest, prior to foreclosure, is subject to redemption by the judgment debtor/partner, by another partner, or by the partnership.

Various state exemption laws are applicable to the transferable interest and as

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400. KY. REV. STAT. ANN. § 362.2-704(4) (LexisNexis 2006).
405. KY. REV. STAT. ANN. § 362.2-703(1) (LexisNexis 2006); accord 362.1-504; § 362.285(1); § 275.260. The decision in Hubbard v. Talbott Tavern, Inc., No. 2003-CA-001468-MR, 2006 WL 2089308 (Ky. App, July 28, 2006), as regards charging orders is not a correct application of the law. The Court of Appeals upheld a trial court order that “assigned” to the judgment creditor the judgment debtor’s membership interest in each of three LLCs and further directed that, by reason of the assignment, the judgment debtor be dissociated and cease to be a member of each of the LLCs. It said as well that the assignments of the membership interests would continue until the judgment was satisfied. The Court justified the order of dissociation on the basis of § 275.280(1), which provides that a member is dissociated when they “make an assignment for the benefit of creditors.” The charging order provision of the KyLLCA, KY. REV. STAT. ANN. § 275.260 (LexisNexis 2006), does not use the word or otherwise authorize an assignment.
406. KY. REV. STAT. ANN. § 362.2-703(2) (LexisNexis 2006).
407. KY. REV. STAT. ANN. § 362.2-703(3) (LexisNexis 2006).
such may limit the charging order in full or in part.\textsuperscript{408} It is also provided that the charging order is the exclusive means by which a judgment creditor may satisfy the judgment against the partner’s transferable interest.\textsuperscript{409} The charging order exists to balance two valid and competing interests; that of the judgment creditor to collect on the judgment and the interest of the partnership to operate with minimal interruption from a partner’s creditor.\textsuperscript{410} Therefore, while the holder of the charging order has a lien on the distributions, as made, to the judgment debtor/partner, she has no right to participate in management and does not become a substitute partner or have even the rights of a transferee. At the same time the partner/judgment creditor remains a partner, her management rights are not diminished, and remains subject to the tax liability on partnership allocations and distributions.\textsuperscript{411} However, upon foreclosure of the charging order, which transfers the transferable interest to the purchaser, the partner may be expelled from the partnership.\textsuperscript{412}

The representative of a deceased partner has the rights of a transferee, and not of a partner, but is afforded for purposes of settling the estate the information rights of a current limited partner.\textsuperscript{413}

H. \textit{KyULPA Article 8 – Dissolution}

A limited partnership shall be dissolved and its activities wound up upon:\textsuperscript{414}

\begin{itemize}
  \item An event specified in the partnership agreement;\textsuperscript{415}
  \item The approval of all of the partners;\textsuperscript{416}
\end{itemize}

\textsuperscript{408} KY. REV. STAT. ANN. § 362.2-703(4) (LexisNexis 2006); see also Rutledge, Changing Orders, supra note 403, at 27.

\textsuperscript{409} KY. REV. STAT. ANN. § 362.2-703(5) (LexisNexis 2006). Exclusivity language appears as well in the charging order provision of the KyLLCA. KY. REV. STAT. ANN. § 275.260 (LexisNexis 2006). Although RUPA § 703, KY. REV. STAT. ANN. § 362.481 (LexisNexis 2006), did not contain exclusivity language, it was often so interpreted; see RUPA § 504 cmt. 5 (1997).

\textsuperscript{410} See Rutledge, Charging Orders, supra note 403.

\textsuperscript{411} See Rutledge, Charging Orders, supra note 403; Stein, supra note 403; Robert R. Keatinge, Transfers of Partnership and LLC Interests - Assignees, Transferees, Creditors, Heirs, Donees, and Other Successors, § 504.3, in PROCEEDINGS OF THE 32ND ANNUAL PHILIP E. HECKERLING INSTITUTE ON ESTATE PLANNING (1998).

\textsuperscript{412} See KY. REV. STAT. ANN. § 362.2-603(4)(b) (LexisNexis 2006); see also § 362.2-601(2)(d)(2) (LexisNexis 2006).

\textsuperscript{413} KY. REV. STAT. ANN. § 362.2-704 (LexisNexis 2006). The information rights that may be exercised by the representative are set forth in § 362.2-304.

\textsuperscript{414} KY. REV. STAT. ANN. § 362.2-801 (LexisNexis 2006); § 362.2-802.

\textsuperscript{415} KY. REV. STAT. ANN. § 362.2-801(1) (LexisNexis 2006). While the partnership agreement need not be in writing, see § 362.2-102(17), the partnership is required to keep a record of “any events upon the happening of which the limited partnership is to be dissolved and its activities wound up.” § 362.2-111(9)(d). Under § 362.487(1), such an event needed to be specified in the certificate of limited partnership, or, in accordance with § 362.487(2), could be set forth in a written partnership agreement: §§ 362.487(1)-(2).

\textsuperscript{416} KY. REV. STAT. ANN. § 362.2-801(2) (LexisNexis 2006). This provision is non-uniform. ULPA § 801(2) (2001) calls for the approval of all of the general partners and a majority of the
• After the dissociation of a general partner, if there is at least one remaining general partner and the partners entitled to receive a majority of the distribution decide to dissolve;\(^{417}\)
• Ninety days after the dissociation of the last general partner, unless within that ninety-day period the limited partners elect a new general partner and that new general partner is admitted in accordance with that consent;\(^{418}\)
• Ninety days after the dissociation of the last limited partner, unless a new limited partner is in that period admitted;\(^{419}\)
• Administrative dissolution;\(^{420}\) or
• Judicial dissolution on the basis that “it is not reasonably practicable to carry on the business of the limited partnership in accordance with its partnership agreement.”\(^{421}\)

After dissolution, a limited partnership continues in existence only for the purposes of its winding up.\(^{422}\) In the course of the winding up, the limited partnership is to discharge its liabilities, settle and close its activities, and marshal and distribute its assets.\(^{423}\) If the limited partnership does not have a general partner, by a majority vote in accordance to their right of the distributions, the limited partners may elect a person to wind up the limited

limited partners, determined in proportion to the ratios to receive distributions, in order to approve the voluntary dissolution of the limited partnership. The modification of this threshold, which may be further modified in the partnership agreement, is intended to increase the utility of KyULPA for estate planning purposes. This non-uniform provision continues the rule of unanimity amongst all of the partners contained in KyRULPA. See § 362.487(3).

\(^{417}\) KY. REV. STAT. ANN. § 362.2-801(3)(a) (LexisNexis 2006). The election to dissolve the limited partnership needs to be made within ninety days after the general partner’s dissociation. In this instance all partners vote as a single class and voting rights are proportional to distributional rights. See § 362.2-503. As transferees do not exercise management rights or otherwise participate in the direction of the limited partnership, § 362.2-701; § 362.2-702(1)(c), they do not participate in the vote, and the distributional rights associated with the transferable interests held by transferees are excluded from the calculation of a majority.

\(^{418}\) KY. REV. STAT. ANN. § 362.2-801(3)(b) (LexisNexis 2006); see also § 362.2-401. Cf. § 362.487(4) (limited partnership will dissolve unless partners vote to continue it).

\(^{419}\) KY. REV. STAT. ANN. § 362.2-801(4) (LexisNexis 2006); see also § 362.2-301.

\(^{420}\) KY. REV. STAT. ANN. § 362.2-801(5) (LexisNexis 2006); see also § 362.2-809.

\(^{421}\) KY. REV. STAT. ANN. § 362.2-802 (LexisNexis 2006). This is the same standard as that applied in KyRULPA. See § 362.489. This provision is referenced in § 362.2-110(2)(i), which proscribes any effort in the partnership agreement to “vary the right of a court to decree dissolution in the circumstances specified in KRS 362.2-802.” § 362.2-110(2)(i). The partnership agreement may add additional bases for seeking judicial dissolution. Whether the partnership agreement may require the arbitration of whether “it is not reasonably practicable to carry on the activities of the limited partnership in conformity with the partnership agreement” is open to dispute. While the official comment in ULPA § 110(b)(9) (2001) indicates that arbitration of such disputes is proper, there exists case law to the contrary. See, e.g., Sivsa Entmt’v. World Int’l Network, No. B164377, 2004 WL 1895080 (Cal. Ct. App. Aug. 25, 2004); Willie Gary LLC v. James & Jackson, No. 1781, 2006 WL 75309 (Del. Ch. Jan. 10, 2006).

\(^{422}\) KY. REV. STAT. ANN. § 362.2-803(1) (LexisNexis 2006); accord § 271B.14-050(1); § 275.300(2); § 362.1-802(1); see also § 362.2-202(2)(c); § 362.2-803(2)(a).

\(^{423}\) KY. REV. STAT. ANN. § 362.2-803(2)(b) (LexisNexis 2006).
partnership. That person has agency authority on behalf of the limited partnership and is required to change the amendment of the certificate of limited partnership to state that the limited partnership has no general partner and identify themselves as the person appointed to wind it up. Judicial supervision of the winding up may be ordered where there is no general partner and no person is appointed to oversee the winding up within a reasonable time or at any other time the applicant shows good cause.

After dissolution, an action of a general partner or a person appointed to oversee the winding up will bind the limited partnership if the action is appropriate for the winding up or as to persons who do not have notice of the dissolution, if it would be appropriate to bind the limited partnership in its ordinary course. After dissolution, a dissociated general partner binds a limited partnership for up to two years or such shorter period ending upon notice of the dissociation on an act appropriate for the winding up or as to those without notice of the dissolution on an act that would have been appropriate to bind the partnership in its ordinary course. A general partner with knowledge of the dissolution that causes the limited partnership to incur an obligation other than one appropriate for the winding up, or a dissociated general partner binding the limited partnership on any obligation, is liable to the limited partnership for all resulting damages incurred by the partnership and any other current or dissociated general partner.

Known claims against the dissolved limited partnership may be addressed and disposed of by notice from the limited partnership to the creditor. A claimant must respond to the notice and file a claim within the defined time

424. KY. REV. STAT. ANN. § 362.2-803(3) (LexisNexis 2006).
425. KY. REV. STAT. ANN. § 362.2-803(3)(a) (LexisNexis 2006); see also § 362.2-804. Cf. § 362.491 (in absence of a general partner, the limited partners are empowered to oversee winding up). A person appointed, in the absence of a general partner, to oversee the winding up of the limited partnership is not a general partner and is not subject to § 362.2-408. See ULPA § 803 cmt. (2001).
426. KY. REV. STAT. ANN. § 362.2-803(3)(b) (LexisNexis 2006); see also § 362.2-202(2)(c) (LexisNexis 2006).
428. KY. REV. STAT. ANN. § 362.2-804(1) (LexisNexis 2006); see also § 362.2-402(1).
429. KY. REV. STAT. ANN. § 362.2-804(2) (LexisNexis 2006); see also § 362.2-606.
430. KY. REV. STAT. ANN. § 362.2-805 (LexisNexis 2006).
431. Known claims do not include contingent claims or those based on an event occurring after the effective date of dissolution. KY. REV. STAT. ANN. § 362.2-806(4) (LexisNexis 2006); accord § 271B.14-060(4); § 275.320(4).
432. KY. REV. STAT. ANN. § 362.2-806 (LexisNexis 2006). The notice must be in a record and must set forth the requirements of the claim, provide a mailing address to which a claim is to be sent, state a deadline for receipt of claims, which deadline may not be less than one-hundred-twenty days after the claimant’s receipt of the notice, state the claims will be barred if not received within that period and unless the limited partnership was from its inception a limited liability limited partnership, state the claims against the general partners on those partnership obligations will be likewise time barred. Accord § 271B.14-060; § 275.320. This provision has no counterpart in KyRULPA.
period of not less than one-hundred-twenty days or the claim will be time barred. A claim may also be barred if the limited partnership rejects the claim and the claimant does not commence an action for its enforcement within ninety days after receipt of the notice of rejection.\textsuperscript{433} A limited partnership may as well publish notice of its dissolution and solicit creditor claims.\textsuperscript{434} The creditors whose claims may be time barred through publication are known claimants who did not receive the record notice of the dissolution, claimants who submitted a claim on which the limited partnership did not act, and claims based on a contingency or an event occurring after the effective date of dissolution.\textsuperscript{435} A claim that is not barred may be enforced to the extent of the undistributed assets of the limited partnership and the liquidating distributions made and may as well be enforced against the general partner who is liable thereon.\textsuperscript{436} However, a claim barred as to enforcement against the limited partnership is likewise barred as against any general partner.\textsuperscript{437}

A domestic limited partnership may be administratively dissolved if it does not file its annual report with the Secretary of State within sixty days after the due date, it is without a registered office or agent for sixty days, or it fails to notify the Secretary of State of changes in its registered office or registered agent.\textsuperscript{438} The Secretary of State, by a letter sent to the limited partnership at its registered office, will notify it that grounds exist for the administrative dissolution, and the limited partnership will be afforded sixty days to correct those deficiencies.\textsuperscript{439} Thereafter, the Secretary of State may administratively dissolve the limited partnership.\textsuperscript{440} A limited partnership administratively dissolved

\textsuperscript{433} Curiously, there is no requirement that the rejection of a claim be in a record.

\textsuperscript{434} KY. REV. STAT. ANN. § 362.2-807(1) (LexisNexis 2006). The notice is published at least once in a paper of general circulation in the county in which the limited partnership’s principal office or, if that office is not in Kentucky, the county in which the registered office, is located. § 362.2-807(2)(a). The published notice must describe the information required in a claim against the limited partnership and the mailing address to which it may be sent. § 362.2-807(2)(b). The published notice must also state that a claim will be time barred if no proceeding to enforce it is brought within five years of the publication and that claims against general partners will also be time barred. §§ 362.2-807(2)(c)-(d).

\textsuperscript{435} KY. REV. STAT. ANN. § 362.2-807(3) (LexisNexis 2006). Cf. § 271B.14-070(3) (claims barred two years after publication); § 275.325(3) (claims barred two years after publication unless against professional limited liability company).

\textsuperscript{436} KY. REV. STAT. ANN. § 362.2-807(4) (LexisNexis 2006).

\textsuperscript{437} KY. REV. STAT. ANN. § 362.2-808 (LexisNexis 2006). While both the KyBCA and the KyLLCA allow shareholders and members, respectively, to waive limited liability for some or all debts and obligations of the entity, § 271B.6-220(2); § 271B.2-020(2)(b)(5); § 275.150(2), neither addresses the survival (or not) of claims against responsible shareholders/members when time barred against the corporation/LLC.

\textsuperscript{438} KY. REV. STAT. ANN. § 362.2-809(1) (LexisNexis 2006); accord §§ 271B.14-200(1)-(3); §§ 275.295(1)(a)-(c).

\textsuperscript{439} KY. REV. STAT. ANN. §§ 362.2-809(2)-(3) (LexisNexis 2006).

\textsuperscript{440} KY. REV. STAT. ANN. § 362.2-809(1) (LexisNexis 2006). A copy of the certificate of dissolution is to be mailed by the Secretary of State to the limited partnership at its registered office. With respect to this provision as well as the preceding provision, providing that the Secretary of State will give notice to the limited partnership by mail to its registered office, there is
dissolved continues in existence but may carry on only those activities that are necessary to its winding up and liquidation.\textsuperscript{441} The authority of an appointed registered agent is not terminated by the administrative dissolution of a limited partnership.\textsuperscript{442} A limited partnership, having been administratively dissolved, may apply for reinstatement provided that it has not taken any action necessary to wind up and terminate its business.\textsuperscript{443} If the Secretary of State grants reinstatement to the limited partnership, the reinstatement relates back to the date of the administrative dissolution, the limited partnership may carry on with business as if the administrative dissolution never occurred.\textsuperscript{444} A denial of an application for reinstatement may be appealed to the Franklin Circuit Court.\textsuperscript{445}

In winding up its activities, the assets of the limited partnership (which for these purposes include required contributions from general partners) will be applied first to satisfy the limited partnership’s obligations to creditors, a class that may include partners as well as creditors.\textsuperscript{446} To the extent that the limited partnership has assets after satisfying creditors’ claims, those assets are to be distributed in cash or in kind amongst the partners.\textsuperscript{447} If, on the other hand, the assets of the limited partnership are insufficient to satisfy creditor claims, persons who were general partners in the limited partnership that was not a limited liability limited partnership are obligated to contribute towards the unsatisfied obligations, with the \textit{pro rata} share of the obligations being based

\textsuperscript{441} KY. REV. STAT. ANN. § 362.2-809(4); accord § 275.300(2); § 271B.14-210(3).

\textsuperscript{442} KY. REV. STAT. ANN. § 362.2-809(5) (LexisNexis 2006); accord § 275.300(3)(g); § 271B.14-210(4).

\textsuperscript{443} KY. REV. STAT. ANN. §§ 362.2-810(1), (4) (LexisNexis 2006); accord § 271B.14-220(4) (reinstatement possible if corporation has not undertaken actions necessary to its winding up). The application for reinstatement must set forth the name of the limited partnership and the effective date of the administrative dissolution, state that the grounds for the administrative dissolution either never existed or have been addressed, state that the name of the limited partnership satisfies the legal requirements and be submitted with the reinstatement penalty and the filing fee, and any delinquent annual reports. § 362.2-810(1)(a)-(d)


\textsuperscript{445} KY. REV. STAT. ANN. § 362.2-811 (LexisNexis 2006); accord § 275.295(4); § 271B.14-240.

\textsuperscript{446} KY. REV. STAT. ANN. § 362.2-812(1) (LexisNexis 2006). Unlike KyRULPA, KyULPA does not immediately subordinate claims for declared but unpaid distributions to a second tier of obligations. \textit{Compare} KY. REV. STAT. ANN. § 362.2-812(1), with § 362.493(1).

\textsuperscript{447} KY. REV. STAT. ANN. § 362.2-812(2) (LexisNexis 2006). This provision is non-uniform. Under ULPA § 812(2) (2001), all limited partnership assets are to be liquidated and the proceeds thereof distributed in cash; ULPA § 812 does not contemplate distributions in kind. The non-uniform language has been added in KyULPA to permit in kind distributions. The agreement of limited partnership may provide that, upon liquidation, all assets will be distributed in cash, and in-kind distributions will not be permitted. \textit{See} KY. REV. STAT. ANN. § 362.2-110(1) (LexisNexis 2006).
upon the right to receive distributions amongst the general partners. To the extent that a general partner does not make a required contribution obligation, the other general partners are required to satisfy that obligation, and those contributing general partners then have a claim against the general partner who is in default. The estate of a deceased general partner is liable for any contribution obligations they would have under this provision, and an assignee for the benefit of creditors or person appointed to represent their interests, as well as any other partner, may enforce these contribution obligations.

I. KyULPA Article 9 - Foreign Limited Partnerships

Article 9 of ULPA addresses the treatment of and qualification to transact business by foreign limited partnerships. A foreign limited partnership is governed as to its internal affairs and the liability of its partners, general and limited, for debts and obligations of the partnership by the law of the state under which it is organized. While differences between the laws of Kentucky and of the jurisdiction of organization are not a basis for refusing to grant a certificate of authority to transact business, a certificate of authority to transact business does not authorize a foreign limited partnership to engage in a business or exercise a power that is not available to a domestic limited partnership.

Like certain other acts, KyULPA defines not what constitutes “transacting business,” which would necessitate the requirement to qualify to do so, but

448. KY. REV. STAT. ANN. § 362.2-812(3) (LexisNexis 2006).
449. KY. REV. STAT. ANN. § 362.2-812(3)(b) (LexisNexis 2006); § 362.2-812(3)(c).
450. See KY. REV. STAT. ANN. § 362.2-812(4) (LexisNexis 2006).
452. KY. REV. STAT. ANN. § 362.2-812(6) (LexisNexis 2006).
453. See also KY. REV. STAT. ANN. § 362.2-102(9) (LexisNexis 2006) (defining “foreign limited liability limited partnership”); § 362.2-102(10) (defining “foreign limited liability limited partnership”).
454. KY. REV. STAT. ANN. § 362.2-901(1) (LexisNexis 2006); accord § 271B.15-050(3); § 275.380(1)(a). KyRULPA provided only that the law of the jurisdiction of organization would govern the liability of the limited partners, § 362.495, leaving open the question as to whether Kentucky or foreign law would govern the liability of the general partners. One consequence of the KyULPA rule is that the law of piercing the veil as it exists in the jurisdiction of organization will apply in any piercing suit that may be brought against a foreign limited partnership in Kentucky.
455. KY. REV. STAT. ANN. § 362.2-901(2) (LexisNexis 2006); accord § 275.380(1)(b). For example, the material differences between RULPA and KyULPA may not preclude a foreign limited partnership organized under an adoption of RULPA from qualifying to transact business under KyULPA.
456. KY. REV. STAT. ANN. § 362.2-901(3) (LexisNexis 2006); accord § 271B.15-050(3); § 275.380(2). As such, in that a domestic limited partnership organized under KyULPA may not render professional services, see § 362.2-104(2), neither may a foreign limited partnership qualifying to transact business under KyULPA. See also Rutledge, Holy Grail, supra note 58, at 439-43. Conceivably, however, a foreign limited partnership practicing a profession could qualify under KyRULPA as it does not preclude a professional limited partnership.
457. Whether a foreign business organization is transacting business in the state is largely a question of fact to be determined by the circumstances of each particular case. See, e.g., Etheridge
rather sets forth a non-exclusive list of certain acts that do not constitute transacting business. The act makes clear that owning income producing real or personal property, unless otherwise excluded, will constitute transacting business and that what constitutes “transacting business” does not apply to determine whether a foreign limited partnership is subject to service of process, taxation, or other regulation by Kentucky.

A foreign limited partnership that is transacting business in Kentucky applies for a certificate of authority by filing an application with the Secretary of State. In addition to the information required by the act, the application must be

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v. Grove Mfg. Co., 287 F. Supp. 437 (W.D. Ky. 1968). The phrase “doing business” is not a technical term but should be read as ordinary words having their ordinary meaning. See WSAZ, Inc. v. Lyons, 254 F.2d 242 (6th Cir. 1958). In the only modern (i.e., within the last 25 years) published case decided on the issue, the Kentucky Court of Appeals held that a foreign corporation was not transacting business in Kentucky where it: (i) sanctioned steeplechase races, (ii) collected in New York race entry materials and prepared booklets and identification badges and (iii) rented and delivered, but did not set up, race related equipment. Commonwealth ex rel. Stephens v. Nat’l Steeplechase & Hunt Ass’n, Inc., 612 S.W.2d 347 (Ky. Ct. App. 1981).

459. KY. REV. STAT. ANN. § 362.2-903 (LexisNexis 2006); accord § 271B.15-010(2); § 275.385(2). KyULPA does not include in the list of activities that do not constitute transacting business “owning, without more, real or personal property.” Cf. § 271B.15-010(2)(i); § 275.385(2)(i).
460. KY. REV. STAT. ANN. § 362.2-903(2) (LexisNexis 2006).
461. KY. REV. STAT. ANN. § 362.2-903(3) (LexisNexis 2006); see also Intercargo Ins. Co. v. B.W. Farrell, Inc., 89 S.W.3d 422, 427 (Ky. Ct. App. 2002) (Louisiana performance bond issuer subject to long-arm jurisdiction where bond signed in Kentucky following board meeting in Kentucky authorizing bond and issuer used letterhead of an affiliate with a Kentucky address); Ky. Dep’t of Educ. v. Gravitt, 673 S.W.2d 428, 432 (Ky. Ct. App. 1984) (foreign corporation that agreed to modify van in Kentucky [most likely an isolated transaction or a transaction in interstate commerce] subject to long-arm jurisdiction); Nat’l Steeplechase, 612 S.W.2d at 348–49 (association whose activities did not require qualification to transact business subject to service of process under the long-arm statute); Mich. Wis. Pipeline Co. v. Commonwealth, 474 S.W.2d 873, 875 (Ky. 1971) (foreign corporation with property in Kentucky, while subject to taxation and jurisdiction in Kentucky, was not required to qualify to transact business where all activities were in interstate commerce).
462. The application must set forth: the name of the foreign limited partnership, which name must comply with KY. REV. STAT. ANN. § 362.2-108, or, if it does not, a fictitious name adopted as provided in § 362.2-905; the name of the jurisdiction under whose law the limited partnership is organized; its principal office address and other addresses required by the jurisdiction of organization; the street address of the initial registered office in Kentucky and the name of the registered agent at that office; the name, street and mailing address of each general partner; and a statement as to whether the foreign limited partnership is a foreign limited liability limited partnership. KY. REV. STAT. ANN. § 362.2-902(1) (LexisNexis 2006); accord § 271B.15-030(1); § 275.395(1). Applications for a certificate of authority need to be corrected or amended to keep the information therein current. § 362.2-908; accord § 271B.15-040; § 275.400. If a foreign limited partnership holding a certificate of authority changes its name to one that does not meet the requirements of KyULPA, it may not transact business in Kentucky until it receives an amended certificate of authority issued under a fictitious name. § 362.2-905(2); accord § 271B.15-400(1)(a); § 275.400(1)(a). A limited partnership that has an appointed registered agent may also be served through the Secretary of State in accordance with the long-arm statute. See, e.g., Haven Point Enters., Inc. v. United Ky. Bank, Inc., 690 S.W.2d 393, 394 (Ky. 1985) (service of process on Secretary of State in accordance with long-arm statute, even where foreign corporation had a
accompanied by the equivalent of a certificate of existence from the foreign limited partnership’s jurisdiction of organization and the consent of the initial agent for service of process to serve in that capacity. Assuming the application is complete and the filing fee properly paid, the Secretary of State will return to the foreign limited partnership a certificate of authority to transact business. The attorney general may bring an action against a foreign limited partnership that is transacting business without authority.

A certificate of authority to transact business may be revoked by the Secretary of State if the foreign limited partnership does not file its annual report, is without a registered office or agent, or fails to notify the Secretary of State of changes in the registered office or agent or if the foreign limited partnership is dissolved or ceases to exist by reason of a merger. The Secretary of State will notify the foreign limited partnership that grounds exist for the revocation of the certificate of authority, give it sixty days to respond, and thereafter may revoke the certificate of authority, whereupon the authority of the foreign limited partnership to transact business in Kentucky ceases. The revocation of a certificate of authority shall appoint the Secretary of State as the foreign limited partnership’s agent for service of process for claims arising during the period it was qualified to transact business, but the revocation does not terminate the authority of the appointed registered agent.

A foreign limited partnership, having received a certificate of authority, may cancel the qualification by filing a certificate of cancellation with the Secretary of State. The cancellation of a certificate of authority will not terminate the registered agent/office in Kentucky, was effective and conferred personal jurisdiction); Star Elk horn Coal Co. v. Red Ash Pocahontas Coal Co., 102 F. Supp. 258 (E.D. Ky. 1951); Ford Motor Credit Co. v. Nantz, 619 S.W.2d 709 (Ky. Ct. App. 1980); Dakota Enters., Inc. v. Carter, No. 2001-CA-002417-MR, 2003 WL 21241656 (Ky. Ct. App. May 30, 2003).

463. KY. REV. STAT. ANN. § 362.2-902(2) (LexisNexis 2006); accord § 271B.15-030(2). Cf. § 275.395(1)(g) (for foreign LLC, application need only include a statement that foreign LLC exists without requirement of official certificate). KyRULPA does not require either a certificate of existence or a statement as to its good standing under the laws of the jurisdiction of organization. § 362.497.

464. KY. REV. STAT. ANN. § 362.2-902(3) (LexisNexis 2006); accord § 271B.15-030(3); § 275.395(2); § 362.497(3); § 362.1-117(2).

465. KY. REV. STAT. ANN. §362.2-904 (LexisNexis 2006); accord § 362.499. Filing fees are set forth in § 362.2-122.

466. KY. REV. STAT. ANN. § 362.2-910 (LexisNexis 2006); accord § 362.509; § 362.1-1105.

467. See KY. REV. STAT. ANN. § 362.2-904 (LexisNexis 2006).

468. KY. REV. STAT. ANN. § 362.2-906; accord § 271B.15-300; § 275.400.

469. KY. REV. STAT. ANN. §§ 362.2-907(1)-(3) (LexisNexis 2006); accord § 271B.15-310; § 275.445. A foreign limited partnership whose certificate of authority is revoked may appeal to the Franklin Circuit Court. §§ 362.2-907(6)-(8).


471. KY. REV. STAT. ANN. § 362.2-909 (LexisNexis 2006); accord § 271B.15-200; § 275.435.
Secretary of State’s authority to serve as agent for service of process for causes of action arising from having transacted business in Kentucky.

J. KyULPA Article 10 - Actions by Partners

Article 10 of ULPA, titled “Actions by Partners,” addresses direct and derivative actions brought in limited partnerships. The partnership agreement may not “unreasonably” restrict the right to bring such an action. A direct action may be brought by a partner against another partner or the partnership to protect that partner’s rights or interests under the partnership agreement, KyULPA or independently of the partnership relationship, but the plaintiff is required to plead and prove an injury that is not solely the consequence of an injury to the limited partnership. A derivative action may be brought by any partner to enforce a right of the limited partnership provided that demand has been made upon the general partners and they have not done so within a reasonable time and that the partner bringing the action was a partner at the time of the conduct giving rise to the cause of action or is the successor by operation of law of one who was a partner. Save for the recovery of expenses and reasonable attorneys fees expended in a successful derivative action, all proceeds of a derivative action are property of the limited partnership on whose behalf the action was brought and not of the plaintiff bringing the action on behalf of the limited partnership.

K. KyULPA Article 11 - Conversion and Merger

Article 11 of KyULPA sets forth the terms and conditions under which a limited partnership may merge with or convert into another form of business

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475. Ky. Rev. Stat. Ann. §§ 362.2-1002-1003 (LexisNexis 2006). The complaint must “with particularity” recite the date and content of the demand made on the general partner(s) and the response thereto. § 362.2-1004; accord § 271B.7-400(1); § 362.513 (ownership requirement); § 271B.7-400(2) (demand requirement). While there is no requirement that the demand is in writing, such is advisable in order that this requirement, if need be, may be satisfied. KyRULPA permitted a derivative plaintiff to proceed without making a demand upon the general partners where the demand would be not likely to succeed, in effect a futility argument. See Ky. Rev. Stat. Ann. § 362.511 (LexisNexis 2002); § 362.515; accord § 271B.7-400(2). While neither ULPA nor KyULPA contains an “adequate representation” requirement for the limited partner bringing a derivative action, cf. Ky. Rev. Stat. Ann. § 271B.7-400(1) (LexisNexis 2003), Fed. R. Civ. P. 23.1 does impose such a rule, and a court may find that one should be imposed as a matter of common law.

organization. These provisions have been substantially modified from the
uniform act in order to remain consistent with provisions adopted in 1994
addressing mergers and conversions between general partnerships, limited
partnerships and limited liability companies. The provision begins with a
series of defined terms that are used exclusively in Article 11. With respect to
conversions, those that are provided for are of:

- Partnership into a limited partnership;
- Limited partnership into a partnership;
- Limited partnership into a limited liability company; and
- Limited liability company into a limited partnership.

With respect to the conversion of a limited liability company into a limited
partnership, the plan of conversion must be in a record and must set forth: the
name of the LLC; the name of the limited partnership into which it will be
converted; the terms and conditions of the conversion, including how the interest
in the converting limited liability company will be treated in the converted
limited partnership; and the organizational documents of the converted limited
partnership. This express provision with respect to the requirement of a
writing for the conversion of an LLC into a limited partnership necessarily
precludes an oral plan of conversion. Of course, while other conversions do not
mandate that the plan of conversion be set forth in a writing, such is always
advisable.

In order to be approved by a converting limited partnership, the plan of
conversion must be approved by all partners in the converting limited
partnership. While the agreement of limited partnership may provide for the
approval of the conversion by less than unanimous consent of all partners,
protections exist for those who, subsequent to the conversion, will be generally
liable for the debts and obligations of the converted entity. A plan of
conversion, after approval, may be amended or abandoned as provided therein or

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by that same vote of the partners as was necessary for its approval. In the non-uniform provision, it is made express that no partner has the right to dissent from a conversion unless that right of dissent is set forth in the partnership agreement.

When the conversion is of a limited liability company into a limited partnership, a certificate of limited partnership must be delivered to the Secretary of State setting forth the information otherwise required for a certificate of limited partnership, as well as a statement that the limited liability company has been converted into a limited partnership, the name of the converting limited liability company and its jurisdiction of organization, the effective date of the conversion, statement that the conversion was approved as required by the statute governing the converted LLC, and if the converted limited liability company is a foreign limited liability company not authorized to transact business in Kentucky, the address to which service served upon the Secretary of State may be forwarded. The conversion of the limited liability company into a limited partnership is effective when the certificate of limited partnership takes effect. A converted organization remains the same entity both before and after the conversion. Upon a conversion taking effect, all property and contract rights, as well as all other rights, privileges and immunities of the converting entity become those of the converted entity without assignment, reversion or impairment, the obligations of the converting entity are the obligations of the converted entity, an action or proceeding against the converting entity may be continued as if the conversion had not occurred, and the name of the converted entity may be substituted in that pending action or proceeding in place of the name of the converting entity, and any written partnership agreement shall be binding upon each person who becomes a partner in the converted partnership. A converted entity organized outside the Commonwealth of Kentucky is deemed to have consented to the jurisdiction of the courts of Kentucky to enforce any obligations of the converting limited partnership if it was in Kentucky subject to suit on that obligation. In a nonuniform provision, although one simply

repetitious of other provisions of KyULPA, one who, by reason of a conversion, becomes a general partnership in a limited partnership that is not itself a limited liability limited partnership will be liable on only those obligations of the limited partnership incurred after the conversion.\textsuperscript{494}

Limited partnerships are authorized to merge with domestic or foreign partnerships, limited partnerships, limited liability companies or corporations, provided that, with respect to any domestic limited partnership that is a party to the merger, the merger is properly approved and is not forbidden by the partnership agreement, that with respect to each domestic partnership, limited liability company or corporation, the applicable controlling laws have been satisfied, and that any foreign entity party to the merger properly complies with its governing laws.\textsuperscript{495} There must exist a written plan of merger setting forth the name of each business entity participating in the merger and name of the entity surviving the merger, the terms and conditions of the proposed merger including a statement as to whether limited liabilities retained by the surviving business entity, the manner of conversion of interest in the various entities and to those of the surviving entity or into cash or other property, amendments to the publicly filed organizational documents of any limited liability company, corporation or limited partnership that is surviving the entity, and such additional terms as are deemed necessary or desirable.\textsuperscript{496} Unless the partnership agreement provides otherwise, the plan of merger must be approved by all of the partners.\textsuperscript{497} A plan of merger may provide for the manner in which it may be amended before the articles of merger were filed with the Secretary of State, as well as the means by which it may abandoned or subject to contractual right, and in the absence of such a provision it may be abandoned or amended by that vote necessary for its initial approval.\textsuperscript{498} In a non-uniform provision, there exists no right of dissent from a merger except as may be set forth in the partnership agreement.\textsuperscript{499}

While the statutory language with respect to the approval of a merger does not specifically do so, as contrasted with the language with respect to the

\begin{itemize}
\item \textsuperscript{494} KY. REV. STAT. ANN. § 362.2-1105(4) (LexisNexis 2006); see also § 362.2-404(2); accord § 275.370(5).
\item \textsuperscript{495} KY. REV. STAT. ANN. § 362.2-1106 (LexisNexis 2006). This provision is entirely non-uniform.
\item \textsuperscript{496} KY. REV. STAT. ANN. § 362.2-1106(2) (LexisNexis 2006); accord KY. REV. STAT. ANN. § 275.355 (LexisNexis 2003).
\item \textsuperscript{497} KY. REV. STAT. ANN. § 362.2-1107(1) (LexisNexis 2006). Cf. KY. REV. STAT. ANN. § 275.370(2) (LexisNexis 2003) (providing, in part, that conversion of a limited partnership into a limited liability company must be approved by all the partners “notwithstanding any provision to the contrary in the limited partnership agreement”). KY. REV. STAT. ANN. § 362.2-1108(1)(a) (LexisNexis 2006), as adopted, contains a typographical error; the first “of” in the provision should read “and.”
\item \textsuperscript{498} KY. REV. STAT. ANN. § 362.2-1107(3) (LexisNexis 2006).
\item \textsuperscript{499} KY. REV. STAT. ANN. § 362.2-1107(4) (LexisNexis 2006). This provision is based upon the Delaware LLC Act. See DEL. CODE ANN. tit 6, § 18-210 (2006); accord KY. REV. STAT. ANN. § 275.030(6) (LexisNexis 2006); § 275.345(3); § 275.350(4).
\end{itemize}
approval of a conversion, the approval of a merger, notwithstanding a provision of the partnership agreement allowing less than the approval of a merger by less than unanimous vote of all partners, remains subject to the provision that the approval is not effective without the approval of those partners who will become personally liable to the debts and obligations of the surviving entity. 500

After the plan of merger is approved by each constituent organization, the surviving entity is to deliver to the secretary of state articles of merger executed by each party to the merger and setting forth the name and jurisdiction of organization of each entity that is a constituent party to the merger, the plan of merger, the name of the business entity surviving the merger, a statement that the plan of merger was duly authorized by each constituent business entity in accordance with its governing law, and if the surviving entity is not organized in Kentucky, a statement that it agrees that it may be served with process in Kentucky in a proceeding to enforce any obligation of party to the merger that was organized in Kentucky as well as for the enforcement of its obligations arising from the merger and the appointment of the Secretary of State as its agent for service process in any such proceeding. 501 The merger takes effect upon the effective filling of the articles of merger. 502 Upon filing, the articles of merger cancel the Certificate of Limited Partnership of any limited partnership that does not survive the merger. 503 On a merger taking effect, the separate existence of any domestic limited partnership other than a domestic limited partnership surviving the merger, ceases, and the title of all real estate and other property of any domestic limited partnership party to the merger and not surviving it becomes vested in the surviving entity without reversion or impairment, the surviving entity takes on responsibility for liabilities of each domestic limited partnership that is a party to the merger, any proceeding pending against a domestic limited partnership that is a party of the merger may be continued against the surviving entities, and the name of the surviving entities may be substituted in that proceeding, the certificate of limited partnership, as well as the agreement of limited partnership, if it is the entity surviving the merger, as amended to the extent provided in the plan of merger and the conversion in the

501. Ky. Rev. Stat. Ann. § 362.2-1108(1) (LexisNexis 2006). Furthermore, if the entity surviving the merger is a foreign partnership, limited partnership or limited liability company, the surviving entity is liable for any obligation of payment to dissenting shareholders under subchapter 13 of the KyBCA, and appoints the secretary of state as its agent for service of process with respect to the enforcement thereof. § 362.2-1108(3)
503. Ky. Rev. Stat. Ann. § 362.2-1108(5) (LexisNexis 2006). This rule is in contrast to that set forth at § 275.370, which requires that the certificate of limited partnership be cancelled before the conversion into an LLC, § 275.370(3)(d), and that the conversion is effective upon the cancellation of the certification of limited partnership, § 275.370(4), and is consistent with Ky. Rev. Stat. Ann. § 362.541(5).
interest of the various constituents to the merger are converted as provided in the plan of merger.\footnote{504}

The deletion from a certificate of limited partnership that it is a limited liability limited partnership must have the approval of all general partners unless the limited partnership agreement provides that amendment may be made by the consent of less than all the general partners, which authorization for a less than unanimous approval of the deletion may be utilized if and only if the general partner consented to that provision,\footnote{505} and that consent does not exist merely because the partner has agreed that the partnership agreement may be amended by the consent of less than all partners.\footnote{506}

Neither a conversion nor a merger of the limited partnership will discharge any current or former general partner from liability for the debts and obligations of the limited partnership, but at the same time various rights with respect to discharge and contribution are retained.\footnote{507} Furthermore, the lingering apparent agency of general partners of a limited partnership taking part in a conversion or merger otherwise itself is recognized, and where the limited partnership was not an LLLP, the partner remains personally liable after the merger to third parties if they did not have notice of the conversion or merger and had reasonable belief that they were doing business with a limited partnership that is not a limited liability limited partnership properly represented by that person as a general partner.\footnote{508} Furthermore, the former general partners of a limited partnership taking part in a merger or conversion may continue to bind the surviving entity to third parties who do not have notice of the conversion or merger and who reasonably believe that they are dealing with a limited partnership and that the person with whom they are dealing is a general partner thereof.\footnote{509}

The provisions set forth in KyULPA with respect to the mergers and conversions of limited partnership are permissive and are not mandatory, and limited partnerships may take part in similar transactions under such other means as may be provided by other laws.\footnote{510}

\begin{footnotes}
\footnote{504}{KY. REV. STAT. ANN. § 362.2-1109 (LexisNexis 2006); accord KY. REV. STAT. ANN. § 275.365; § 271B.11-060 (LexisNexis 2003). The conversion of any of a partnership, limited partnership, corporation, or limited liability company into a partnership, limited partnership, corporation, or limited liability company, or any merger of any combination of partnerships, limited partnerships, corporations, or limited liability companies, is exempt from the real estate transfer tax otherwise imposed by KY. REV. STAT. ANN. § 142.050(2) (LexisNexis 2006). See § 142.050(7)(h).}
\footnote{505}{KY. REV. STAT. ANN. § 362.2-1110(2) (LexisNexis 2006).}
\footnote{506}{KY. REV. STAT. ANN. § 362.2-1110(3) (LexisNexis 2006).}
\footnote{507}{KY. REV. STAT. ANN. § 362.2-1111 (LexisNexis 2006).}
\footnote{508}{KY. REV. STAT. ANN. § 362.2-1111(2) (LexisNexis 2006).}
\footnote{509}{KY. REV. STAT. ANN. § 362.2-1112 (LexisNexis 2006); accord § 362.1-404(6).}
\footnote{510}{KY. REV. STAT. ANN. § 362.2-1113 (LexisNexis 2006); accord § 362.1-908.}
\end{footnotes}
L. KyULPA Article 12 - Miscellaneous Provisions

Article 12 contains a series of “miscellaneous,” but at times still crucial provisions. First, it is directed that this act be applied and interpreted so as to promote uniformity among the states. 511 The official name of KyULPA, the “Kentucky Uniform Limited Partnership Act (2006),” is provided. 512 Severability is provided for. 513 The effective date for newly formed partnerships and the application of KyULPA to pre-existing partnerships, a topic already discussed, is addressed. 514 Last, it is specified that KyULPA does not affect actions or rights commenced or accrued prior to it taking effect. 515

III. ARE WE FINALLY DONE?

It certainly would be nice if, with the adoption of RUPA and ULPA, we could say that Kentucky’s menu of organizational laws were up to date and we may for the time being expect the law to stabilize. Alas, such is not to be. Business organization law continues to develop at a dizzying pace. 516 Both already existing 517 and in-progress uniform business organization acts 518 will need to be considered for adoption in Kentucky. Updates to the KyBCA and the KyLLCA 519 will need to be drafted and adopted. There has been released a new model non-profit corporation act that needs to be considered. Junction box transaction statutes will continue to develop 520 and may be appropriate for adoption, and the future model of a unified business entity code remains a possibility. 521 Still, while much work remains to be done even after the adoption

511. KY. REV. STAT. ANN. § 362.2-1201 (LexisNexis 2006); accord § 362.165(4); § 362.519; § 362.1-1201.
512. KY. REV. STAT. ANN. § 362.2-1202 (LexisNexis 2006).
513. KY. REV. STAT. ANN. § 362.2-1203 (LexisNexis 2006); accord § 362.1-1203; § 271B.17-040.
514. KY. REV. STAT. ANN. § 362.2-1204 (LexisNexis 2006); accord § 362.1-1204.
515. KY. REV. STAT. ANN. § 362.2-1205 (LexisNexis 2006); accord § 362.1-1205; § 271B.17-030(1)(b); § 271B.17-030(1)(d); see also § 362.525.
519. Since its adoption in 1988, the KyBCA has not been regularly reviewed and as appropriate, updated to the evolving Model Business Corporation Act. Bills proposing modest updates to this law as well as the LLC Act, both submitted to the 2006 General Assembly, were not taken up. H.B. 349, 350. NCCUSL, in the summer of 2006, completed and approved the Revised Uniform Limited Liability Company Act, 6A U.L.A. 213 (Supp. 2007), and the Committee on Partnerships and Unincorporated Business Organizations of the Section of Business Law, American Bar Association, is drafting a new Prototype Limited Liability Company Act.
520. E.g., MODEL ENTITY TRANSACTIONS ACT, 6A U.L.A. 2 (Supp. 2007).
of KyRUPA and KyRULPA, Kentucky has taken a significant step forward in moving to the forefront of states having modern business organization laws.

IKENTUCKY BLUE SKY LAW: A PRACTITIONER’S GUIDE TO KENTUCKY’S REGISTRATIONS AND EXEMPTIONS

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I. INTRODUCTION

Securities play a unique role in our society. Like traditional goods, they are bought, sold, and marketed by both individuals and businesses. Unlike traditional goods, however, securities do not have any intrinsic value in themselves, but rather they represent rights in something else. Their value is derived on the profitability or future prospects of the corporation or other entity which issued them, and, to a larger extent, how much people are willing to pay for them based on their evaluation of those prospects. Additionally, because securities are issued, rather than produced, they can be issued in unlimited amounts and virtually without cost. Due to these distinguishing characteristics, governmental regulation of securities focuses on assuring that when securities are created and offered to the public, investors are receiving all material information of what they are purchasing.

In Kentucky, as is the case in virtually every state, the regulation of securities offerings is centered on the process of registration, or an exemption therefrom. This article examines the law of registrations and exemptions in Kentucky. It is intended to be a quick reference guide for practitioners when confronting some of the common questions arising in a transactional securities practice. Section II of this article provides an introduction to securities practice in Kentucky, and its interaction with federal securities laws in general. Section III addresses the specific registration exemptions available in Kentucky, and offers some practical advice for those using one of the many exemptions. Section IV provides an in-depth discussion on the three methods of registration in Kentucky (notification, coordination, and qualification), Section V highlights Kentucky’s antifraud provisions, and Section VI sets forth a conclusion.

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II. BACKGROUND

A. History of Kentucky Blue Sky Law

Kentucky is one of many states to have adopted laws governing transactions involving securities, or “blue sky laws.” The purpose of adopting a blue sky law is to prevent the sale of fraudulent securities to unsophisticated investors. The name originated from a depiction of the type of scheme the laws were intended to prevent; that is “speculative schemes which have no more basis than so many feet of ‘blue sky.’” Kentucky’s blue sky law and all other blue sky laws owe their origin to Kansas Banking Commissioner J.N. Dolley, who is credited with developing blue sky legislation in 1911. Under Dolley’s guidance, the Kansas legislature passed legislation making Kansas the first state to adopt a law that required issuers to disclose various financial statements to the Banking Commissioner. Under this law, the Banking Commissioner had the power to reject an offering if he thought an issuer did not plan on doing honest business or offer a reasonable return to investors. Kentucky followed the lead of Kansas, and in 1920 enacted the Commonwealth’s first blue sky law, which was codified in sections 883e1 to 883e26 of the Kentucky Acts of 1920. The purpose of enacting this statute was to protect investors “against the sale of worthless money obligations.”

The current version of the Kentucky Securities Act (the “Act”) is based directly from the Uniform Securities Act of 1956, which was enacted by Kentucky in 1960. The most recent notable amendment to the Act occurred in

2. Id.
4. Mahoney, supra note 1, at 231.
5. Id.
6. Id.
7. Lewis v. Creasey Corp., 248 S.W. 1046, 1047 (Ky. 1923). See also Mahoney, supra note 1, at 232.
8. Lewis, 248 S.W. at 1049. The Court stated: [T]he primary purpose of Blue Sky Laws is to protect investors from investments in securities whereby a profit is promised and expected without any active efforts on the part of the investor, and which scheme contemplates that the company or individual who receives the investment will employ it himself or itself in such a manner as to reap a profit to the holder of the sold security; and that it was not intended to apply to contracts containing mutual obligations, such as are daily entered into in commercial life, and from which a profit can only be reaped by the uses which the investor alone makes of them. See also KY. REV. STAT. ANN. § 292.530 (West 2006).
1998 in response to the then-recently enacted National Securities Markets Improvement Act of 199610 ("NSMIA").11 These amendments were made after a year long review of what was essentially the 1956 Uniform Securities Act.12 Not only were amendments made to the Act, but also comprehensive revisions were made to the rules and regulations promulgated thereunder (the "Regulations").13

While the amendments were substantial, a few stand out as noteworthy.14 One of the amendments involved when a private claim must be initiated.15 Prior to the amendments, securities claims had to commence within three years of the "contract of sale."16 Kentucky amended this provision for the purpose of granting plaintiffs more time to bring their claim.17 Together with a later 2001 amendment, the Act now provides that plaintiffs may bring a cause of action for violations of the antifraud provisions so long as such actions are brought within three years of the plaintiff discovering, or in the exercise of reasonable care should have discovered, the "act, omission, or transaction,"18 that constituted the violation.19 The amendments in 2001 changed the timing of when an action under the statute accrues from the date of sale to a discovery rule.20 As a result, plaintiffs’ lawyers faced with a statute of limitations issue involving an antifraud violation now should focus on the date of the plaintiff’s injury.21

Another noteworthy revision following from the 1998 amendments was modernizing Kentucky’s limited offering exemption to make it self-executing.22 As a result of the 1998 amendments, filings are no longer required with

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securities law should be construed in harmony with federal securities law partly because an independent construction would encourage forum shopping).


12. Id. at 10.

13. See id.

14. See id. at 11-14.

15. Id. at 12.

16. See id; See also Ky. Rev. Stat. Ann. § 292.480(3) (West 1972) (amended 1998) (providing in part: No person may sue under this section more than three years after the contract of sale); See also Huto v. Bockweg, 579 S.W.2d 382, 385 (Ky. Ct. App. 1979) (holding that a shorter statute of limitations under the Act was constitutional).

17. Id; See Lewis, supra note 11, at 10-14.

18. Ky. Rev. Stat. Ann. § 292.480(5) (West 2006) (“No person may sue under this section more than three years after the date the occurrence of the act, omission, or transaction constituting a violation of this chapter was discovered, or in the exercise of reasonable care should have been discovered”).

19. Id. (In 2001, amendments were enacted that tolled the statute of limitations to three years after the date that the violation was discovered, or in the exercise of reasonable care should have been discovered; See also Lewis supra note 11, at 12.


Kentucky’s Division of Securities as long as, among other things, the issuer does not offer or sell securities to more than 15 purchasers (which limitation excludes “accredited investors” as defined in Rule 501 of the Securities Act),23 or the aggregate offering price of the securities, including securities sold outside of Kentucky, does not exceed $1,000,000 and the total number of purchasers (excluding “accredited investors”) does not exceed 35.24

B. Administration

To understand Kentucky’s blue sky law, it is helpful to understand who is in charge of its enforcement. The Office of Financial Institutions, through its Division of Securities (“Division”), is charged with its administration.25 The Division has four principal resources to protect the public under the Act.26 First, the Division has the power to investigate potential fraud.27 Second, the Division can issue a cease and desist order if an issuer has unlawfully issued securities without registration in Kentucky.28 Third, the Division can institute an action in court for an injunction if its orders are not complied with.29 Fourth, the Division

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24. Ky. Rev. Stat. Ann. § 292.410(1)(i)(3)(c) (West 2006); See also Lewis supra note 11, at 14; See also Blue Sky L. Rep. (CCH) ¶ 27,112 at 22,123 (noting the increase to the offering price from $500,000 to $1,000,000 at subsection (1)(i)(3)(b)).

25. Ky. Rev. Stat. Ann. § 292.500(1) (West 2006); See also Lewis supra note 11, at 10-14; See also Target Oil & Gas Corp. v. Commonwealth, No. 2004-CA-01947-MR, 2006 WL 1443980, at *4 (Ky. Ct. App. May 26, 2006) (holding that the executive director has the power to issue a subpoena duces tecum because it is within his statutory authority and this does not invade the company’s constitutional rights).


The executive director in his discretion: (a) May make such public or private investigations within or outside of this state as he deems necessary to determine whether any registration should be granted, denied, or revoked, or whether any person has violated or is about to violate any provision of this chapter or any rule or order under this chapter, or to aid in the enforcement of this chapter or in the prescribing of rules and forms hereunder.


Whenever it appears to the executive director that any person has engaged or is about to engage in any act or practice constituting a violation of any provision of this chapter or any rule or order under this chapter, he may in his discretion bring any or all of the following remedies: (1) Issue a cease and desist order, with or without a prior hearing, appealable to Franklin Circuit Court, against the person or persons engaged in the prohibited activities directing that person or persons to cease and desist from illegal activity. In order to issue an order without a prior hearing, the executive director must find that the delay in issuing a final cease and desist order will cause harm to the public.


Whenever it appears to the executive director that any person has engaged or is about to engage in any act or practice constituting a violation of any provision
can assess fines against persons who have violated the Act.\textsuperscript{30} If the fines are not paid, the Division’s recourse is to notify the Attorney General who will then institute an action for its recovery.\textsuperscript{31}

Although the Division actively pursues those individuals committing securities fraud upon the public, it has acknowledged that fraud still persists.\textsuperscript{32} A comment letter from the Division’s former director states, “some of the firms we regulate – particularly those headquartered out–of–state and with small satellite offices in Kentucky – demonstrate a marked nonchalance towards their supervisory responsibilities.”\textsuperscript{33} This cavalier attitude has led to the commission of frauds by agents of several of these firms . . . [and have] caused harm in the tens of millions of dollars to our citizens[.].”\textsuperscript{34} In order to prevent fraud in the Commonwealth, the Division now undertakes a routine examination of securities professionals.\textsuperscript{35}

C. Federal Securities Laws

1. Framework of Federal Securities Regulation

While the focus of this article is on Kentucky blue sky law, an understanding of these laws would be fragile at best without first considering the role and

of this chapter or any rule or order under this chapter, he may in his discretion bring any or all of the following remedies: (2) An action in the Franklin Circuit Court or any other court of competent jurisdiction to enjoin any such acts or practices and to enforce compliance with this chapter or any rule or order under this chapter. Upon a proper showing a permanent or temporary injunction, restraining order, or writ of mandamus shall be granted and a receiver or conservator may be appointed for the defendant or the defendant's assets.

30. KY. REV. STAT. ANN. § 292.500(14) (West 2006) (stating that “[t]he executive director may assess civil fines against any person who violates any provision of this chapter or any rule or order under this chapter”);

See also KY. REV. STAT. ANN. § 292.470(3)(c) (West 2006) which states

Whenever it appears to the executive director that any person has engaged or is about to engage in any act or practice constituting a violation of any provision of this chapter or any rule or order under this chapter, he may in his discretion bring any or all of the following remedies: (3) Issue a final order, after notice and an opportunity for a hearing, containing findings of fact and conclusions of law, directing any person or persons found to have engaged in, or about to be engaged in, activity that constitutes a violation of this chapter or any rule or order under this chapter (c) To pay fines assessed under KRS 292.500(14) and costs assessed under KRS 292.500(15).

31. KY. REV. STAT. ANN. § 292.500(16) (West 2006) (stating that “[i]f fines or costs assessed under this section are not paid, the executive director may notify the Attorney General who shall promptly institute an action in the name of the Commonwealth of Kentucky, in the Franklin Circuit Court for the recovery of the fines or costs”).

32. See generally, Blue Sky L. Rep. (CCH) ¶ 27,588 at 22,580 (Comment Letter, Marion H. Lewis, Director, Division of Securities) (December 8, 1998).

33. Id.

34. Id.

35. Id.
influence of federal securities laws. After the 1929 stock market crash, and in
response to abuses in the securities industry, Congress enacted two landmark
pieces of legislation to supplement state securities laws: 36 the Securities Act of
1933 (the “Securities Act”), 37 and the Securities and Exchange Act of 1934 (the
“Exchange Act”). 38 The Securities Act aims to prevent exploitation of the public
due to the sale of unsound, fraudulent, and worthless securities through
misrepresentation. 39 To this end, its main focus is on registration and offering
requirements during the primary placement of securities. 40

The Exchange Act created federal regulation of securities trading in the
secondary markets and its main focus is the regulation of those markets. 41 The
Exchange Act also established the Securities and Exchange Commission
(“SEC”) for the purposes of administering the Securities Act. 42

2. Limited Regulation of “Covered Securities”

In 1996, Congress examined the system of dual registration with the federal
and state securities authorities and came to the conclusion that some amount of
federal preemption was necessary. 43 As a result, Congress promulgated the
National Securities Market Improvement Act of 1996 (“NSMIA”). 44 Among
other things, NSMIA extensively amended Section 18 of the Securities Act to
provide that no law, rule, regulation, order, or other administrative action of any
state requiring registration or qualification of securities or securities transactions
will apply to a security that is a “covered security” or any security that will be a
covered security upon completion of the transaction. 45 NSMIA also prohibits
states, such as Kentucky, from directly or indirectly imposing conditions upon

39. S.E.C. v Koscot Interplanetary, Inc., 497 F.2d 473, 479 n.9 (5th Cir. 1974). The Fifth
Circuit noted:
The remedial purposes of the Securities Act of 1933, were expressed as follows: “The aim is to prevent further exploitation of the public by the sale of
unsound, fraudulent, and worthless securities through misrepresentation; to
place adequate and true information before the investor; to protect honest
enterprise, seeking capital by honest presentation against the competition
afforded by dishonest securities offered to the public through crooked
promotion . . . .”
Id. (quoting the Senate Committee on Banking & Currency, S. Rep. No. 47, 73d Cong., 1st Sess. 1
(1933)).
41. See generally DAVID L. RATNER & THOMAS LEE HAZEN, SECURITIES REGULATION IN A
42. Id.
43. Id.
45. Id.
the use of any prospectus and other offering document (such as a private placement memorandum) related to covered securities. While states are prohibited from imposing conditions on the use of offering documents by issuers of covered securities, states do retain the authority to investigate and bring enforcement actions with respect to fraud and deceit or unlawful conduct by brokers or dealers in connection with securities or securities transactions.

Practitioners desiring to take advantage of the preemption benefits of NSMIA must first determine whether or not the securities at issue fit within the definition of “covered securities.” The term “covered securities” is defined in Section 18(b) of the Securities Act and refers to securities that are listed on certain national stock exchanges (e.g., New York Stock Exchange), and securities that are covered because of the type of transaction involved or the nature of the issuer.


Except as otherwise provided in this section, no law, rule, regulation, or order, or other administrative action of any State or any political subdivision thereof—

(1) requiring, or with respect to, registration or qualification of securities, or registration or qualification of securities transactions, shall directly or indirectly apply to a security that—

(A) is a covered security; or

(B) will be a covered security upon completion of the transaction; (2) shall directly or indirectly prohibit, limit, or impose any conditions upon the use of—

(A) with respect to a covered security described in subsection (b) of this section, any offering document that is prepared by or on behalf of the issuer; or

(B) any proxy statement, report to shareholders, or other disclosure document relating to a covered security or the issuer thereof that is required to be and is filed with the Commission or any national securities organization registered under section 78o-3 of this title, . . . ; or

(3) shall directly or indirectly prohibit, limit, or impose conditions, based on the merits of such offering or issuer, upon the offer or sale of any security described in paragraph (1).


A security is a covered security if such security is—

(A) listed, or authorized for listing, on the New York Stock Exchange or the American Stock Exchange, or listed, or authorized for listing, on the National Market System of the Nasdaq Stock Market (or any successor to such entities); (B) listed, or authorized for listing, on a national securities exchange (or tier or segment thereof) that has listing standards that the Commission determines by rule (on its own initiative or on the basis of a petition) are substantially similar to the listing standards applicable to securities described in subparagraph (A); or

(C) is a security of the same issuer that is equal in seniority or that is a senior security to a security described in subparagraph (A) or (B).

See also Lander v. Hartford Life & Annuity Ins. Co., 251 F.3d 101, 109 (2d Cir. 2001) (holding that a variable annuity is a “covered security”).

49. See 15 U.S.C. § 77r(b) (2000); See also KY. REV. STAT. ANN. § 292.310(6) (West 2006) (stating that “Covered Security” means any security that is a covered security under Section 18(b) of the Securities Act of 1933 or rules or regulations promulgated thereunder.”); See also http://www.sec.gov/rules/final/33-8442.htm.
a. Exchange Listed Securities

NSMIA, in conjunction with Rule 146 promulgated by the SEC, provides for exclusive federal registration of securities listed, or authorized for listing, on the New York Stock Exchange, Nasdaq Global Select Market, American Stock Exchange, Tier I of the Pacific Exchange, Tier I of the Philadelphia Stock Exchange, and the Chicago Board of Options Exchange. At the time this article was written, the SEC had recently published a Release that proposed to treat securities listed on the Nasdaq Capital Market (“NCM”) (formerly known as the Nasdaq Smallcap Market) as “covered securities” under the Securities Act. The proposal stated that the SEC did not currently believe that NCM’s listing standards qualified for “covered security” status, but if proposed changes to the listing standards of NCM were adopted by the SEC, the new standards would qualify for “covered security” status. If such status is granted, securities listed on the Nasdaq Capital Market would be exempt from state law registration requirements.

b. Certain Issuers and Exempt Offerings

NSMIA’s definition of “covered securities” also provides for exclusive federal registration of securities when those securities are issued by an investment company registered, or has filed a registration statement, under the Investment Company Act of 1940. Further, NSMIA preempts state registration of transactions that are exempt from registration under federal law pursuant to Sections 4(1) and 4(3) of the Securities Act, provided the issuer files reports with the SEC pursuant to Section 13 or 15(d) of the Exchange Act. Section 4(1) is the primary exemption for secondary market transactions because it exempts from federal registration transactions by any person other than an issuer, underwriter, or dealer (each defined in the Securities Act). Section 4(3) exempts ordinary dealer transactions except those occurring immediately following a registered public offering.

NSMIA also provides a state registration preemption for transactions involving most securities covered under Section 3(a) of the Securities Act (the exempt securities section of the Securities Act). Examples of securities that are exempt from federal securities registration requirements under Section 3(a) and,

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52. Id.
53. Id.
as such, qualify for preemption from state securities registration requirements include the following: securities of banks and employee benefit plans,\textsuperscript{59} commercial paper,\textsuperscript{60} savings and loan securities,\textsuperscript{61} and insurance and annuity contracts.\textsuperscript{62}

Arguably one of the most useful additions from NSMIA was the addition of federal preemption for securities issued in connection with offerings under SEC rules or regulations promulgated under Section 4(2) of the Securities Act; however, this particular provision does not prohibit a state from imposing notice filing requirements “that are substantially similar to those required by rule or regulation under Section 4(2) that [were] in effect on September 1, 1996.”\textsuperscript{63} Currently, Kentucky requires issuers offering securities pursuant to Rule 506 to file with the Division no later than 15 days after the first sale of such security in Kentucky (1) a copy of the notice on SEC Form D, (2) a $250 filing fee, and (3) a consent to service of process signed by the issuer (i.e., Form U-2, Uniform Consent to Service of Process).\textsuperscript{64}

The benefits of this provision to practitioners are significant considering the popularity of Rule 506 of Regulation D.\textsuperscript{65} Rule 506 is presently the only federal rule providing an exemption pursuant to Section 4(2) of the Securities Act. Rule 506 is a “safe harbor” for issuers, meaning that transactions undertaken in compliance with the Rule will be considered to have been undertaken in accordance with Section 4(2) of the Securities Act.\textsuperscript{66} Among other things, Rule 506 limits the number of purchasers to no more than 35; however, “accredited investors” (as defined in Rule 501(a)) are exempted from the definition of “purchasers.”\textsuperscript{67} Additionally, each purchaser who is not an accredited investor, either alone or with his purchaser representative must have, or the issuer must reasonably believe that he has, such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment.\textsuperscript{68} This is known by some practitioners as the “sophistication” requirement.

While practitioners no longer have to worry about dual registration when the issuer’s securities fit within the definition of covered securities, practitioners still must be knowledgeable of state securities laws. This is so because many securities will not qualify for covered security status, and also because the

\begin{itemize}
\item \textsuperscript{60} 15 U.S.C. § 77c(a)(3) (2000).
\item \textsuperscript{64} KY. REV. STAT. ANN. § 292.327(2) (West 2006).
\item \textsuperscript{65} 17 C.F.R. § 230.506 (2006); See generally http://www.sec.gov/answers/rule506.htm
\item \textsuperscript{66} Id.
\item \textsuperscript{67} Id.
\item \textsuperscript{68} Id.
\end{itemize}
antifraud provisions of the particular states still govern the offers and sales of such securities.\(^69\)

D. What Is a “Security” Under the Act?

Registration under the Act only applies to an offer or sale of a “security.”\(^70\) Before diving into registrations and exemptions under the Act, it is necessary for practitioners to have a knowledgeable understanding of how Kentucky defines a “security.” Comparing Kentucky’s definition of security with that of the definition of security under the Securities Act, practitioners will inevitably see many similarities.\(^71\) Certainly, common to each definition are stocks, bonds, debentures, treasury stock, and notes.\(^72\) A distinction, however, is that Kentucky’s definition explicitly states that “‘security’ does not include any insurance or endowment policy or annuity contract under which an insurance company promises to pay a fixed number of dollars either in a lump sum or periodically for life or some other specified period.”\(^73\)

While Kentucky’s definition of “security” contains many examples of what a security is, it does not cover every financial instrument.\(^74\) In analyzing whether an interest is a security, courts in Kentucky have adopted the federal test popularly known as the \textit{Howey} test, after the famous orange grove case.\(^75\) In

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\(^69.\) See 1 Bromberg & Lowenfels on Sec. Fraud and Commodities Fraud § 2:197 (2006).
\(^70.\) KY. REV. STAT. ANN. § 292.310(18) (West 2006) defines security as:
any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, vatical settlement investment, voting-trust certificate, certificate of deposit for a security; fractional undivided interest in oil, gas, or other mineral rights; or, in general, any interest or instrument commonly known as a “security,” or any certificate of interest in or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

\(^72.\) Id.
\(^73.\) KY. REV. STAT. ANN. § 292.310(18) (West 2006).
applying the Howey test, the form of the contract, transaction or scheme involved is disregarded, and instead the focus is on the economic reality of the interest. In other words, the test is one of substance, not form.

Under the Howey test, courts look to “whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others.” Every part of the Howey test must be met in order for the interest to be a security. The Division has taken the approach of looking at the substance of the interest over the form of the interest in order to determine whether it is a security. This means that although the interest may fall within the literal reading of Kentucky’s definition of a security, the Division may still determine that it is not a security for purposes of the Act. Although the Division’s determination of whether an interest qualifies as a security is extremely important, the ultimate determination of whether an interest is a security is reserved to the court.

While it is important for practitioners to analyze whether an interest is a security on a case-by-case basis, certain interests are so common that the determination of whether an interest is a security can be established by the way the business is organized. In a no-action letter dated January 29, 1996, the Division provided helpful guidance to securities practitioners faced with the issue of whether a particular interest in an entity is considered a security.

The letter stated that generally ownership of stock in a corporation will be considered a security. On the other hand, an interest in a general partnership is usually not considered a security, as long as it is a true general partnership,
because it fails the fourth prong of the Howey test, i.e., profits derived solely from the efforts of others.87 In determining whether profits are being derived “solely from the efforts of others,” the Division stated that the number of partners involved plays a role.88 This is because there is a greater chance that some partners will be passive investors if the partnership is large.89 Also, for a partnership interest not to be considered a security, each partner must exercise their power in an independent or meaningful way.90

With respect to interests (i.e., units) in limited liability companies, the Division has taken the position that, as a general rule, such interests are securities under the Act because they are investment contracts.91 While the Division considers this the general rule, it has provided guidance as to what types of LLC interests would not be considered securities.92 Factors that indicate that an LLC unit is not a security are the following: (1) the expectation of profits comes from the joint efforts of all of the members, (2) none of the members are passive investors, and (3) the transferability or sale of a member’s interest is limited (e.g., buy-sell provision in the operating agreement).93

Although practitioners can analyze whether LLC interests are securities using the factors set forth above, a more conservative approach is to utilize the safe harbor for LLC membership interests located in Regulation 10:360.94 This Regulation provides that an LLC membership interest will not be considered a security as long as the aggregate number of members of the limited liability company do not exceed 35, and at least one of the following requirements are met: (1) each member is actively engaged in the management of the company, (2) the articles of organization or operating agreement of the LLC vest management in a manager who is a member and the articles or operating agreement provide that the managing member may be replaced by any other member through a majority vote of the members, or (3) each member is authorized to bind the LLC under applicable law or under the articles of organization or operating agreement.95 In determining whether all members are actively engaged in the business, the regulation states:

[E]vidence that members vote or have the right to vote, have the right to information concerning the business and affairs of the limited liability company, or have the right to participate in the management of the limited liability company, shall not alone

87. *Id.*
88. *Id.*
89. *Id.* at 22,569.
91. *Id.*
92. *Id.*
93. *Id.*
95. *Id.*
establish that all members are actively engaged in the management of the limited liability company.\textsuperscript{96}

In addition to the usual categories of securities (e.g., stock, partnership interests and limited liability interests), Kentucky courts have addressed whether other not-so-common interests come within the definition of “security.” An “inside shareholder fee,” which is a payment made to obtain insider stock, has been held to be a “security.”\textsuperscript{97} In \textit{Kefalas v. Bonnie Brae Farms, Inc.}, the court held that purchasers of fractional interests in thoroughbred syndications, where a right to breed a mare to a stallion was purchased, was not a security because profits derived from the venture depended on the skill of the owner as opposed to the manager of the syndication.\textsuperscript{98} Additionally, in \textit{Scholarship Counselors Inc. v. Waddle}, a scholarship trust fund was held to be a security, although characterized as a sale of services, partially because the return advertised was to come about solely from the efforts of the trust administrators.\textsuperscript{99} In \textit{Johns v. Johns}, the court held that a security distribution, which arises out of a property distribution from a divorce settlement, does not invoke the Act because it is not an offer or sale of securities.\textsuperscript{100}

**III. Exemptions to Registration**

**A. Introduction**

Registering securities under the Act is expensive and time-consuming. As such, if state registration is not preempted by NSMIA, a practitioner’s first inquiry should be whether an exemption from registration under the Act might be available. Kentucky has two basic categories of exemptions:

- those based upon the nature of the securities involved (i.e., exempt securities),\textsuperscript{101} and

- those based upon the transactions in which the securities are offered and sold (i.e., exempt transactions).\textsuperscript{102}

It is important to note that both categories provide an exemption only from the registration provisions; the antifraud provisions\textsuperscript{103} and broker-dealer registration requirements\textsuperscript{104} still apply in the offering.

\begin{itemize}
\item \textsuperscript{96} \textit{Id.}
\item \textsuperscript{97} \textit{Hutto}, 579 S.W.2d at 384.
\item \textsuperscript{98} 630 F. Supp. 6, 8 (E.D. Ky. 1985).
\item \textsuperscript{99} 507 S.W.2d 138, 142 (Ky. 1974).
\item \textsuperscript{101} KY. REV. STAT. ANN. § 292.400 (West 2006).
\item \textsuperscript{102} KY. REV. STAT. ANN. § 292.410 (West 2006).
\item \textsuperscript{103} KY. REV. STAT. ANN. § 292.440 (West 2006).
\item \textsuperscript{104} KY. REV. STAT. ANN. § 292.330 (West 2006).
\end{itemize}
B. Exempt Securities

Regulation 292.400 sets forth a list of securities that are granted exemptions from the registration requirements. These types of securities are granted such status because the nature of the issuer makes registration unnecessary or unduly burdensome in comparison to the benefits of registration to public investors. The following is a non-exclusive list of exempt securities in Kentucky:

- **Government Securities**—Any security issued or guaranteed by the United States, any state, any political subdivision of a state, or any agency or corporate or instrumentality of one or more of the foregoing, or any security issued or guaranteed by Canada or any other foreign government that the United States maintains diplomatic relations with, if the security is a valid obligation by the issuer or guarantor;

- **Banks and Savings Institutions**—Any security issued by and representing an interest in, debt of, or guaranteed by (a) any bank organized under the laws of the United States or any state, or (b) any federal savings and loan association.

- **Rural Electric and Rural Telephone Cooperative Corporations**—Any security issued by corporations formed under KRS Chapter 279;

- **Credit Unions**—Any security issued, or guaranteed by a credit union;

- **Railroads, Public Utilities, and Holding Companies**—Any security issued or guaranteed by any common carrier, public utility, or holding company which is: (a) a company registered under the Public Utility Holding Company Act of 1934, (b) regulated in respect of its rates and charges by some other governmental agency, or (c) regulated in respect of the issuance or guarantee

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of the security by the United States, a state, or Canada;\textsuperscript{112}

- Exchange-Listed Securities—Any security listed or approved for listing upon notice of issuance on the New York Stock Exchange, the American Stock Exchange, the Chicago Stock Exchange, the Pacific Stock Exchange, the Philadelphia Stock Exchange, the Chicago Board Options Exchange, or any other stock exchange approved by the commissioner;\textsuperscript{113}

- Non-Profit Organizations—Any security issued by a person organized and operated not for private profit, but exclusively for religious, educational, benevolent, charitable, fraternal, social, athletic, or reformatory purposes, or as a chamber of commerce or trade or professional association;\textsuperscript{114}

- Commercial Paper—Any commercial paper that arises out of a current transaction or the proceeds of which have been or will be used for the current transactions,

\textsuperscript{112} KY. REV. STAT. ANN. § 292.400(7) (West 2006).

\textsuperscript{113} KY. REV. STAT. ANN. § 292.400(8) (West 2006) (This exemption is available only for securities listed on Tier I of those exchanges having more than one tier. Interestingly, the NASDAQ Stock Market LLC has recently been granted “exchange” status). See NASDAQ Frequently Asked Questions, http://www.nasdaq.com/about/FAQsExchange.stm (last visited February 11, 2007). Even though the Nasdaq Global Select Market is absent from the above list of exchanges, these securities are still considered “covered securities” under Section 18 of the Securities Act; thus, are exempt from Kentucky registration. Of particular interest will be whether securities listed on the Nasdaq Capital Market will also be granted “covered security” status. See discussion supra Part IIC.2.(i).

\textsuperscript{114} Compare KY. REV. STAT. ANN. § 292.400(9) (West 2006), and 15 U.S.C. § 77c(a)(4) (2000). This exemption is not self-executing, meaning a claim of exemption must first be filed with the commissioner per KY. REV. STAT. ANN. § 292.415(1) (West 2006). 808 KY. ADMIN. REGS. 10:170 (2006) provides the following list of what is required to request this exemption in which the commissioner has 10 business days to determine whether the exemption is unavailable:

(a) A declaration that the KRS 292.400(9) exemption shall be relied upon; (b) A sample copy of the security that will be issued; (c) A copy of the Articles of Incorporation and Bylaws of the issuer or the equivalent governing instruments; (d) A prospectus, offering circular, or memorandum making full disclosure of material facts, including a discussion of all salient risk factors; (e) A representation that an offeree or purchaser shall have access to information concerning the issuer; (f) Copies of all advertising or other material to be distributed in connection with the offering; (g) A copy of the subscription agreement or other similar agreement; (h) A copy of a proposed agreement or proposed form of agreement with a securities broker-dealer or underwriter; (i) A copy of the preliminary or definitive Trust Indenture or Trust Agreement, if any.
and which evidence an obligation to pay cash within nine months of the date of issuance;\textsuperscript{115}

- Employee Benefit Plans—Any security issued in connection with an employee stock purchase plan; stock option plan; savings, pension, profit-sharing, or similar benefit plan; including any underlying security;\textsuperscript{116}

- Agricultural Cooperative Associations—Any security by a corporation formed under or which have the provisions of KRS 272.101 to 272.345;\textsuperscript{117}

- Cooperative Corporations—Memberships and voting stock issued by cooperative corporations, including corporations that are formed under or have adopted the provisions of KRS 272.020 to 272.050;\textsuperscript{118}

- Insurance Companies—Any security issued by and representing an interest in or a debt of, or guaranteed by, any insurance company organized under the laws of any state and authorized to do business in Kentucky;\textsuperscript{119} and

- Other Exempt Securities—Any security for which the commissioner expressly by rule or order finds that registration is not necessary or appropriate in the public interest for the protection of investors.\textsuperscript{120}

C. Exempt Transactions

The offer and sale of some securities is exempt from registration because of the nature of the transaction involved. A list of these “exempt transactions” is

\textsuperscript{115} KY. REV. STAT. ANN. § 292.400(10) (West 2006) (This exemption is similar to the exemption provided by Section 3(a)(3) of the Securities Act for short-term (9 months) paper, except that the federal language in 15 U.S.C. § 77c(a)(3) (2000) specifically mentions notes and drafts).

\textsuperscript{116} KY. REV. STAT. ANN. § 292.400(11) (West 2006). If the plan does not qualify under Section 401 of the Internal Revenue Code and provides for contributions by employees, the statute provides that a notice specifying the terms of the plan should be filed with the commissioner before the securities are used. By rule, this notice provision has been waived if the offer or sale qualifies for the registration exemption of 17 C.F.R. § 230.701 (2006). See 808 KY. ADMIN. REGS. 10:300 (2006).

\textsuperscript{117} KY. REV. STAT. ANN. § 292.400(12) (West 2006). Before claiming this exemption, a claim of exemption must first be filed with the commissioner. KY. REV. STAT. ANN. § 292.415(1) (West 2006); See supra note 118 for the list of what is required to request exemption.

\textsuperscript{118} KY. REV. STAT. ANN. § 292.400(13) (West 2006).


\textsuperscript{120} KY. REV. STAT. ANN. § 292.400(14) (West 2006).
provided in Section 410 of the Act.\(^{121}\) In analyzing these transactions, practitioners should not assume that all transactional exemptions are self-executing; sometimes a notice filing and fee are required to perfect the exemption. The following paragraphs describe some of the more commonly used exemptions.

1. Isolated Non-Issuer Transactions

Isolated non-issuer transactions, whether effected through a broker-dealer or not, are exempt from the registration requirements for securities.\(^{122}\) Section 310 of the Act defines “non-issuer” as not directly or indirectly for the benefit of the issuer.\(^{123}\) The Sixth Circuit Court of Appeals has held that an incidental benefit is not the same as a direct or indirect benefit.\(^{124}\) The number of sales made is also a key indication of whether the transaction falls within this exemption.\(^{125}\) While this exemption does not have any direct utility in connection with the capital raising process, it does provide a useful exemption for persons engaging in offers and sales of securities.

In a no-action letter dated May 19, 1988, the Division of Securities addressed the issue of whether customers who received a gift of securities from a developmental company would be permitted to use the isolated non-issuer exemption in the event the customers immediately resold the securities.\(^{126}\) In sum, the Division stated that such exemption would not be available unless the corporation took two steps to help stem the possibility of customers immediately reselling the securities they received.\(^{127}\) (Thus, having the appearance of the customers acting as a conduit for the company.) First, a restrictive legend had to be placed on the gifted shares stating that the shares were not registered and that they had to be registered or properly exempted before sales could be made.\(^{128}\) Second, the transfer agent had to take reasonable steps to assure that the

\(^{121}\) KY. REV. STAT. ANN. § 292.410 (West 2006).

\(^{122}\) KY. REV. STAT. ANN. § 292.410(1)(a) (West 2006). See Blinder, Robinson & Co., Inc. v. Goettsch, 403 N.W.2d 772, 774 (Iowa 1987) (holding that the isolated nonissuer transaction was not unconstitutionally vague).

\(^{123}\) KY. REV. STAT. ANN. § 292.310(13) (West 2006).

\(^{124}\) See Watson v. Shaffner, Nos. 88-6409 & 89-5007, 1990 WL 3487, at *3 (6th Cir. Jan. 19, 1990) (holding that while a corporation may derive an incidental benefit from having a co-owner as an employee, the benefit is not sufficient to constitute a “direct or indirect benefit” transforming the agreement into an issuer transaction, thus it would not prevent the application of the non-issuer exemption).

\(^{125}\) Commonwealth v. Allen, 441 S.W.2d 424, 429 (Ky. 1969) (holding that the sale of stock to 10 purchasers, when 30 were contacted, were not “isolated sales” and were not exempt from registration).


\(^{127}\) Id. at 22,565.

\(^{128}\) Id.
restrictions were not taken lightly. The Division cautioned that if an active secondary market were to develop without registration in Kentucky, an investigation would be conducted.

2. Bona Fide Pledgee Transactions

A transaction “executed by a bona fide pledgee without any purpose of evading [the Act]” is exempted from registration. A pledge used as a method to transfer securities in violation of the registration provisions of the Act will not qualify as a “bona fide” transaction.

3. Sales to Certain Financial Institutions

Any offer or sale to a bank, savings institution, trust company, insurance company, investment company (as defined in the Investment Company Act of 1940), pension or profit-sharing trust, or other financial institution or institutional buyer, or to a broker-dealer, whether acting for itself or in some fiduciary capacity, is exempt from Kentucky’s registration provisions. The general justification for this exemption is that these investors are “sophisticated investors,” and as such, are not in need of the protections of registration. Moreover, these institutions, due to their size, are able to make well-informed decisions because of their ability to obtain enough information about the issuer.

129. Id. Unfortunately, no specifics were provided by the Division with regard to what steps should be taken to assure that the “restrictions were not taken lightly.”

130. Id.


133. K Y. REV. STAT. ANN. § 292.410(1)(h) (West 2006). See also Blue Sky L. Rep. (CCH) ¶ 27,555 at 22,551-52 (Charles C. Mihalek, Jr. Director, Division of Securities) (March 7, 1975) (granting a no action request, since the Division held that the partnership was an “institutional buyer,” where a transaction was to be made by a person to a family partnership, whose purpose was to provide a medium to pool the family assets, and the family was advised by a staff who made the actual investment decisions and primary purpose was to invest and hold stock, bonds, and other investment products); See also KY. REV. STAT. ANN. § 292.310(2) (West 2006) (defining a broker-dealer as any person that is engaged in the business of effectuating transactions for anyone).


4. Kentucky Private Offering

Another important registration exemption in Kentucky is the limited offering exemption located in Section 410(1)(i) of the Act. Subsection 410(1)(i) permits securities to be offered or sold to individuals without registration if specific qualifications are met. This exemption is available when all of the following conditions are met:

- No General Advertising—The issuer may not offer or sell the securities by means of a form of general advertisement or general solicitation;

- Investment Intent—The issuer must reasonably believe that each purchaser of the securities is acquiring the securities for investment and is aware of any restrictions imposed on the transferability and resale of the securities. Issuers can form a reasonable belief by either obtaining a written representation signed by the purchaser, or by placing a restrictive legend on the certificate;

- Other Condition—In addition to the above-listed requirements, the transaction also must satisfy one of the following three conditions:
  
  (i) Each purchaser must have access to all the material facts with respect to the securities by reason of such purchaser’s active involvement or management in the organization, or such purchaser’s family relationship with a person in active involvement or management;

  (ii) There are not more than 15 purchasers in Kentucky (excluding an unlimited number of “accredited investors” as defined in Rule 501 of Regulation D); or

  (iii) The aggregate offering price of the securities, including securities sold outside of Kentucky, does not exceed $1,000,000, the total number of purchasers within and outside of Kentucky.

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136. KY. REV. STAT. ANN. § 292.410(1)(i) (West 2006); See Allen, 441 S.W.2d at 428 (discussing if an offer occurred). See Wilson, 675 S.W.2d at 13.

137. KY. REV. STAT. ANN. § 292.410(1)(i) (West 2006).


139. KY. REV. STAT. ANN. § 292.410(1)(i)(2) (West 2006).

140. KY. REV. STAT. ANN. § 292.410(1)(i)(3) (West 2006).
(excluding accredited investors) does not exceed 35, and each purchaser who is not an accredited investor receives all of the material facts with respect to the offering or is a purchaser described in (i) above.

Those who receive a fee in connection with the sale of securities are not relieved of complying with the broker-dealer provisions of KRS 292.330. Further, the commissioner has the power to increase the maximum number of purchasers or offering amount if he/she feels that it is in the best interest of the public or the protection of investors. Any request to increase either or both of these conditions must be made in writing to the commissioner before any sale is made in reliance on the requested increase.

5. Existing Security Holders

Similar to the federal registration exemption set forth in Section 3(a)(9) of the Securities Act, the Kentucky Act exempts certain transactions with existing security holders. Section 410(1)(k) of the Act sets forth a transactional exemption for any transaction pursuant to an offer to existing security holders of the issuer, including persons who at the time of the transaction are holders of convertible securities, non-transferable warrants, or transferable warrants exercisable within not more than ninety (90) days of their issuance, as long as no commission or other remuneration is paid or given directly or indirectly for soliciting any security holder in Kentucky.

6. Offers When Registration Statements are Filed

Section 410(1)(l) of the Act sets forth a registration exemption for offers, but not sales, of securities for which a registration statement has been filed, and (1) neither a stop order or refusal order is in effect, and (2) there are no pending

141. KY. REV. STAT. ANN. § 292.410(1)(i)(4) (West 2006).
143. Id. Stating that:
   The request should be accompanied by the following: (a) a statement of the amount of the increase in the maximum offering amount or in the number of purchasers requested, and the issuer’s reasons for requesting the increase; (b) a copy of the offering circular or other written materials being distributed to prospective purchasers; (c) a copy of the written representation and legend serving as the issuer’s basis for reasonable belief of a purchaser’s investment intent and awareness of restrictions on the transferability and resale of the security being acquired; and (d) a filing fee of two hundred and fifty dollars ($250).

Id.
144. KY. REV. STAT. ANN. § 292.410(1)(k) (West 2006).
public proceedings or examinations.\textsuperscript{145} It is important to note that this exemption is limited in scope as it only applies to offers and not sales.\textsuperscript{146}

7. Stock Dividends

The issuance by a company of any stock dividend, whether the corporation distributing the dividend is the issuer of the stock or not, is exempt from the registration under the Act.\textsuperscript{147} This exemption is contingent on stockholders giving nothing of value for the distribution, aside from the surrender of a right to a cash dividend where the stockholder can elect to take a dividend in cash or stock.\textsuperscript{148} An example of this exemption in use is when companies make a stock distribution pursuant to an announced stock split.

8. Preorganization Subscriptions

Like other states that have adopted the Uniform Securities Act, Kentucky has an exemption designed to allow new businesses to obtain subscriptions for their securities before first registering them.\textsuperscript{149} Section 410(1)(j) of the Act provides that “[a]ny offer or sale of a preorganization certificate or subscription” is exempt, provided no commission or other remuneration is paid or given directly or indirectly for soliciting prospective subscribers, and the number of subscribers does not exceed 25.\textsuperscript{150} While no limitation is placed on the number of offerees, the subsequent sale of the securities, however, does not fall within this exemption, and either the sale must be covered by another exemption or the securities must be registered.\textsuperscript{151}

9. Professional Service Entities

Pursuant to the commissioner’s authority to exempt transactions in the public interest,\textsuperscript{152} Kentucky Regulation 10:150 provides an exemption for securities issued by professional service corporations, professional limited liability companies, or professional limited liability partnerships, provided that such entities are duly organized, the securities are sold only to professionals, the

\begin{itemize}
\item \textsuperscript{145} KY. REV. STAT. ANN. § 292.410(1)(l) (West 2006).
\item \textsuperscript{146} Id.
\item \textsuperscript{147} KY. REV. STAT. ANN. § 292.410(1)(m) (West 2006).
\item \textsuperscript{148} Id. KY. REV. STAT. ANN. § 292.410(1)(m) states:
\begin{quote}
The issuance of any stock dividend, whether the corporation distributing the dividend is the issuer of the stock or not, if nothing of value is given by stockholders for the distribution other than the surrender of a right to a cash dividend where the stockholder can elect to take a dividend in cash or stock.
\end{quote}
\item \textsuperscript{149} KY. REV. STAT. ANN. § 292.410(1)(j) (West 2006).
\item \textsuperscript{150} Id.
\item \textsuperscript{151} Id.
\item \textsuperscript{152} KY. REV. STAT. ANN. § 292.410(1)(q) (West 2006).
\end{itemize}
seller reasonably believes that each buyer is purchasing for investment, and each buyer is provided access to information concerning the entity.\textsuperscript{153}

10. Kentucky Uniform Limited Offering Exemption

While securities offered or sold in compliance with Rule 506 of Regulation D fit within the definition of “covered securities” under NSMIA,\textsuperscript{154} issuers conducting offerings under Rules 504\textsuperscript{155} or 505\textsuperscript{156} are also afforded an exemption from registration in Kentucky. The elements of this exemption are as follows:

- No General Advertising—The issuer may not engage in general advertising or general solicitation;\textsuperscript{157}

- Investment Intent—The issuer must reasonably believe that each purchaser in Kentucky is acquiring the securities for investment and is aware of the restrictions imposed on the transferability and resale of the security (e.g., obtaining a written representation from the purchaser or placing a restrictive legend on the certificate);\textsuperscript{158} and

- Notice on Form D—The issuer must file with the Department a notice on Form D (manually signed), along with the other offering documents furnished by the issuer to an offeree and a $250 filing fee: (a) within 15 days after the first sale of a security from or into Kentucky in the case of a Rule 505 offering, or (b) at least 10 business days prior to the first sale of a security from or into Kentucky in the case of a Rule 504 offerings.\textsuperscript{159}

It is important for practitioners to keep in mind that the antifraud provisions of the Act still apply to offers and sales under this exemption.\textsuperscript{160} Further, this exemption is not available if the issuer disqualifies under the “bad boy” provisions of the regulation.\textsuperscript{161}

\textsuperscript{153} 808 KY. ADMIN. REGS. 10:150 (2006).
\textsuperscript{154} See discussion supra Part II.C.2.
\textsuperscript{155} 17 C.F.R. § 230.504 (2006).
\textsuperscript{156} 17 C.F.R. § 230.505 (2006).
\textsuperscript{158} 808 KY. ADMIN. REGS. 10:210 § (1)(3)(b) (2006).
\textsuperscript{159} 808 KY. ADMIN. REGS. 10:210 § (1)(3)(c) (2006).
\textsuperscript{160} See infra Part V.
\textsuperscript{161} See 808 KY. ADMIN. REGS. 10:210 § (1)(4) (2006).
11. Sale of Business

The offer or sale of 100 percent of the ownership interest in a corporation is exempt from registration in Kentucky as long as the stock is sold to one individual or preexisting entity.162

12. Accredited Investor Exemption

By rule, any offer or sale of a security by an issuer is exempt if sales are made exclusively to persons who are accredited investors (as defined in Rule 501 of Regulation D), and who the issuer reasonably believes are purchasing for investment and not with a view to sell in connection with a distribution of the securities.163 The exemption is not available for an issuer that (1) issues interests in an oil, gas, or mineral enterprise, (2) is in the development stage and (i) has no specific business plan or purpose or (ii) the business plan or purpose is to engage in a merger of acquisition.164 This exemption also denies eligibility if certain “bad boy” provisions are triggered.165

While federal securities laws may be implicated, this exemption allows issuers to make general announcements about the proposed offering if the information contained in the announcement is limited.166 Within 15 days after the first sale in Kentucky, the issuer must file a notice form, a consent to service of process (i.e., Form U-2), a copy of the general announcement, and a fee in the amount of $250.167

IV. THE REGISTRATION PROCESS

A. Introduction

In the event state registration of an offering is not preempted by NSMIA and is not exempt under any of Kentucky’s registration exemptions, the securities underlying the offering will require registration.168 Kentucky blue sky law provides three methods of registration: notification,169 coordination,170 and

162. 808 Ky. Admin. Regs. 10:240 (2006) (Before this regulation was promulgated, the Division advised practitioners of the availability in this situation of KRS 292.410(1)(i)). See Blue Sky L. Rep. (CCH) ¶ 27,571 at 22,561 (No-Action Letter, Ronda S. Paul, Director, Div. of Securities) (Dec. 18, 1985).
qualification. In general, registration by notification is the simplest method. Coordination is the next preferred method, in terms of ease of compliance, followed by registration by qualification. This section details the requirements for securities registration in Kentucky.

B. Registration by Notification

Registration by notification is available to certain “blue chip” businesses meeting specific qualifications. Often, securities issued by these businesses already qualify for “covered security” status, thus preempting registration requirements; however, this may not always be the case.

In order for issuers to be able to use this registration method, they must first satisfy certain threshold criteria. First, the issuer and any predecessors must have been in continuous operation for at least five years. Second, the issuer or its predecessor cannot have defaulted during the current fiscal year, or the last three fiscal years in paying principal, interest, or dividends on securities with fixed maturity, fixed interest, or securities having a dividend provision. Third, the issuer and any predecessors must satisfy an average net earnings test.

An issuer that satisfies the earnings and operational history test set forth above must register its securities using Form U-1, Uniform Application to Register Securities (a sample of which is attached hereto as Appendix A). The Form must contain the following information:

- A statement demonstrating the issuer’s eligibility for registration by notification;
- The issuer’s name, address, and form of organization; the state (or foreign jurisdiction) and the date of its organization; and the general character and location of its business;
- With respect to any person on whose behalf any part of the offering is to be made (e.g., selling security holder),

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171. KY. REV. STAT. ANN. § 292.370 (West 2006).
173. KY. REV. STAT. ANN. § 292.350(1)(a) (West 2006). Nonissuers may use notification to register securities if any security of the same class has ever been registered in Kentucky, or the security being registered was originally issued pursuant to an exemption in Kentucky, or if previously publicly offered and sold, was not offered and sold within Kentucky. KY. REV. STAT. ANN. § 292.350(1)(b) (West 2006).
if such person is an officer, director, partner or a person occupying a similar status or performing similar functions, or any affiliate of such person, his name and address, the amount of securities held by him as of the date of the filing, and a statement of his reasons for making the offering;\textsuperscript{180}

\begin{itemize}
  \item A description\textsuperscript{181} and amount of the securities being offered both inside and outside of Kentucky;\textsuperscript{182}
  \item The price at which the securities are to be offered for sale to the public, if other than at the market price, and the estimated maximum aggregate underwriting and selling discounts or commissions and finders’ fees (including cash, securities, or anything else of value);\textsuperscript{183}
  \item Names and addresses of the managing underwriters, if any, and a description of the plan of distribution of any securities which are to be offered otherwise than through an underwriter;\textsuperscript{184}
  \item Description of any security options outstanding or to be created in connection with the option (e.g., stock options outstanding);\textsuperscript{185}
  \item Any adverse legal consequences previously entered in connection with the securities being registered by any court or securities and exchange commission;\textsuperscript{186}
  \item A copy of any offering circular or prospectus used, or intended to be used, in connection with the offering;\textsuperscript{187}
  \item In certain circumstances, certain financial statements concerning the issuer;\textsuperscript{188}
\end{itemize}

\textsuperscript{183} \textit{Ky. Rev. Stat. Ann.} § 292.350(2)(f) (West 2006) (the form must also disclose any known variation of the pricing, other than variations, because of underwriting and selling discounts or commissions).
The Form is submitted to the Division along with an examination fee in the amount of $125, and a registration fee of 3/50ths of 1% of the aggregate offering price of the securities which are to be offered in Kentucky, but in no case can the registration fee be less than $60 nor more than $1,200.189

Unless a stop order is in effect or a proceeding regarding the offering is pending, a registration statement filed under the notification method of registration automatically becomes effective at 3:00 p.m. Eastern Standard Time in the afternoon of the fifth full business day after its filing or the last amendment.190

C. Registration by Coordination

Registration by coordination is available in Kentucky when a registration statement under the Securities Act or an offering statement under Regulation A of the Securities Act has been filed with the SEC.191 This method of coordination permits the issuer to avoid unnecessary duplication and to use substantially the same materials in complying with registration requirements at both federal and state levels.192 Under the Act, registration on the state level automatically becomes effective when the federal registration becomes effective if (1) no stop order is in effect; (2) the registration has been on file with the executive director for 10 days; and (3) a statement of the maximum and minimum proposed offering prices and the maximum underwriting discounts has been on file for two days.193 The issuer must notify the executive director; however, when the federal registration statement or offering document is declared effective by the SEC, and must file a post-effective amendment, containing the information and documents in the price amendment.194

Form U-1, Uniform Application to Register Securities, is also used in this process.195 The statute provides that the following information must be contained in the Form:

- One copy of the latest form of prospectus or offering circular under the Securities Act or Regulation A, together with all amendments thereto;196
- The amount of securities to be offered in Kentucky;197

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189. KY. REV. STAT. ANN. § 292.380(5) (West 2006) (fees must be paid using separate checks).
190. KY. REV. STAT. ANN. § 292.350(3) (West 2006).
191. KY. REV. STAT. ANN. § 292.360(1) (West 2006).
193. KY. REV. STAT. ANN. § 292.360(3) (West 2006).
194. KY. REV. STAT. ANN. § 292.360(3)(c) (West 2006).
196. KY. REV. STAT. ANN. § 292.360(2)(a) (West 2006) (the 1998 amendments reduced the number of copies required from three to one).
• A list of states where a registration statement or similar document has been or is expected to be filed;¹⁹⁸

• Notification of any adverse judgments, orders or decrees previously issued in connection with the offering;¹⁹⁹

• If required, a copy of the articles of incorporation and bylaws (or equivalents if not a corporation), a copy of any agreements with underwriters, a copy of any indenture or other instrument governing the issuance of the security, and a specimen or copy of the security;²⁰⁰

• If requested, any other information or documents filed under the Securities Act or Regulation A;²⁰¹ and

• An undertaking to forward promptly to the executive director all amendments to the federal registration statement or offering document, other than an amendment which merely delays the effective date.²⁰²

Issuers who file a registration statement by coordination are required to keep the registration current by filing any post-effective amendment not already on file with the Department; filing a copy of the issuer’s annual report on Form 10-K under the Exchange Act, or a document containing the certain prescribed information; and filing a statement of the aggregate amount of securities sold in the state of Kentucky during the preceding 12 month period.²⁰³

D. Registration by Qualification

Registration by qualification is the most demanding and time-consuming of the three ways to register, and generally is the last choice for issuers and practitioners alike.²⁰⁴ In the post-NSMIA regulatory environment, and given the availability of registration by coordination when offerings are conducted on a broad scale, registration by qualification will be relied upon most often for “intrastate” offerings exempt from federal registration by Securities Act Section 3(a)(11). While offerings under SEC Rules 504 and 505 may also use registration by qualification on the state level, the easier method of conducting these types of offerings is to take advantage of Kentucky’s limited offering

¹⁹⁷. KY. REV. STAT. ANN. § 292.360(2)(b) (West 2006).
¹⁹⁸. KY. REV. STAT. ANN. § 292.360(2)(c) (West 2006).
¹⁹⁹. KY. REV. STAT. ANN. § 292.360(2)(d) (West 2006).
²⁰⁰. KY. REV. STAT. ANN. § 292.360(2)(e) (West 2006).
²⁰¹. KY. REV. STAT. ANN. § 292.360(2)(f) (West 2006).
²⁰². KY. REV. STAT. ANN. § 292.360(2)(g) (West 2006).
exemption, as described in Part III.C.10. above. Often, issuers using this method are unseasoned issuers or of local interest.205

Registration by qualification is the most burdensome form of registration because it requires issuers to submit a voluminous amount of information about the issuer and the offering.206 As with the other forms of registration, a Form U-1 may be used.207 The following discussion sets forth a non-exclusive list of information required in the registration statement:

- Basic information about the issuer and any subsidiaries, the state or foreign jurisdiction and date of its organization, the general character and location of its business, any physical property and equipment, and a statement of the general competitive conditions in the industry or business in which it is or will be engaged;208

- Personal data about corporate officers, directors (or persons occupying a similar status), and 10% shareholders including the amount of securities held by each and a description of any material interest or transaction effected between the issuer and such person for a period of three years;209

- The aggregate remuneration paid by the issuer to corporate officers, directors and 10% shareholders during the past twelve months, an estimate of the aggregate amount that is to be paid to them during the next twelve months, and the amount paid, or to be paid, to each of those individuals who have or will receive more than $15,000;210

- If the issuer was organized less than three years before filing, personal data regarding any promoter and any amount paid, or to be paid, to such person;211

- Details relating to capitalization and long-term debt (on both a current and pro forma basis); a description of each security outstanding or to be registered; and the amount and kind of consideration for which the issuer

205. Id.
has issued any of its securities within the past two years;\textsuperscript{212}

\begin{itemize}
\item Details relating to the offerings, including: (a) the kind and amount of securities, (b) the estimated underwriting and selling discounts or commissions, (c) estimated professional fees, (d) cash proceeds expected from the offerings, (e) the proposed use of such proceeds, and (f) a description of any stock options;\textsuperscript{213}
\item Copies and a description of every material contract made other than in the ordinary course of business if it is to be performed at or after the filing of the registration statement or was made within the past two years;\textsuperscript{214}
\item A list of states in which a registration statement has been or is expected to be filed;\textsuperscript{215}
\item Any adverse order, judgment or decree in connection with the offering;\textsuperscript{216}
\item Copies of any prospectus or circular (e.g., sales literature) to be used;\textsuperscript{217}
\item A specimen or copy of the security being registered, and a copy of the issuer's organizational documents;\textsuperscript{218}
\item An opinion of counsel as to the legality of the security being offered;\textsuperscript{219}
\item Financial statements of the issuer set in relation to the size of the offering or the business history of the history;\textsuperscript{220}
\item Consents from any professional (e.g., engineer, accountant, appraiser), if such person is named as
\end{itemize}

\textsuperscript{212} KY. REV. STAT. ANN. § 292.370(2)(f) (West 2006).
\textsuperscript{213} KY. REV. STAT. ANN. §§ 292.370(2)(g)-(i) (West 2006).
\textsuperscript{214} KY. REV. STAT. ANN. § 292.370(2)(j) (West 2006).
\textsuperscript{215} KY. REV. STAT. ANN. § 292.370(2)(k) (West 2006).
\textsuperscript{216} KY. REV. STAT. ANN. § 292.370(2)(l) (West 2006).
\textsuperscript{217} KY. REV. STAT. ANN. § 292.370(2)(m) (West 2006).
\textsuperscript{218} KY. REV. STAT. ANN. § 292.370(2)(n) (West 2006).
\textsuperscript{219} KY. REV. STAT. ANN. § 292.370(2)(o) (West 2006).
\textsuperscript{220} KY. REV. STAT. ANN. § 292.370(2)(p) (West 2006).
having prepared or certified a report or valuation used in the registration process;\textsuperscript{221} and

- Any other information as the commissioner requires by rule or order.\textsuperscript{222}

In general, registrations by qualification are not subject to merit review. Notwithstanding this general proposition, the Act does permit the commissioner to issue stop orders denying the effectiveness of any registration statement if he finds that the order is in the public interest and the offering “has worked or tended to work, a fraud upon purchasers[,] or would so operate.”\textsuperscript{223} Further, the commissioner may issue stop orders in the event that he makes a determination that the offering would be made with “unreasonable amounts of underwriters’ and sellers’ discounts . . . and unreasonable amounts or kinds of options.”\textsuperscript{224} A registration statement by qualification becomes effective when the executive director orders.\textsuperscript{225}

1. Small Corporate Offering Registration (SCOR)

Although registration by qualification is the most difficult form of registration under the Act, smaller companies in Kentucky do have an alternative when engaging in a more localized distribution. Kentucky has adopted by regulation a NASAA sponsored modification to registration by qualification known as the “Small Corporate Offering Registration,” or SCOR.\textsuperscript{226} The SCOR method utilizes Form U-7 for registration by qualifying corporate issuers for small offerings\textsuperscript{227} (a copy of Form U-7 is attached as Appendix B).\textsuperscript{228} Form U-7 is not available for selling security holders, blind pool offerings or other offerings for which the specific business or properties cannot presently be described.\textsuperscript{229}

The pertinent criteria that issuers must satisfy in order to be eligible for SCOR registration are the following: (1) the offering price for stock must be at least $5 per share,\textsuperscript{230} (2) the company and its affiliates cannot be subject to

\textsuperscript{221} KY. REV. STAT. ANN. § 292.370(2)(q) (West 2006).
\textsuperscript{222} KY. REV. STAT. ANN. § 292.370(2)(r) (West 2006).
\textsuperscript{223} KY. REV. STAT. ANN. § 292.390(1)(e) (West 2006).
\textsuperscript{224} KY. REV. STAT. ANN. § 292.390(1)(f) (West 2006).
\textsuperscript{225} KY. REV. STAT. ANN. § 292.380(1) (West 2006).
\textsuperscript{226} 808 KY. ADMIN. REGS. 10:280 (2006).
\textsuperscript{227} 808 KY. ADMIN. REGS. 10:280 § 1 (2006).
\textsuperscript{228} 808 KY. ADMIN. REGS. 10:280 § 1 (2006).
\textsuperscript{229} 808 KY. ADMIN. REGS. 10:280 § 1(1) (2006).
\textsuperscript{230} 808 KY. ADMIN. REGS. 10:280 § 1(3) (2006) (if an issuer registers its securities through SCOR, it is not allowed to undertake a stock split for two years after the effective date unless an exception is granted by the Department).
certain “bad boy” provisions; and (3) the aggregate offering cannot exceed $1,000,000, less the aggregate offering price for all securities sold within the 12 months before the start of, and during the offering of, the securities under Rule 504 promulgated under the Securities Act.

A properly completed Form U-7, together with a Form U-1, constitutes an application for registration under the states listed at the bottom of the cover page of the form. The disclosure document on Form U-7 acts as the offering circular or prospectus. Once declared effective, the company simply reproduces the document and disseminates it to potential investors. It is important to note that this document must be delivered to each investor before the “sale” is made. This means issuers must deliver the document to investors before (1) any order is entered, (2) the subscription agreement is signed, or (3) any part of the purchase price is received.

E. General Provisions Regarding Registration Statements

With respect to timing, every registration statement is effective for at least one year from its effective date. All notice filings for covered securities are effective for one year following receipt by the Division. Amendments to registration statements filed using registration by coordination or qualification have to be marked to show every change made from the last amendment filed.

V. Antifraud Provisions

At the heart of all securities regulation is the protection of the investor. To this end, the Kentucky legislature has enacted several sections that seek to prevent companies and their agents from making misleading filings and representations with respect to securities offerings. The first section, KRS 292.440, makes it unlawful for persons to make, in any document filed with the executive director (or the executive director’s designee), any statement which is, at the time and in light of the circumstances under which it was made, false or misleading in any material respect.

Section 450 of the Act makes it unlawful to make any representation to a prospective purchaser that the executive director has passed upon the

235. Id.
237. Id.
238. KY. REV. STAT. ANN. § 292.380(6) (West 2006).
239. KY. REV. STAT. ANN. § 292.327(1)(c) (West 2006).
truthfulness, completeness, or non-misleading nature of any registration statement, exemption thereunder, or notice filing for a covered security.\textsuperscript{242} Section 470 of the Act sets forth remedies that are available to the executive director when it appears that a person is engaged, or about to be engaged, in any securities violation.\textsuperscript{243} Examples include issuing a cease and desist order without a prior hearing, instituting an action in the Franklin Circuit Court to enjoin violations of the Act, and assessing certain fines and costs.\textsuperscript{244}

Finally, Section 480 of the Act grants harmed investors a private right of action.\textsuperscript{245} Generally, the amount recoverable by the investor is the consideration paid for the security, together with interest and reasonable attorneys’ fees, less any amount recovered by the investor upon its sale.\textsuperscript{246}

\section*{VI. CONCLUSION}

A basic principle in securities law, both at the state and federal level, is that a sale of a security must either be registered, or exempt from registration. Section III of this article sets forth the most commonly-used registration exemptions in Kentucky, while Section IV discusses the three types of registration (notification, coordination, and qualification) if an exemption is not available, or is not desired.

While securities law in Kentucky is based directly upon the Uniform Securities Act of 1956, the state has enacted several amendments and issued many interpretive opinions. Because virtually all states have made modifications to their blue sky laws, the idea of complete uniformity among the states simply does not apply. Unless preempted by NSMIA, practitioners must review each

\textsuperscript{242} KY. REV. STAT. ANN. § 292.450 (West 2006) states:

\begin{enumerate}
\item Neither the fact that an application for registration under KRS 292.330 or a registration statement under KRS 292.350, 292.360, or 292.370 has been filed, nor the fact that a person or security is effectively registered, constitutes a finding by the executive director that any document filed under this chapter is true, complete, and not misleading. (2) Neither any such fact nor the fact that an exemption or exception is available for a security or a transaction means that the executive director has passed in any way upon the merits or qualifications of, or recommended or given approval to, any person, security, or transaction. It is unlawful to make, or cause to be made, to any prospective purchaser, customer, or client any representation inconsistent with this section. (3) Neither the fact that a notice filing for a covered security or for a covered adviser has been filed, nor the fact that the person, security, or transaction is registered or exempt from registration, constitutes a finding by the executive director that any document filed under this chapter is true, complete, and not misleading or that the person, security, or transaction is entitled to claim an exemption. (4) It is unlawful to make or cause to be made to any prospective purchaser, customer, or client any representation inconsistent with this section.
\end{enumerate}

\textsuperscript{243} KY. REV. STAT. ANN. § 292.470 (West 2006).

\textsuperscript{244} \textit{Id}.

\textsuperscript{245} KY. REV. STAT. ANN. § 292.480 (West 2006).

\textsuperscript{246} KY. REV. STAT. ANN. § 292.480(1) (West 2006).
state’s requirements when conducting an offering of securities. For this reason, this article has been written primarily as a resource for practitioners when confronting a securities issue in the Commonwealth of Kentucky.
ADMINISTRATION OF PRINCIPAL AND INCOME FOR THE COMMONWEALTH: A SURVEY OF THE KENTUCKY PRINCIPAL AND INCOME ACT

by Kevin R. Ghassomian, Esq.* and Jennifer T. Leonard*

I. INTRODUCTION

Most fiduciaries have encountered estates and trusts with current and future beneficiaries whose interests are at odds with each other. Generally, the current beneficiary receives distributions of income and the future beneficiary is the ultimate recipient of principal.1 Thus, it is up to the fiduciary to determine whether a receipt of property is to be treated as “income,” and thereby currently distributable, or “principal,” to be held for the residuary or remainder beneficiary.2 Likewise, the fiduciary must decide whether to charge expenses of the estate or trust against income or principal. As one can surmise, these determinations are fraught with tension, as each beneficiary lobbies to maximize its share of the estate or trust property.3 The fiduciary, alone in the midst of these competing interests, must remain impartial, balancing receipts and disbursements between income beneficiaries and remaindermen without favor.4

As most fiduciaries can attest, maintaining impartiality is difficult; but it has become more practicable due in large part to the ascendance of “total return” investing, an approach to fiduciary asset management that seeks to maximize gains of the estate or trust as a whole regardless of whether returns fall on the

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1. The terms “principal” and “corpus” are used interchangeably in the authority cited for this article. Generally, “principal” is used in state statutes and “corpus” is used in the Internal Revenue Code. *Fiduciary Accounting Income Under State Law*, Tax Management: Estates, Gifts, and Trusts Portfolios: Trustee Investments (BNA) No. 852-2nd, at A-55 (Jan. 10, 2005). However, their definitions are the same. *Id.*


3. *Id.*

4. *Restatement (Second) of Trusts § 183 (1959)* (stating, “[w]hen there are two or more beneficiaries of a trust, the trustee is under a duty to deal impartially with them”). *See also* Alyssa A. DiRusso & Kathleen M. Sablone, *Statutory Techniques for Balancing the Financial Interests of Trust Beneficiaries*, 39 U.S.F. L. Rev. 261, 262 (2005).
income or principal side of the ledger. Although “total return” investing tends to improve overall financial yields, the fiduciary’s investment decisions will either have an income bent, favoring current beneficiaries, or a growth orientation that decidedly favor the remaindermen. Inevitably, such investment tilts exacerbate conflicts between current and future beneficiaries, making it all but impossible for a fiduciary to remain even-handed in administering income and principal interests.

Fortunately, the fiduciary’s balancing act has been steadied by various legislative initiatives including, most notably, the 1997 Uniform Principal and Income Act (“Uniform Act”). The Uniform Act effectively addresses tensions between current and future beneficiaries by establishing a protocol for fiduciary administration in accordance with the dual goals of impartiality and optimum investment returns. Kentucky’s version of the Uniform Act, known as the Kentucky Principal and Income Act (“Kentucky Act”), went into effect on January 1, 2005.

For the most part, the provisions of the Kentucky Act mirror those of the Uniform Act; however, there are several notable differences. This article examines variations between the Uniform Act and the Kentucky Act and also details many of their common provisions. Section II opens with a discourse on the historical predecessors and influences that led to the adoption of the Kentucky Act, including a brief foray into the evolution of the “total return” investing. Section III picks up with a general overview of the Kentucky Act, its noteworthy provisions and departures from the terms of the Uniform Act. Section IV closes with a cursory review of the Internal Revenue Service (“IRS”) response to the Uniform Act and its state law counterparts.

II. LEGISLATIVE BACKGROUND

Through the years, market trends and corresponding changes in investment theory have led to a gradual modification of the rules governing income and principal administration. Specifically, a rigid fiduciary accounting regime that sometimes arbitrarily distinguished between income and principal interests slowly gave way to a new flexible approach, integrating a fiduciary’s management and investment of these interests into a unified portfolio of assets.

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5. See DiRusso & Sablone, supra note 4, at 262.
6. Id.
7. Id.
9. See generally id.
12. See generally DiRusso & Sablone, supra note 4, at 262.
13. Id.
This section provides background on the development of this approach, beginning with its roots in the “prudent man rule” and leading ultimately to the near nationwide adoption of the Uniform Act and its passage in Kentucky.

A. The Prudent Man Rule.

The first widely accepted standard governing fiduciary investment discretion was the “prudent man rule.”\(^\text{14}\) Initially articulated by the Massachusetts Supreme Judicial Court in Harvard College v. Amory,\(^\text{15}\) it required fiduciaries, in this case a trustee, “to observe how men of prudence, discretion and intelligence manage their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income, as well as the probable safety of the capital to be invested.”\(^\text{16}\) As it was applied by subsequent courts, the “prudent man rule” evolved to require the exercise of “prudence” in making or retaining each individual investment, failing to take into account the role of a particular asset in the fiduciary’s overall mix of investments.\(^\text{17}\)

This myopic interpretation of investment “prudence” was picked up and effectively endorsed by the Restatement (Second) of Trusts in 1959.\(^\text{18}\) Thereafter, many states codified it into law, some going so far as to restrict fiduciaries to investing in an approved list of assets.\(^\text{19}\) As investment options increased, however, the rigidity of the “prudent man rule,” as it had been applied, became evident, exposing the failure of the courts to keep pace with contemporary investment theory.\(^\text{20}\) The law had to change if fiduciaries were to maintain respectable rates of return on their investments.\(^\text{21}\) Mercifully, it did change thanks mainly to the advent of “modern portfolio theory” and the “total return” approach to investing, the philosophical precipitators of current fiduciary investment practices.\(^\text{22}\)

\(^{14}\) Id. at 264. See also Mayo Adams Shattuck, The Development of the Prudent Man Rule for Fiduciary Investment in the United States in the Twentieth Century, 12 Ohio St. L.J. 491 (1951) (discussing in detail the prudent man rule and its integration into trusts).

\(^{15}\) 26 Mass. 446 (1830).

\(^{16}\) Id. at 461.

\(^{17}\) See DiRusso & Sablone, supra note 4, at 266. See also, Restatement (Third) of Trusts § 227 (1992) (noting that the courts failed to apply the generality and flexibility of the rule as initially intended).

\(^{18}\) Restatement (Second) of Trusts § 227 (1959).

\(^{19}\) Id. at § 227 cmt. p (noting “[i]n some States the statutes are more restricted, allowing only such investments as government securities, first mortgages on land, and certain types of bonds”). Later, states adopted the more flexible prudent man rule. Restatement (Third) of Trusts § 227 (Introduction, pp.3-7) (1992).

\(^{20}\) See generally, DiRusso & Sablone, supra note 4, at 266-67.

\(^{21}\) Id.

\(^{22}\) Id.
B. *Modern Portfolio Theory and Total Return Investing*

1. Modern Portfolio Theory

Modern portfolio theory is premised on two fundamental tenets. The first is that investment returns are correlated to the degree of risk assumed by the investor in making its investment selections. Such risk includes both “market risk,” which applies systemically to all investments as determined by external factors, and “non-market risk,” which applies to individual investments as dictated by events and occurrences peculiar to the investment itself.

To illustrate, “market risk” derives from events like elections, natural disasters and other macroeconomic forces, whereas “non-market risk” emanates from the investment itself such as the death of a company’s chief executive officer, a strike by its employees or the development of an innovative new product. Investors generally cannot protect against market risk, as it applies to everyone engaged in the marketplace; thus, differentiation of investment returns depends on one’s ability to contain “non-market risk.” Modern portfolio theory presumes that the “prudent” investor will act to reduce non-market risks through diversification of asset holdings. Diversification as a risk reduction technique is based on the simple notion that different assets react differently to the same systemic influences; thus, higher yields by one company will offset, to some degree, the lower yields of another.

The second tenet of modern portfolio theory is market efficiency. Generally, modern portfolio theory presumes that the price of an investment is based upon the sum total of all the information currently known by the public about that investment. Thus, no matter how diligent an investor is in gathering information about a company, its price will have already adjusted to incorporate that information before the investor can act upon it. As such, proponents of modern portfolio theory assert that it is futile to try to “beat” the market and

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25. *Id.* at 13.
26. *Id.*
31. *Id.* See also *Restatement (Third) of Trusts § 227* (Reporter’s Notes, pp. 74-75 ) (1992).
conscientious or “prudent” investors should merely attempt to mirror its performance.33

2. Total Return Investing.

Traditionally, fiduciaries concerned themselves with the preservation of principal; thus, they were long-inclined to favor bonds when investing estate and trust assets.34 After World War II, however, bond yields began to drop so fiduciaries responded by increasing their equity holdings.35 This trend continued after the late 1960s, throughout the 1970s and into the early 1980s, as fiduciaries sought to outpace rising rates of inflation by enhancing their equity positions.36

“In the 1990s, falling dividend yields and interest rates” along with a “raging bull market” resulted in a heightened “tension between income and remainder beneficiaries.”37 Whether assets were invested in equities or bonds, during this period, neither could produce enough income, as traditionally defined, to provide income beneficiaries with a satisfactory return, thereby, compromising the fiduciary’s ability to satisfy its duty of impartiality.38 States responded by enacting remedial legislation that allowed for “total return” investment which permitted fiduciaries to manage estate and trust portfolios for maximum overall gains, without regard to traditional notions of income and principal oriented investments.39

This focus on “total return” fit well with the modern portfolio theory’s emphasis on diversification, enabling fiduciaries to run the gamut of investment options based upon the risk tolerance of the beneficiaries.40 Thus, total return investing considers the aggregate return of interest, dividend, rent income, and capital appreciation without regard to rigid fiduciary accounting rules, simultaneously satisfying the needs of income beneficiary with that of remainderman.41

33. Horn, supra note 23, at 16. (stating that “investors are not able to outperform the market at whatever mix of risk and reward they seek, and therefore, any attempt to do so is futile, counterproductive, and wasteful”). See also RESTATEMENT (THIRD) OF TRUSTS § 227 (Reporter’s Notes, pp. 75) (1992).
34. DiRusso & Sablone, supra note 4, at 268.
35. Id.
36. Id.
37. See Adam J. Wiensch & L. Elizabeth Beetz, The Liberation of Total Return, TRUSTS AND ESTATES, Apr. 2004, at 44.
38. See generally id.
39. Id. This theory rejects the idea that investors should assess risk and return of each investment before adding it to their portfolio. See also, DiRusso & Sablone, supra note 4, at 268.
40. See generally, Wiensch & Beetz, supra note 37, at 44.
41. See generally, DiRusso & Sablone, supra note 4, at 268.
C. The Prudent Investor Rule and the Uniform Prudent Investor Act

The coincidence of modern portfolio theory and total return investing had a significant impact on fiduciary investment practices, as there was now a broadly accepted body of empirical and theoretical knowledge that fiduciaries could rely on in defending nontraditional investment picks.\(^{42}\) Courts were soon persuaded, and by the 1990s, a new standard for fiduciary asset management had evolved.\(^{43}\) The American Law Institute picked up on the new standard, officially naming it the “prudent investor rule,” in its \textit{Restatement (Third) of Trusts}, a death knell for the defunct “prudent man rule.”\(^{44}\) Subsequently, the National Conference of Commissioners on Uniform State Laws issued the \textit{Uniform Prudent Investor Act}\(^{45}\) which has since been adopted in most states.\(^{46}\)

In its prefatory note, the \textit{Uniform Prudent Investor Act} highlights the following adjustments to prior notions of investment “prudence:”

1. The standard of prudence is applied to any investment as part of the total portfolio, rather than to individual investments. In the trust setting the term “portfolio” embraces all the trust’s assets. UPIA § 2(b).

2. The tradeoff in all investing between risk and return is identified as the fiduciary’s central consideration. UPIA § 2(b).

3. All categoric restrictions on types of investments have been abrogated; the trustee can invest in anything that plays an appropriate role in achieving the risk/return objectives of the trust and that meets the other requirements of prudent investing. UPIA § 2(e).

4. The long familiar requirement that fiduciaries diversify their investments has been integrated into the definition of prudent investing. UPIA § 3.

5. The much criticized former rule of trust law forbidding the trustee to delegate investment and management functions has been reversed. Delegation is now permitted, subject to safeguards.\(^{47}\) UPIA § 9.

\(^{42}\) \textit{Id.} at 269.
\(^{43}\) \textit{Id.}
\(^{44}\) \textit{Restatement (Third) of Trusts} § 227 (1992).
Although Kentucky has not adopted the *Uniform Prudent Investor Act*, the “prudent investor rule” has been incorporated into state law which provides that all banks and corporate fiduciaries in Kentucky must comply with “prudent investor” standards in investing trust and estate assets.

D. The Uniform Principal and Income Act

The Uniform Law Commissioners promulgated the first Uniform Principal and Income Act in 1931 in response to fiduciaries seeking guidance in the following four areas of inquiry:

1. How is income earned during the probate of an estate to be distributed to trusts and to persons who receive outright bequests of specific property, pecuniary gifts, and the residue?

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KY. REV. STAT. ANN. § 286.3-277 states in full:

1) Notwithstanding the provisions of any other law, a bank empowered to act as a fiduciary or trust company, when investing, reinvesting, purchasing, acquiring, exchanging, selling, and managing property held in a fiduciary capacity, shall act as a prudent investor would, in light of the purposes, terms, distribution requirements, and other circumstances of the fiduciary account.

2) The standard described in subsection (1) of this section requires the exercise of reasonable care, skill, and caution, and is to be applied to investments not in isolation but in the context of the account portfolio and as part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the account.

3) In making and implementing investment decisions, the bank or trust company has a duty to diversify the investments of the account unless, under the circumstances, it is prudent not to do so.

4) In addition, the bank or trust company shall: a) conform to fundamental fiduciary duties of loyalty and impartiality; b) act with prudence in deciding whether and how to delegate authority and in the selection and supervision of agents; and c) incur only costs that are reasonable in amount and appropriate to the investment responsibilities of the account.

5) The duties of the bank or trust company under this section are subject to the rule that in investing the funds of the account, the bank or trust company: a) has a duty to the beneficiaries of the account to conform to any applicable statutory provisions governing investment by fiduciaries; and b) has the power expressly or impliedly granted by the terms of the account or applicable instrument and has a duty to the beneficiaries of the account to conform to the terms of the account directing or restricting investments by the bank or trust company.

50. *Id.* Individual fiduciaries may elect to have KRS § 286.3-277 apply to them as well pursuant to KRS § 386.454(3); however, it requires approval of the district court. *Ky. Rev. Stat. Ann.* § 386.454(3) (LexisNexis 1999 & Supp. 2005).
When an income interest in a trust begins (i.e., when a person who creates the trust dies or when she transfers property to a trust during life), what property is principal that will eventually go to the remainder beneficiaries and what is income?

When an income interest ends, who gets the income that has been received but not distributed, or that is due but not yet collected, or that has accrued but is not yet due?

After an income interest begins and before it ends, how should its receipts and disbursements be allocated to or between principal and income?51

The Uniform Law Commission’s main focus in addressing these issues under the 1931 Uniform Act was to provide a standardized protocol for fiduciaries administering income and principal interests that would be fair and reasonable to both current and future beneficiaries.52 This remained their focus in 1964 when the act was revised to account for the introduction of new investment instruments that were not contemplated under the 1931 version of the Uniform Act;53 however, as already noted, the advent of modern portfolio theory and total return investing made it all but impossible for fiduciaries to remain fair and reasonable.54 The investment climate of the 1990s simply did not produce adequate income returns, as defined under traditional fiduciary accounting rules;55 thus, income beneficiaries, feeling slighted by fiduciary investment selections that ostensibly favored remaindermen, began to challenge fiduciaries, questioning their supposed impartiality.56

In 1997, the Uniform Law Commission responded by updating the Uniform Act with the specific intention of addressing the outcry by fiduciaries struggling to maintain respectable rates of return, as required by the Uniform Prudent Investor Act, while satisfying their duty of impartiality.57 The prefatory note of the 1997 Uniform Act offers the following rationale behind its adoption:

Now it is time to update the principal and income allocation rules so the two bodies of doctrine can work well together. This revision deals

51. See Unif. Principal & Income Act (amended 1997), Prefatory Note, 7B U.L.A. 132 (2000). Although, these four questions are presented in the preface to the 1997 Act, they have consistently been the driving purpose behind each version of the Act. Id.
53. See Unif. Principal & Income Act (amended 1997), Prefatory Note, 7B U.L.A. 194 (2000). Specifically, “trustees who found it difficult to administer trusts under the older Act due to the development of new forms of investment property for trustees,” especially in “corporate distributions and also in the holding of mineral resources as a trust investment.” Id.
54. See DiRusso & Sablone, supra note 4, at 262.
55. See Wiensch & Beetz, supra note 37, at 44.
56. Id.
conservatively with the tension between modern investment theory and traditional income allocation. The starting point is to use the traditional system. If prudent investing of all the assets in a trust viewed as a portfolio and traditional allocation effectuate the intent of the settlor, then nothing need be done. The Act, however, helps the trustee who has made a prudent, modern portfolio-based investment decision that has the initial effect of skewing return from all the assets under management, viewed as a portfolio, as between income and principal beneficiaries... To leave a trustee constrained by the traditional system would inhibit the trustee’s ability to fully implement modern portfolio theory.  

Kentucky, which had adopted both the 1931 and 1964 versions of the Uniform Act, readily accepted the 1997 version of the Uniform Act, thereby ushering in a new regime of fiduciary asset management.  

III. THE KENTUCKY PRINCIPAL AND INCOME ACT  

The Kentucky Act is a significant departure from the rules which previously governed fiduciaries in that it seeks to integrate flexibility into principal and income management as a means of accommodating the total return approach to investment. Due to the Kentucky Act’s recent passage, there is little binding interpretive precedent on the subject; thus, the ensuing discourse merely surveys key provisions and points out notable distinctions between the Kentucky Act and the Uniform Act.  

A. Survey of Key Provisions  

The Kentucky Act is divided into five substantive articles governing the administrative lifecycle of an income interest in an estate or trust. Article 1 primarily sets forth the duties and powers that a fiduciary has in managing an income interest. Articles 2 and 3 detail the rules for determining income and principal.
apportioning receipts and disbursements between income and principal after a
decedent dies, in the case of an estate, or after an income interest in a trust
ends.\textsuperscript{65} Articles 4 and 5 cover the allocation of receipts and disbursements to
income or principal during the administration of an income interest.\textsuperscript{66} There is
actually a sixth article in the Kentucky Act; however, it merely recites the short
title of the act for reference purposes.\textsuperscript{67}

1. Article 1 - Definitions and Fiduciary Duties

i. Fiduciary Duties

A fundamental tenet of fiduciary law is strict adherence to the intent of a
testator or settlor.\textsuperscript{68} Presumably, a valid will or trust document is the purest
expression of such intent;\textsuperscript{69} thus, the terms of such instruments govern the
fiduciary in allocating receipts and disbursements to or between principal and
income.\textsuperscript{70} Article 1 of the Kentucky Act, acknowledging the primacy of intent,
requires fiduciaries to comply with the terms of the governing instrument,
whether a will or trust, even if those terms contradict other provisions of the
Kentucky Act.\textsuperscript{71} Anticipating instances when the governing instrument will be
silent on such matters, the Kentucky Act allocates all such receipts or
disbursements to principal, a default in the Kentucky Act that seems to favor
remaindermen, the presumptive beneficiaries of interests in principal.\textsuperscript{72}

Conveniently illustrating the tension inherent in income and principal
administration, the very next provision of Article 1 requires, again when the
governing instrument is silent, that the fiduciary “administer the trust or estate
impartially, based on what is fair and reasonable to all of the beneficiaries.”\textsuperscript{73} As
previously noted, impartiality is no simple task.\textsuperscript{74} A fiduciary must struggle to
balance the often competing interests of income beneficiaries and remaindermen,
as each has a strong preference as to whether a receipt from an investment lands

\textsuperscript{65} KY. REV. STAT. ANN. §§ 386.456-386.464.
\textsuperscript{67} KY. REV. STAT. ANN. §386.504.
\textsuperscript{68} Clay v. Crawford, 183 S.W.2d 797, 804 (1944) (stating that “[t]he fundamental rule in the
construction of a trust instrument is to ascertain the intent of the parties, particularly of the trustor.
That is to be done from the language employed, read in the light of the contemporary
circumstances, the object to be accomplished, and all other attendant facts actually or presumably
within the knowledge of the parties”).
\textsuperscript{69} Combs v. First Sec. Nat. Bank & Trust Co., 431 S.W.2d 719, 720 (1968).
\textsuperscript{70} KY. REV. STAT. ANN. § 386.452(1)(a) (LexisNexis 1999 & Supp. 2005).
\textsuperscript{71} KY. REV. STAT. ANN. § 386.452(2).
\textsuperscript{72} KY. REV. STAT. ANN. § 386.452(1)(d).
\textsuperscript{73} KY. REV. STAT. ANN. § 386.452(2) (emphasis added).
\textsuperscript{74} See Gillett & Guzman, supra note 2, at 1.
in the “income” account or the “principal” account. Fortunately, the Kentucky Act provides a means for ameliorating such discord.

ii. The Power to Adjust

Under the Kentucky Act, the most helpful tool a fiduciary has in balancing the financial interests of income beneficiaries and remaindermen is the power to adjust receipts and expenses between income and principal. This power is particularly useful in light of the aforementioned ascendance of “total return investing,” which rejects the practice of labeling returns as either income or principal and thereby, increases the potential for disproportionate investment yields favoring either the income beneficiaries or remaindermen. With the power of adjustment, a fiduciary can account for such variations on an annual basis by treating a receipt as income that would otherwise have been deemed principal and vice versa. In so doing, the fiduciary can more equitably negotiate tensions between beneficiaries, thereby fulfilling his or her duty of impartiality.

For example, the Kentucky Act allows a fiduciary to invest in assets that yield little income but have the potential for great capital appreciation. Generally, a capital gain dividend is treated as principal, which is not distributable to the income beneficiary. With the power to adjust however, the fiduciary can instead allocate a portion of the principal to income when the fiduciary sees a need to increase the amount of distributable income. In other situations, the fiduciary may allocate a portion of the estate or trust’s income to principal. For example, in a period of high inflation, the fiduciary may invest in bonds that provide a high return. To make up for the diminution of principal value attributable to inflation and other factors, the fiduciary may transfer annually a portion of the income that the bonds generate to principal.

It is important to emphasize that the power to adjust does not authorize a fiduciary to increase or decrease a beneficiary’s interest in income or principal.

75. DiRusso & Sablone, supra note 4, at 262-63.
80. The prudent investor rule found in KY. REV. STAT. ANN. § 286.3-277 (LexisNexis 2004 & Supp. 2006) embodies this idea.
83. Id. § 104 cmt., example (2), at 147.
84. Id.
85. Id.
86. Id. § 104 cmt., at 143.
It merely allows the fiduciary to reallocate income and principal when “the income component of a portfolio’s total return is too small or too large because” of the fiduciary’s investment decisions. The goal is to provide the fiduciary with a means of maximizing overall investment returns while still maintaining its duty of impartiality to all beneficiaries.

a. Requirements to Exercise the Power to Adjust.

Under the Kentucky Act, the following four requirements must be satisfied before a fiduciary can exercise the power to adjust:

1. The fiduciary must manage assets in accordance with the prudent investor rule, whether by law or election;

2. The governing instrument must describe the income beneficiary’s distribution rights with reference to “income” in the traditional trust accounting sense;

3. The fiduciary must be unable to administer the assets impartially with respect to all the beneficiaries; and

4. The adjustment must be approved by District Court.

With regard to the first requirement, in Kentucky the prudent investor rule governs all banks and corporate fiduciaries pursuant to KRS 286.3-277. Individual fiduciaries may elect to have KRS 286.3-277 apply to them as well pursuant to KRS 386.454(1); however, in either case, whether KRS 286.3-277 applies by law or election, the governing instrument must also enable the fiduciary to comply with the principles of prudent investment, i.e., it must not expressly prohibit it. Assuming the governing instrument makes such allowances, there would be no need to adjust between income and principal if the governing instrument did not also associate distributions with its income; thus, the second requirement, noted above, is met if the governing instrument also provides for an income beneficiary of some sort.

As already discussed, standards of prudent investment often result in disproportionate treatment of income beneficiaries and remaindermen from a financial standpoint. Hence, the third requirement that must be met before a fiduciary can adjust between income and principal is that the terms of the governing instrument and principles of prudent investment make it impossible

87. Id.
88. Id.
92. Id.
for the fiduciary to meet its duty of impartiality to all the beneficiaries. 93 If the fiduciary concludes that it cannot impartially administer the assets on behalf of the beneficiaries, then the fiduciary has satisfied the third requirement. 94

The Kentucky Act requires one last step before making an adjustment between income and principal. 95 The fiduciary must obtain District Court approval96 which, as defined by the Kentucky Act, requires the consent of all current beneficiaries and all “remainder beneficiaries in the oldest generation.” 97 This requirement of the Kentucky Act differs from the corresponding provisions of the Uniform Act98 which simply allow the fiduciary to use its own discretion in making adjustments based upon a list of several factors.99

Though ostensibly burdensome, the Kentucky Act’s fourth requirement does have at least two possible benefits. First, it reduces the potential for disgruntlement among the beneficiaries since they effectively have to consent to

93. Id.
94. Id.
95. Id.
96. Id.
97. Ky. Rev. Stat. Ann. § 386.450(3) (LexisNexis 1999 & Supp. 2005) (stating that “‘District Court approval’ means the consent of: (1) All current beneficiaries; (2) All remainder beneficiaries in the oldest generation; and (3) The court”). Questions have been raised as to what constitutes the oldest generation. Bruce K. Dudley, Kentucky Principal and Income Act, in PRACTICAL RISK MANAGEMENT FOR TRUSTEES AND OTHER FIDUCIARIES A-4 (Office of Continuing Legal Education, Univ. of Ky. College of Law 2005) (asking “[w]ho are the remainder beneficiaries in the oldest generation” and whether a grandchild counts as the remainder beneficiary in the oldest generation or if it is just the child of the settlor).
98. The corresponding section of the Uniform Act can be found in § 104. UNIF. PRINCIPAL & INCOME ACT § 104 (amended 1997), 7B U.L.A. 141 (2000).
99. The following are factors contained in § 104(b):
(1) The nature, purpose, and expected duration of the trust;
(2) the intent of the settlor;
(3) the identity and circumstances of the beneficiaries;
(4) the needs for liquidity, regularity of income, and preservation and appreciation of capital;
(5) the assets held in the trust; the extent to which they consist of financial assets, interests in closely held enterprises, tangible and intangible personal property, or real property; the extent to which an asset is used by a beneficiary; and whether an asset was purchased by the trustee or received from the settlor;
(6) the net amount allocated to income under the other sections of this [Act] and the increase or decrease in the value of the principal assets, which the trustee may estimate as to assets for which market values are not readily available;
(7) whether and to what extent the terms of the trust give the trustee the power to invade principal or accumulate income or prohibit the trustee from invading principal or accumulating income, and the extent to which the trustee has exercised a power from time to time to invade principal or accumulate income;
(8) the actual and anticipated effect of economic conditions on principal and income and effects of inflation and deflation; and
(9) the anticipated tax consequences of an adjustment.

the adjustment beforehand.\textsuperscript{100} Second, it prevents a beneficiary, who is serving as the fiduciary, from self-dealing by strictly prohibiting adjustments under such circumstances.\textsuperscript{101} As a practical matter, however, even though the Kentucky Act does not contain the list of considerations referenced under the Uniform Act,\textsuperscript{102} a prudent fiduciary should still take them into account when contemplating an adjustment.\textsuperscript{103}

Finally, the Kentucky Act also provides a list of specific circumstances when a fiduciary shall not be permitted to make an adjustment, despite having met the other statutory requirements.\textsuperscript{104} Generally, these prohibitions are intended to prevent unwanted tax consequences from occurring. For example, the Kentucky Act forbids adjustments that would diminish the income interest of a surviving spouse when an estate may be entitled to a marital deduction with respect to the trust in which the surviving spouse has a terminable interest.\textsuperscript{105} A fiduciary may also release the power to adjust, permanently or for a limited period of time, if

\begin{itemize}
  \item \textsuperscript{100} Morris, supra note 61, at 8.
  \item \textsuperscript{102} See supra note 95 for the list of factors.
  \item \textsuperscript{103} Morris, supra note 61, at 8 (stating that the rationale for the adjustment in consideration of the factors in the Uniform Act may also want to be presented to the district court when asking for approval).
    A fiduciary shall not make an adjustment: (a) \[that\] diminishes the income interest in a trust that requires all of the income to be paid at least annually to a spouse and for which an estate tax or gift tax marital deduction would be allowed, in whole or in part, if the fiduciary did not have the power to make the adjustment; (b) \[that\] reduces the actuarial value of the income interest in a trust to which a person transfers property with the intent to qualify for a gift tax exclusion; (c) \[that\] changes the amount payable to a beneficiary as a fixed annuity or a fixed fraction of the value of the trust assets; (d) \[from\] any amount that is permanently set aside for charitable purposes under a will or the terms of a trust unless both income and principal are so set aside; (e) \[if\] possession or exercising the power to make an adjustment causes an individual to be treated as the owner of all or part of the trust or estate for income tax purposes, and the individual would not be treated as the owner if the fiduciary did not possess the power to make an adjustment; (f) \[if\] possessing or exercising the power to make an adjustment causes all or part of the trust or estate assets to be included for estate tax purposes in the estate of an individual who has the power to remove a fiduciary, appoint a fiduciary, or both, and the assets would not be included in the estate of the individual if the fiduciary did not possess the power to make an adjustment; (g) \[if\] the fiduciary is a beneficiary of the trust of estate; or (h) \[if\] the fiduciary is not a beneficiary, but the adjustment would benefit the fiduciary directly or indirectly; except that any effect on the fiduciary’s compensation shall not preclude an adjustment so long as the fiduciary’s fees are reasonable and otherwise comply with the applicable law.
  \item \textsuperscript{105} Id. at § 386.454(4)(a).
\end{itemize}
the fiduciary is concerned that holding or exercising the power may impose unwanted tax burdens or cause other tax-related problems.106

b. Conversion to Unitrust

Another difference between the Kentucky Act and the Uniform Act is that the Kentucky Act includes, under its power of adjustment provision, the ability to convert to a unitrust payout.107 This approach effectively allows the fiduciary to define “income” as an annual distribution equal to 3% to 5% of the net fair market value of the trust’s assets as determined at the end of the calendar year, regardless of whether such assets would otherwise be considered income or principal as traditionally defined by state law.108

By converting to a unitrust payout, a fiduciary can better allocate the benefits of the trust between current and future beneficiaries, thereby, enabling the trustee to satisfy its duty of impartiality while simultaneously investing to maximize total return.109 A unitrust can also be administratively simpler for the fiduciary because the income beneficiary is entitled to a certain percentage and all beneficiaries generally understand the calculation.110 Furthermore, because a certain sum can be distributed on a regular basis, a unitrust may allow an income beneficiary to better plan his or her finances.111

Although a unitrust approach carries some welcome benefits, at times it can be overly strict and inflexible.112 For example, if a fiduciary converts to a unitrust payout, the income beneficiary will receive the designated percentage of the assets yearly, an approach that may not allow a trustee to withhold income if circumstances warrant.113 If the trustee does wish to withhold the unitrust

106.  Id. at § 386.454(6).
107.  Id. at § 386.454(2) (providing in part that that “[a] trustee may adjust between principal and income to the extent . . . the trustee determines after applying the rules in KRS 386.452(1), that the trustee is unable to comply with KRS 386.452(2) and the adjustment, including an adjustment method such as an annual percentage distribution if the percentage is not less than three percent (3%) nor more than five percent (5%) of the fair market value of the trust assets determined annually . . .”).
108.  Id. For a detailed discussion of the procedures used to convert to a unitrust, see Wayne F. Wilson, Uni-trust Conversion Procedure Under Kentucky’s Principal and Income Act, in PRACTICAL RISK MANAGEMENT FOR TRUSTEES AND OTHER FIDUCIARIES C-11 (Office of Continuing Legal Education, Univ. of Ky., College of Law., 2005).
109.  Morris, supra note 61, at 6. Trustees can also better achieve impartiality if a unitrust is adopted. James P. Teufel, Beware the Unitrust Conversion, TRUSTS & ESTATES, Apr. 2003, at 60.
111.  Id. A beneficiary could receive a unitrust distribution quarterly or even monthly. Id. at 19.
112.  Morris, supra note 61, at 6.
113.  Id. This may happen when an income beneficiary does not need the income or receiving the income will create adverse tax consequences. Id.
income distribution, the district court must once again approve. Also, there is some uncertainty as to whether a conversion to a unitrust is a taxable event.

2. Article 2 - Decedent's Estate or Terminating Income Interest

Article 2 details the powers and responsibilities of a fiduciary when an income interest in a trust or estate ends. Among those responsibilities, a fiduciary must determine the amount of net income and net principal to be received by a remainder beneficiary. The fiduciary also has the discretion to pay and deduct administration expenses and interest on death taxes from either income or principal; however, death taxes, funeral expenses, and debts must be paid from the principal. Permitting the fiduciary to choose the source of payment for such expenses eliminates the need to adjust between principal and interest that may arise when, for example, an expense that is paid from principal is deducted for income tax purposes or an expense that is paid from income is deducted for estate tax purposes.

When handling distributions to residuary and remainder beneficiaries, the fiduciary is to pay these beneficiaries the net income earned during the period of administration on the basis of each beneficiary's proportionate interest in the undistributed assets. Determination of proportionate interest is based upon asset values as of the date reasonably near the time of distribution, rather than the "date of death" values.

3. Article 3 - Apportionment at Beginning and End of Income Interest

Article 3 covers the apportionment of receipts and disbursements at the beginning and end of an income interest of a trust or estate. According to Article 3, an income interest begins on the date (1) specified in the trust

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114. Id.
115. Teufel, supra note 109, at 60.
118. Ky. Rev. Stat. Ann. § 386.456(2)(b). However, interest on death taxes may be paid from income provided that estate tax marital or charitable deduction will not be affected. Unif. Principal & Income Act § 201(2)(B) cmt. (amended 1997), 7B U.L.A. 152 (2000). Interest on estate and inheritance taxes may be deducted for income tax purposes without having to reduce the estate tax deduction for amounts passing to a charity or surviving spouse, whether the interest is paid from principal to income. Id.
120. Henry C.T. Richmond, III, Kentucky Principal and Income Act, in 31st Annual Midwest/Midsouth Estate Planning Institute B-12 to -13 (Office of Continuing Legal Education, Univ. of Ky. College of Law 2004).
document or (2) when an asset becomes “subject to a trust or successive income interest."\(^{124}\) Likewise, Article 3 provides the end date of an income interest is “[(1)] the day before an income beneficiary dies or [(2)] . . . on the last day of a period during which there is no beneficiary to whom a trustee may distribute income.”\(^{125}\)

Article 3 then sets forth the following rules for apportioning receipts and disbursements when a decedent dies or an income interest begins:\(^{126}\)

i. Periodic Payments

Periodic receipts such as rents, dividends, interest and annuities, and disbursements such as the interest portion of a mortgage payment, are allocated to principal if they are due but unpaid before an income interest begins or the date a decedent dies.\(^{127}\)

ii. Nonperiodic Payments

Nonperiodic receipts and disbursements, such as interest on an income tax refund, would be apportioned to principal to the extent it accrues before an income interest begins (or the date a decedent dies) and income if it accrues after the income interest begins (or the date a decedent dies).\(^{128}\)

iii. Undistributed Income

Generally, an income beneficiary, or the estate of that beneficiary if the income interest terminates upon death, is entitled to “undistributed income,” which is “income received before the date on which an income interest ends.”\(^{129}\)

If the income beneficiary has the power to revoke more than 5% of the trust; however, the undistributed income attributable to the revocable portion of the trust is apportioned to principal.\(^{130}\)

The Kentucky Act adds a provision when dealing with charitable beneficiaries which allows a settlor to change the charitable beneficiary prior to the distribution of any undistributed income, “so long as the change does not

\(^{124}\) KY. REV. STAT. ANN. § 386.460(1). In the case of a testamentary trust, an asset becomes “subject to a trust” on the date of a testator’s death; or, in the case of an inter vivos trust, on the date it is transferred to the trust. \textit{Id.} at § 386.460(2).

\(^{125}\) \textit{Id.} at § 386.460(4).

\(^{126}\) \textit{See} KY. REV. STAT. ANN. §§ 386.460 to 386.464.

\(^{127}\) KY. REV. STAT. ANN. § 386.462(2); UNIF. PRINCIPAL & INCOME ACT § 302 (amended 1997), 7B U.L.A. cmt. 156-57 (2000). Thus, this takes on the original common law rule that periodic payments such as rents, dividends, interest, annuities and disbursements are not apportioned. \textit{Id.}

\(^{128}\) KY. REV. STAT. ANN. § 386.462(2). If the due date occurs \textit{after} the date of death, the receipt or disbursement is allocated to income. \textit{Id.}

\(^{129}\) \textit{Id.} at § 386.464(1).

\(^{130}\) \textit{Id.} at § 386.464(2).
alter the income, gift, estate, or other tax benefits available under the terms of the trust.”131

4. Article 4 - Allocation of Receipts During Administration of Trust

Article 4 provides for the proper allocation between income and principal of assets received during administration.132 Article 4 can be divided into three parts: (1) receipts from entities, (2) receipts not normally apportioned, and (3) receipts normally apportioned.133

i. Receipts from Entities

The Kentucky Act defines “entity” as “a corporation, partnership, limited liability company, regulated investment company, real estate investment trust, common trust fund, or any other organization in which a trustee has an interest other than a trust or estate . . . .”134 Generally, receipts from entities are allocated to income;135 however, receipts of the following items are instead allocated to principal: (1) “[p]roperty other than money;”136 (2) “[m]oney received in one (1) distribution or a series of related distributions in exchange for part or all of a trust’s interest in the entity;”137 (3) “[m]oney received in total or partial liquidation of the entity;”138 and (4) “[m]oney received from an entity that is a regulated investment company or a real estate investment trust, if the money distributed is a capital gain dividend for federal income tax purposes.”139 Also, a trustee shall allocate an income distribution from another trust or estate to income and a principal distribution to principal provided that the other trust or estate does not specify otherwise.140

ii. Receipts That Are Not Normally Apportioned

Receipts of the following types of assets are allocated to principal: (1) money “received from the sale, exchange liquidation, or change in form of a principal asset, including stock splits. . . .”141 (2) “[a]mounts recovered from

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131. Id. at § 386.464(3).
134. Ky. Rev. Stat. Ann. § 386.466(1). Note that a property held in tenancy in common or a joint venture is not included. Richmond, supra note 120, at B-16.
135. Ky. Rev. Stat. Ann. § 386.466(2). A number of exceptions apply where receipts received from an entity are allocated to principal. Id. at § 386.466(3).
136. Id. at § 386.466(3)(a).
137. Id. at § 386.466(3)(b).
138. Id. at § 386.466(3)(c).
139. Id. at § 386.466(3)(d).
third parties;” 142 (3) “[n]et income received in an accounting period during
which there is no beneficiary to whom a trustee may or shall distribute
income;” 143 and (4) “options to buy property from the trust.” 144 Also, generally,
life insurance proceeds or similar contracts that insure trusts assets are allocated
to principal.145 Items that are usually allocated to income include receipts from
rental property146 and any interest received from obligations owed to the
trustee.147

iii. Receipts That Are Normally Apportioned

Under the Kentucky Act, receipts from deferred compensation, annuities and
similar payments are apportioned between income and principal.148 To the
extent that a payment is required to be made, pursuant to the required minimum
distribution rules for qualified retirement plans and individual retirement
accounts, 10% of any receipts are allocated to income and the balance is
allocated to principal.149 Any other receipts from such plans, including private
or commercial annuities, and pension, profit-sharing, stock-bonus, or stock-
ownership plans are allocated to principal.150 Receipts from liquidating assets,
such as leasehold interests or patent, copyright and royalty rights, are allocated
similarly, with 10% going to income and the rest to principal.151 Article 4
concludes with detailed rules for the apportionment of receipts from interests in
minerals, water, and other natural resources,152 including timber.153

142. Id. at § 386.470(3).
143. Id. at § 386.470(5).
144. Id. at § 386.470(6).
145. Ky. Rev. Stat. Ann. § 386.476(1). However, assets received from “a contract that
insures the trustee against loss of occupancy or other use by an income beneficiary, loss of income,
or loss of profits from a business” are allocated to income. Id. at § 386.476(2).
received from the sale, redemption, or other disposition of an obligation to pay money to the trustee . . .” Id. at § 386.474(2).
149. Id. at § 386.480(3). Special rules come into play if the IRA names a QTIP trust as a
beneficiary. See infra Part IV.C.2 and accompanying text.
150. Id. at § 386.480(2) (providing that if a payment is received and it is characterized as
income or a dividend, then that payment should be allocated to income).
152. Ky. Rev. Stat. Ann. § 386.484. A rental or lease receipt is allocated to income. Id. at § 386.484(1)(a). If money received from a “royalty, shut-in-well payment, take-or-pay payment, [or]
a bonus . . . is more than nominal,” 90% is allocated to principal and the remaining is allocated to
income. Id. at § 386.484(1)(c).
of timber removed from the land that does not exceed the rate of growth of the timber during the
accounting periods” should be allocated to income. Id. at § 386.486(1)(a). Additionally, if “the
amount of timber removed from the land exceeds the rate of growth of the timber or the net
receipts are from the sale of standing timber,” then this is allocated to principal. Id. at § 386.486(1)(b).
5. Article 5 - Allocation of Disbursements During Administration of Trust

Article 5 of the Kentucky Act covers the allocation of disbursements between income and principal during administration of an income interest.154

i. Disbursements from Income or Principal

Generally, trustee commissions, and investment advisory or custodial services, are paid half from income and half from principal.155 Fees for accountings, judicial proceedings and other expenditures benefiting both the income and remainder beneficiaries are also divided equally between income and principal.156 Alternatively, all ordinary expenses incurred in connection with the administration of the trust (“including interest, ordinary repairs, regularly recurring taxes”) are paid solely from income,157 while disbursements related to environmental matters, inheritance taxes, and payments of principal on trust debts are payable from principal.158

ii. Adjustments Between Income and Principal

Under Article 5 of the Kentucky Act, a trustee can reimburse principal with receipts otherwise allocable to income if the receipt is “from a principal asset that is subject to depreciation,” unless the depreciable property is tangible personal property or real property being used by the beneficiary as a residence.159 This rule only applies to trusts, not estates, because estates are intended to be open for only a limited period and, as such, remaindermen of an estate are not materially disadvantaged by the impact of depreciation.160 Article 5 of the Kentucky Act also permits reimbursements from income to principal for such things as: 1) extraordinarily large repairs paid from principal; 2) capital improvements to a principal asset; 3) disbursements made to prepare property for rental; and 4) disbursements for environmental matters pertaining to principal assets.161

154. KY. REV. STAT. ANN. §§ 386.490-386.502 (comprising Article 5 of the Kentucky Act entitled Allocation of Disbursements During Administration of Trust).
155. KY. REV. STAT. ANN. § 386.490(1).
156. Id. at § 386.490(2).
157. Id. at § 386.490(3).
158. KY. REV. STAT. ANN. § 386.492.
159. KY. REV. STAT. ANN. § 386.494(2).
160. Id. at § 386.494(2)(b).
161. KY. REV. STAT. ANN. § 386.496(2). This includes:
(a) an amount chargeable to income but paid from principal because it is unusually large, including extraordinary repairs; (b) capital improvement to a principal asset, whether in the form of changes to an existing asset or the construction of a new asset, including special assessments; (c) disbursements made to prepare property for rental, including tenant allowances, leasehold improvements, and broker's commissions; (d) payments on an obligation secured by a principal asset to the extent that the amount transferred
Article 5 of the Kentucky Act also deals with income taxes, and adjustments to be made between income and principal as a result of payment of those taxes. Generally, a trustee must pay income tax on receipts allocated to income from income and must pay tax on receipts allocated to principal from principal, including payment of taxes passed through from an entity, such as a partnership. When the respective tax liabilities of the income beneficiary and remaindermen are imbalanced, the Kentucky Act allows the trustee to make adjustments, with District Court approval, between income and principal to help balance their burdens.

IV. TAX IMPLICATIONS

As discussed above, Kentucky and other states that have adopted the Uniform Act provide the fiduciary with significant leeway in defining “income” in various administrative contexts. To keep up with changing state law notions of what constitutes “income,” the IRS revised its definition of “income” for tax purposes to provide guidance to fiduciaries on the tax ramifications of their allocations and apportionments. Finalized on December 31, 2003, these “Final Regulations” generally apply to trusts and estates for tax years ending after January 2, 2004.

A. Definition of Income

Traditional notions of income and principal for fiduciary accounting purposes are still respected under the Final Regulations; thus, dividends, interest, and (e) disbursements described in KRS 386.492(1)(g).

162. KY. REV. STAT. ANN. § 386.498.
163. Id.
164. KY. REV. STAT. ANN. § 386.500(1).
165. I.R.C. § 643(b) (West 2000). The definition of income “is intended to be consistent with traditional fiduciary accounting principals.” Leigh McKee, Kentucky Principal & Income Act & Related Final Regulations, Bluegrass Estate Planning Council Meeting (Nov. 2004). I.R.C. § 643 distinguishes income from distributable net income (DNI). I.R.C. § 643(a), (b) (West 2000). DNI is “used to determine how much of an amount paid, credited, or required to be distributed to a beneficiary will be includible in his gross income.” Treas. Reg. § 1.643 (a)-0 (2006). Specifically, DNI “is the taxable income of the trust modified by generally excluding dividend distributions, personal exemptions, capital gains and losses, extraordinary dividends and taxable stock dividends, and including tax exempt interest.” IRS, Glossary of Trust Terms, http://www.irs.gov/businesses/small/article/0,,id=106554.00.html (last visited February 1, 2007). In other words, DNI is net income modified by the rules under IRC § 643 and distributed to beneficiaries. Suzanne Baillie Schmitt, Practice Alert: IRS Revises the Definition of Trust Income to Reflect Changing State Law Concepts, ESTATE PLANNER’S ALERT, Apr. 2004, at 5. This is the income the beneficiary claims as gross income on his personal income tax return. Id. If the income is not included in the DNI, then it is taxed to the trust. Id.
167. Id. However, a trust which defines income not consistent with IRC § 643 or the Kentucky Act will not be given favorable tax treatment. McKee, supra note 163.
and rents, will generally be allocated to income and proceeds from the sale or exchange of trust assets, i.e., capital gains, will be allocated to principal.\textsuperscript{168} However, the Final Regulations now accept state law variations of these general allocation rules so long as the state law changes maintain a “reasonable apportionment between the income and remainder beneficiaries of the total return of the trust for the year . . . .”\textsuperscript{169} Under the Final Regulations, such “reasonable apportionments” include:

(1) A unitrust amount of no less than 3 \%, and no more than 5 \%, of the trust’s fair market value, whether that value is determined each year or averaged on a multiple year basis; and

(2) Any adjustments between income and principal that are needed to fulfill the fiduciary’s duty of impartiality between the income and remainder beneficiaries.\textsuperscript{170}

Accordingly, under the Kentucky Act, a fiduciary’s conversion of a beneficiary’s “all income” interest to a 3\% to 5\% unitrust payout or reasonable adjustment between income and principal to maintain impartiality among income and remaindermen will be considered a “reasonable apportionment” of a trust’s total return and will, thereby, be respected by the IRS for fiduciary accounting purposes.\textsuperscript{171}

The Final Regulations also describe the rules for switching between methods of distributing income.\textsuperscript{172} If the fiduciary complies “with all requirements of the state statute for switching methods,” and if the methods are authorized by state statute, then the switch does not constitute “a recognition event for [income tax] purposes . . . and will not result in a taxable gift from the trust’s grantor or any of the trust’s beneficiaries.”\textsuperscript{173}

\begin{footnotesize}
\begin{enumerate}
\item\textsuperscript{168} Treas. Reg. § 1.643(b)-1 (2006).
\item\textsuperscript{169} \textit{Id.} This section provides that: 
\end{enumerate}
\begin{itemize}
\item An allocation of amounts between income and principal pursuant to applicable local law will be respected if local law provides for a reasonable apportionment between the income and remainder beneficiaries of the total return of the trust for the year, including ordinary and tax-exempt income, capital gains, and appreciation.
\end{itemize}
\item\textsuperscript{170} Also note that a state statute that permits the trustee to make adjustments between income and principal to fulfill the trustee’s duty of impartiality between the income and remainder beneficiaries is generally a reasonable apportionment of the total return of the trust. \textit{Id.}
\item\textsuperscript{171} McKee, \textit{supra} note 165.
\item\textsuperscript{172} KY. REV. STAT. ANN. § 386.454 (LexisNexis 1999 & Supp. 2005); Morris, \textit{supra} note 61, at 7.
\item\textsuperscript{173} Treas. Reg. § 1.643(b)-1 (2006).
\item\textsuperscript{173} \textit{Id.}
\end{footnotesize}
B. Treatment of Capital Gains

As a general rule, capital gains and losses are allocated to principal for fiduciary accounting purposes;\textsuperscript{174} thus, the remainder beneficiaries of a trust or the residuary beneficiaries of an estate usually pay tax on net gains for Federal tax purposes.\textsuperscript{175} There are, however, exceptions to this general rule if the terms of the governing instrument and applicable local law provide otherwise, or if the fiduciary decides otherwise pursuant to a reasonable and impartial exercise of its discretion (in accordance with the governing instrument and applicable local law). When such conditions are met, capital gains may be allocated to distributable net income (“DNI”)\textsuperscript{176} for Federal tax purposes in the following three situations:\textsuperscript{177}

1. When the fiduciary allocates the gains to income and treats them as such for fiduciary accounting purposes;\textsuperscript{178}

2. When the fiduciary allocates the gains to principal but, for fiduciary accounting purposes, consistently treats the gains as having been distributed to income beneficiaries during the taxable year;\textsuperscript{179} or

3. When the fiduciary allocates the gains to principal but actually distributes the gains to income beneficiaries or uses the gains to determine the amount that is distributed or required to be distributed to a beneficiary.\textsuperscript{180}

There are fourteen examples in the Final Regulations that illustrate these three situations in which capital gains can be allocated to DNI, all of which emphasize the importance of a fiduciary’s consistency in handling the allocations after the first year in which such treatment commenced.\textsuperscript{181}

\textsuperscript{174} KY. REV. STAT. ANN. § 386.470(2) (LexisNexis 1999 & Supp. 2005).
\textsuperscript{175} Morris, supra note 61, at 7.
\textsuperscript{176} Treas. Reg. § 1.643(a)-0 (2006). This section provides that: [DNI] limits the deductions allowable to estates and trusts for amounts paid, credited, or required to be distributed to beneficiaries and is used to determine how much of an amount paid, credited, or required to be distributed to a beneficiary will be includible in his gross income. It is also used to determine the character of distributions to the beneficiaries.
\textsuperscript{177} Treas. Reg. § 1.643(a)-3(b) (2006).
\textsuperscript{178} Treas. Reg. § 1.643(a)-3(b)(1).
\textsuperscript{179} Treas. Reg. § 1.643(a)-3(b)(2).
\textsuperscript{180} Treas. Reg. § 1.643(a)-3(b)(3). Note that this exception requires that the capital gains actually be distributed, requiring a tracing of the actual capital gains realized. Id.
\textsuperscript{181} Treas. Reg. § 1.643(a)-3 (2006).
C. Impact on Various Types of Trusts

1. Marital Deduction Trusts

   i. Qualified Terminable Interest Trusts

   If the assets of a trust are to qualify for the federal estate tax marital deduction as qualified terminal interest property (“QTIP”), (1) the surviving spouse must be entitled to all of the income from the trust for life and (2) no person can have the power to appoint the property to anyone other than the surviving spouse.182 The Final Regulations provide that a surviving spouse’s interest in a trust meets the income requirement if the governing instrument and applicable local law provide the surviving spouse with a “reasonable apportionment” of the trust’s total return for the year.183 Thus, a spouse who, as the income beneficiary, is entitled to a unitrust amount between 3% and 5%, as provided under the Kentucky Act, is deemed to be entitled to all the income for purposes of qualifying the trust for the estate and gift tax marital deduction.184

   The Final Regulations also clarify that the power of a trustee to adjust between income and principal to fulfill the trustee’s duty of impartiality between the income and remainder beneficiaries will not be considered a power to appoint trust property to a person other than the surviving spouse and will not disqualify the trust from satisfying the second prong of the QTIP marital deduction requirements.185

2. IRA Payable to a QTIP Trust

   When an individual retirement account (“IRA”) or similar defined contribution plan186 is payable to a QTIP trust as beneficiary, the IRS views the IRA and the trust itself as two separate items of QTIP; thus, all the income from the trust and the IRA must be distributed to the surviving spouse for life in accordance with the aforementioned QTIP requirements.187 In Revenue Ruling 2006-26, the IRS clarifies that, under the Final Regulations, the “all income” requirement for QTIP treatment is satisfied if the surviving spouse is entitled to the entire IRA’s internal investment income or a 3% to 5% “unitrust” payout of the IRA’s total assets on an annual basis.188

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186. See I.R.C. § 4974(c) (West 2000) for a list of retirement plans which are affected by Rev. Rul. 2006-26.
188. Id.
Revenue Ruling 2006-26, outlining three situations in which a QTIP trust is named as a beneficiary of an IRA, is careful to distinguish between a trustee’s allocation of receipts from an IRA pursuant to state law and the qualification of an IRA for QTIP treatment under the Internal Revenue Code. With regard to the allocation of trust receipts, section 409 of the Uniform Act (and the corresponding section 16 of the Kentucky Act) directs a trustee to allocate 10% of any “required” distributions from an IRA to trust income and 90% to trust principal. All other distributions from IRAs are completely allocable to principal. In seeking to qualify the IRA for QTIP treatment, however, the “10 percent rule” of the Uniform Act (and Kentucky Act) has no bearing as it is an administrative rule for trustees seeking to allocate trust receipts. Hence, reliance on the “10 percent rule” for tax purposes would jeopardize the marital deduction.

3. Generation-Skipping Transfer Tax Trusts

Trusts that were irrevocable on or before September 25, 1985 are generally exempt from the generation-skipping transfer (“GST”) tax. As such, these “grandfathered” trusts can make distributions to individuals that are two or more generations below the original transferor without incurring GST tax liability. With the widespread adoption of the Uniform Act, however, some practitioners questioned whether a trustee’s conversion to a unitrust payout or adjustment between income and principal would cause a “grandfathered” trust to lose its GST tax exempt status. The Final Regulations make clear that such trusts will remain exempt from GST tax as long as the “applicable local law provides for a reasonable apportionment between the income and remainder beneficiaries of the total return of the trust and meets the requirements of § 1.643(b)-1 . . . .” As noted above, the provisions of the Kentucky Act are within the “reasonable apportionment” requirement; thus, a trustee of a “grandfathered” trust duly exercising its powers under the Kentucky Act will not risk the trust’s GST tax-exempt status.

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189. Id.
191. Id.
193. Id. A trust may have to be amended if it only specifies that the spouse is entitled to all the income of the trust, but fails to mention income of the IRA. Id.
195. Id.
198. Id.
4. Charitable Remainder Trusts

The Final Regulations provide that income of a charitable remainder unitrust (“CRUT”) “may not be determined by reference to a fixed percentage of the annual fair market value of the trust property.” The rationale for this provision is that the unitrust amount of a CRUT cannot be less than 5% of the value of the trust assets; thus, a state law permitting a lower unitrust payout runs afoul of this requirement on its face. In addition, the Final Regulations provide that proceeds from the sale or exchange of any assets contributed to a CRUT by its grantor or from the sale or exchange of any assets purchased by a CRUT “must be allocated to principal and not to trust income at least to the extent” of the fair market value of the assets on the date of their contribution or the purchase price of those assets. Otherwise, proceeds from the sale or exchange of any assets may be allocated to income under the governing instrument, if not prohibited by local law.

V. CONCLUSION

It is nearly impossible for a fiduciary to satisfy completely the demands of income beneficiaries and remaindermen when each is ultimately vying for a greater share of the same property. Clearly, a sound grasp of the key provisions of the Uniform Act and the history behind them will aid fiduciaries feeling hamstrung by their obligations to these beneficiaries. The Kentucky Act, though effectively the same as the Uniform Act, contains a few significant operational departures, chief among them the requirement for District Court approval in matters left to the fiduciary’s discretion under the Uniform Act. Regardless, the Uniform Act and its state law counterparts, like the Kentucky Act, are a significant improvement from the inconsistencies and uncertainties of prior law, allowing fiduciaries to serve the best interests of the beneficiaries that depend on them.

200. Id.
201. Id.
202. Id.
203. The coauthors gratefully acknowledge the thoughtful guidance of Leigh McKee and Henry C.T. (Tip) Richmond III in researching and writing this article.
# Appendix A

Kentucky Principal and Income Act  
Comparison of Provisions prior to January 1, 2005 with Provisions after December 31, 2004

<table>
<thead>
<tr>
<th>Income Item</th>
<th>Income</th>
<th>Old Act</th>
<th>Principal</th>
<th>Income</th>
<th>New Act</th>
<th>Principal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent</td>
<td>Rent, including sums for cancellation or renewal.</td>
<td>Rent, including sums for cancellation or renewal.</td>
<td>Refundable deposits held subject to terms of lease until lease terms are satisfied.</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Interest</td>
<td>Interest on loans, including prepayment penalties.</td>
<td>No provision for premium amortization.</td>
<td>Interest, including prepayment penalties, no provision for premium amortization.</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Discount Obligations (e.g. T-bills, savings bonds, zero-coupon bonds, discount bonds, inflation indexed bonds)</td>
<td>Some allocation of discount and tax on OID to income.</td>
<td>Proceeds from sale, redemption, etc of bonds that mature within 1 year of purchase or acquisition by trustee, to the extent the proceeds exceed cost/value at time of acquisition.</td>
<td>Proceeds from sale, redemption, etc of debt received more than 1 year after acquisition by trustee.</td>
<td></td>
<td></td>
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<tr>
<td>Natural resources other than timber</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Delay/annual rentals</td>
<td>Income</td>
<td>Income - nominal amounts only.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Royalties, mining interests, net profit interests</td>
<td>Remainder</td>
<td>Depletion allowance based on tax depletion, but not in excess of 50%.</td>
<td>10% - includes delay/annual rentals that are more than nominal. 90% - includes delay/annual rentals that are more than nominal.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Renewable water</td>
<td>Income</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Proceeds from disposals</td>
<td>Allocated in same manner as receipts.</td>
<td>Income and principal from mineral interests owned on 1/1/2005 may be allocated under new law or prior law. Interests acquired after 1/1/2005 allocated based on new law.</td>
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<tr>
<td>Timber</td>
<td>Allocation to be reasonable and equitable.</td>
<td>To the extent that timber removed does not exceed growth.</td>
<td>To the extent that timber removed exceeds growth or receipts from sale of standing timber.</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Other liquidating property - e.g., leaseholds, patents, copyrights, etc.</td>
<td>Receipts from the property not in excess of 5% per year of its inventory value - KRS 386.285 - Other depletable property - refers specifically only to depreciable comp.</td>
<td>Remaining amount.</td>
<td>10% of receipts. Remaining amount.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Entities</td>
<td>Dividends - corporations only</td>
<td>Proceeds from sale, call, merger, reorg, total or partial liquidation, stock dividends, stock splits - corporations only.</td>
<td>Money received, generally. Tax on liquidating distributions due from trustee or beneficiary. Property other than money. Liquidating distributions (including when the distribution is greater than 20% of the entity's gross assets).</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital gain dividends from RICs and REITs</td>
<td>Ordinary income</td>
<td>All other distributions</td>
<td>All other distributions. Capital gain dividends.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Receipts from sale of unproductive property</td>
<td>Special allocation.</td>
<td>Spouse may require trust assets to be productive if a marital deduction was allowed. Otherwise, principal.</td>
<td></td>
<td></td>
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<tr>
<td>Granting an option</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Deferred comp, annuities, retirement plans</td>
<td></td>
<td>Option proceeds.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>If some part of the payment is characterized as interest or dividends</td>
<td>Receipts from the property not in excess of 5% per year of its inventory value.</td>
<td>Remaining amount.</td>
<td>Amounts characterized as interest or dividends. Amounts other than those characterized as interest or dividends.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>If no part of the payment is characterized as interest or dividends</td>
<td></td>
<td>10% of the amount required to be paid. If necessary to obtain the marital deduction, the additional amount so required.</td>
<td></td>
<td>Remaining amount.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
I got a great plea agreement for my client but he ended up being deported - Immigration Considerations For the Kentucky Criminal Practitioner

Matthew L. Benson, Esq.∗ and Marisa N. Palmieri†

I. INTRODUCTION

A. Goals of This Article and Effectively Representing Non-Citizen Criminal Defendants

The purpose of this survey article is to provide Kentucky criminal practitioners with a useful tool in determining how to effectively represent non-citizen criminal defendants. While there is minimal Kentucky law that focuses on the required standards for representing non-citizen criminal defendants, this survey focuses on current Kentucky law and provides suggestions on how to effectively represent non-citizen criminal defendants. Furthermore, this survey discusses the potential immigration consequences that may result from criminal convictions of non-citizens and provides considerations that should be taken into account by criminal defense attorneys in zealously representing their non-citizen clients.

Section II of this survey is broken down into four subsections. Subsection A discusses what constitutes ineffective assistance of counsel and ineffective assistance claims arising out of plea agreements. Subsection B analyzes current Kentucky law regarding the failure of counsel to advise non-citizen criminal defendants concerning potential immigration consequences that may result from criminal convictions, as well as erroneously advising the client regarding immigration consequences. Subsection C discusses the immigration consequences that should be considered when advising non-citizen criminal defendants on how best to proceed with a pending criminal matter. Finally, subsection D discusses what constitutes a “conviction” for immigration purposes and how it often differs from what constitutes a “conviction” under traditional thinking. Furthermore, Section III of this article provides a proposal

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† Marisa N. Palmieri is a J.D. candidate for 2008 at Salmon P. Chase College of Law, Northern Kentucky University. Marisa earned her B.B.A. in Marketing and Management from the University of Kentucky in 2005.
for Kentucky to adopt a standard requiring trial courts or criminal defense attorneys to make non-citizen criminal defendants aware of potential immigration consequences resulting from criminal convictions.

B. Impact of Immigration Consequences on Non-Citizen Criminal Defendants

As a result of the Illegal Immigration Reform and Immigrant Responsibility Act of 1996 (IIRIRA), non-citizens who are convicted of relatively minor crimes, including misdemeanors, may now face harsh immigration consequences. When the IIRIRA was passed, it not only expanded the criminal grounds for inadmissibility and deportability, but it also restricted the relief available to criminal non-citizens in removal proceedings as well as waivers available to non-citizens seeking admission to the United States. While avoiding trial and entering into plea agreements often seem like the most intelligent alternative for criminal defendants, facing immigration consequences such as deportation are often a much more serious consequence.

Unfortunately, non-citizen defendants are often not being properly advised of potential immigration consequences that may result from a criminal conviction.

5. See INA § 240A(a)(3), 8 U.S.C. § 1229b(a)(3) (2000 & Supp. I 2004) (noting that a non-citizen defendant convicted of an aggravated felony cannot receive a grant of cancellation of removal by the attorney general); See also INA § 242(a)(2)(C), which states: Notwithstanding any other provision of law . . . no court shall have jurisdiction to review any final order of removal against an alien who is removable by reason of having committed a criminal offense covered in section 212(a)(2) [aliens ineligible for admission based on certain criminal convictions] or 237(a)(2)(A)(ii), (B), (C), or (D) [classes of deportable aliens based on criminal convictions], or any offense covered by section 237(a)(2)(A)(ii) [multiple convictions] for which both predicate offenses are, without regard to their date of commission, otherwise covered by section 237(a)(2)(A)(i) [crimes of moral turpitude].
6. United States v. Del Rosario, 902 F.2d 55, 61 (D.C. Cir. 1990) (Mikva, J., concurring) (quoting Ng Fung Ho v. White, 259 U.S. 276, 284 (1922)) (“Deportation is indeed a ‘harsh collateral consequence.’ It can result ‘in loss . . . of all that makes life worth living.’”). See also Justmann, supra note 3, at 704.
conviction. In many jurisdictions, including Kentucky, neither the court nor the defendant’s counsel has a duty to investigate or inform the non-citizen criminal defendant of potential immigration consequences that could result from a criminal conviction. Although this is the current standard adopted by Kentucky, it is important for Kentucky criminal practitioners to effectively and zealously represent non-citizen clients by becoming aware of and making non-citizen clients aware of potential immigration consequences resulting from criminal convictions. While consequences such as deportation, inadmissibility, and ineligibility for naturalization may be considered collateral to the criminal penalty imposed, it is paramount that these consequences are taken into account by criminal practitioners before advising a non-citizen client, as often times these immigration consequences are much more serious and harmful to the non-citizen than the potential criminal penalties that may be imposed. The same cannot generally be said for other collateral consequences resulting from criminal convictions.

II. DISCUSSION

A. Ineffective Assistance of Counsel

The United States Constitution guarantees a right to effective assistance of counsel. Specifically, the Sixth Amendment states that “in all criminal prosecutions, the accused shall enjoy the right to . . . have the Assistance of Counsel for his defense.” However, assistance of counsel does not have to be perfect and free from error. One of the early attempts to determine the scope of Sixth Amendment right to effective assistance of counsel was made in McMann

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10. Fuartado, 170 S.W.3d at 384.
11. See id. at 386.
12. See Justmann, supra note 3, at 704.
13. Id.
14. U.S. Const. amend. VI.
15. Id.
16. McMann v. Richardson, 397 U.S. 759, 774 (1970). The Court stated: It is no denigration of the right to trial to hold that when the defendant waives his state court remedies and admits his guilt, he does so under the law then existing; further, he assumes the risk of ordinary error in either his or his attorney’s assessment of the law and facts. Although he might have pleaded differently had later decided cases then been the law, he is bound by his plea and his conviction unless he can allege and prove serious derelictions on the part of counsel sufficient to show that his plea was not, after all, a knowing and intelligent act.

Id.
v. Richardson, when the United States Supreme Court determined that “the right to counsel is the right to the effective assistance of counsel.” 17 The Court further determined that ineffective assistance of counsel occurs when the counsel’s performance falls below that of a “reasonably competent attorney.” 18

Later, the Supreme Court in Strickland v. Washington elaborated on the meaning and scope of ineffective assistance of counsel under the Sixth Amendment. 19 First, the Court determined that the purpose of the Sixth Amendment right to counsel is to ensure a fair trial. 20 Based on this purpose, the Court further stated that “[t]he benchmark for judging any claim of ineffectiveness must be whether counsel’s conduct so undermined the proper functioning of the adversarial process that the trial cannot be relied on as having produced a just result.” 21

In determining whether a criminal defendant has been deprived of his or her right to effective assistance of counsel, the Court adopted a two-prong test. 22 The defendant must first “show that the counsel’s performance was deficient.” 23 Additionally, “the defendant must show that the deficient performance prejudiced the defense.” 24

Under the first prong, or the “performance” prong, the defendant must show that the defense counsel’s performance “fell below an objective standard of reasonableness.” 25 In determining whether the defense counsel’s advice was reasonable, it must be given “within the range of competence demanded of attorneys in criminal cases.” 26 Furthermore, the reasonableness of counsel’s conduct is to be assessed according to “the facts of the particular case, viewed as of the time of counsel’s conduct.” 27

Under the second prong, or the “prejudice prong,” “[t]he defendant must show that there is a reasonable probability that, but for counsel’s unprofessional errors, the result of the proceeding would have been different.” 28 Therefore, to satisfy the “prejudice prong,” the defendant must show with reasonable probability that the attorney’s error caused him or her to lose the case. 29

17. *Id.* at 771 n. 14.
18. See *id.* at 770-71.
20. *Id.* at 684. “The Sixth Amendment recognizes the right to the assistance of counsel because it envisions counsel’s playing a role that is critical to the ability of the adversarial system to produce just results.” *Id.* at 685.
21. *Id.* at 686.
22. *Id.* at 687.
23. *Id.*
24. *Id.*
26. *Id.* at 687 (quoting *McMann*, 397 U.S. at 770-71).
27. *Id.* at 690.
28. *Id.* at 694.
29. See *id.* at 695.
Applying the standard adopted by Strickland, the Supreme Court in Hill v. Lockhart further determined that the Strickland two-prong test applies to ineffective assistance claims arising out of the plea process. Although the first prong from Strickland applies to these cases, the second prong was slightly modified. When the issue is an attorney’s effectiveness in plea bargaining, the defendant satisfies the prejudice prong by showing that “there is a reasonable probability that, but for counsel’s errors, he would not have pleaded guilty and would have insisted on going to trial.” Therefore, when the defendant pleads guilty, the defendant must show that the counsel’s error is the sole reason the defendant waived the trial and pled guilty.

Kentucky has adopted the standards asserted by the United States Supreme Court in Strickland and Hill. In Sparks v. Commonwealth, the Kentucky Court of Appeals determined that:

A showing that counsel’s assistance was ineffective in enabling a defendant to intelligently weigh his legal alternatives in deciding to plead guilty has two components: (1) that counsel made errors so serious that counsel’s performance fell outside the wide range of professionally competent assistance; and (2) that the deficient performance so seriously affected the outcome of the plea process that, but for the errors of counsel, there is a reasonable probability that the defendant would not have pleaded guilty, but would have insisted on going to trial.

Although Kentucky has adopted this standard for determining ineffective assistance of counsel arising out of plea agreements, it has failed to apply this standard to situations where criminal defense attorneys fail to advise non-citizen defendants of immigration consequences that result from criminal convictions and plea agreements.

B. Kentucky Law and the Failure to Advise Non-Citizen Criminal Defendants on Immigration Consequences of Plea Agreements

Like many other jurisdictions, Kentucky has denied post conviction relief to non-citizen criminal defendants who, without knowledge of the potential immigration consequences, enter guilty pleas and later claim ineffective assistance of counsel. Relying on the “collateral consequences” doctrine,

31. Id. at 58-59.
32. Id. at 59.
33. Id.
35. Id.
36. Id.
37. See Fuartado, 170 S.W.3d at 386.
38. Id. See infra note 219.
Kentucky has determined that criminal defense attorneys do not have a duty to investigate or advise clients of collateral consequences resulting from guilty pleas.40 “A collateral consequence is one that 'remains beyond the control and responsibility of the district court in which that conviction was entered.'”41 Because immigration consequences, such as deportation, are typically viewed to be “collateral” to convictions entered in the trial court, many courts like Kentucky have determined that failure to advise non-citizen clients of immigration consequences will not constitute ineffective assistance of counsel.42

1. Failure to Give Advice on Immigration Consequences

In August 2005, the Kentucky Supreme Court in Commonwealth v. Fuartado addressed for the first time what constituted effective assistance of counsel when representing non-citizen criminal defendants.43 In Fuartado, the Kentucky Supreme Court determined that advising criminal defendants regarding the collateral consequences of a guilty plea is outside the scope of representation required under the Sixth Amendment.44 In Fuartado, the defendant, a native of Jamaica, was charged with a Class C felony of first-degree marijuana trafficking.45 As a result, the defendant entered into a plea agreement which probated his sentence for five years with ninety days to serve on work release.46 The following year, the U.S. Citizen and Immigration Services (USCIS) (formerly known as the INS) formally notified the defendant of its intention to deport him back to Jamaica for his marijuana trafficking conviction.47 Accordingly, the defendant filed a pro se motion for relief to challenge the voluntariness of his guilty plea to the marijuana trafficking.48 The defendant asserted that he involuntarily entered into the guilty plea because neither the trial court nor his defense counsel informed him that deportation would be a consequence of his guilty plea.49

40. Fuartado, 170 S.W.3d at 386.
41. El-Nobani v. United States, 287 F.3d 417, 421 (6th Cir. 2002) (quoting United States v. Gonzalez, 202 F.3d 20, 27 (1st Cir. 2000)). The underlying rationale under the “collateral consequences” doctrine is that “a defendant’s Sixth Amendment right to counsel encompasses criminal prosecutions only, and does not extend to requiring counsel on collateral consequences that may result from such proceedings.” Fuartado, 170 S.W.3d at 386. “A guilty plea that is brought about by a person’s own free will is not less valid because he did not know all possible consequences of the plea and all possible alternative courses of action.” Id. (citing Turner v. Commonwealth, 647 S.W.2d 500, 500-01 (Ky. Ct. App. 1982)).
42. See infra note 219.
43. Fuartado, 170 S.W.3d at 386.
44. Id.
45. Id. at 384-85.
46. Id. at 385.
47. Id.
48. Id.
49. Fuartado, 170 S.W.3d at 385.
The Kentucky Supreme Court determined that advising criminal defendants regarding the collateral consequences of a guilty plea is outside the scope of representation required under the Sixth Amendment. Specifically, the court determined that a defendant’s Sixth Amendment right to counsel “encompasses criminal prosecutions only and does not extend to situations requiring counsel on collateral consequences that may result from such proceedings.” Furthermore, the court stated that a defendant’s right to effective assistance of counsel “encompasses only those activities which tend to protect a criminal defendant’s right to a fair and intelligent determination of guilt or innocence.” Because immigration consequences, such as deportation, are collateral consequences of guilty pleas and are outside the control of the trial court, the court concluded that failure of defense counsel to advise the defendant of potential immigration consequences does not constitute a claim for ineffective assistance of counsel. Thus, the Kentucky Supreme Court determined that criminal defense attorneys have no duty to advise non-citizen criminal defendants of potential immigration consequences that could result from a guilty plea or a plea agreement.

2. Giving Wrong Advice on Immigration Consequences

Following the Fuartado case, the Kentucky Court of Appeals in July of 2006 addressed the issue of whether giving wrong advice regarding immigration consequences constituted ineffective assistance of counsel in Padilla v. Commonwealth. The Kentucky Court of Appeals ultimately determined that giving wrong advice regarding immigration consequences that result from plea agreements could constitute ineffective assistance of counsel. However, the Kentucky Supreme Court granted discretionary review, and thus the decision of Padilla remains pending.

Although the Padilla case is pending on appeal, it is still important for criminal defense attorneys to be aware of the reasoning of the Kentucky Court of Appeals and its potential impact. In Padilla, the defendant was “indicted on charges of possession of marijuana, possession of drug paraphernalia, trafficking in marijuana, and operating a truck without a weight and distance tax number.”

50. Id. at 386.
51. Id.
52. Id.
53. Id.
54. Id.
56. Id. at *9.
58. Id.
The defendant entered into a plea agreement in which he pled guilty to the three drug-related charges. As a result, the vehicular charges were dismissed and he was sentenced to twelve months to be served concurrently for the two drug possession charges and ten years probated for five years for the trafficking charge. However, the defendant filed a pro se motion requesting his sentence be vacated as a result of ineffective assistance of counsel. The defendant asserted that his trial attorney failed to investigate possible immigration consequences involved in his guilty plea. Additionally, the defendant contended that his trial attorney incorrectly advised him that if he pled guilty he “‘did not have to worry about [his] immigration status [because] he had been in the country so long.’”

The Kentucky Court of Appeals determined that if the defendant’s claim was “predicated solely on counsel’s failure to investigate or to advise him of the potential for deportation, Fuartado would require a resolution of his appeal in favor of the Commonwealth.” However, Fuartado did not address situations where the defendant’s counsel gives “erroneous information” concerning immigration consequences after the defendant makes a direct inquiry. Accordingly, the court determined that “affirmative misadvice regarding immigration consequences can in certain circumstances constitute ineffective assistance of counsel.” Because there were relevant issues of fact with respect to the trial attorney’s wrong advice regarding deportation, the court determined that the defendant was entitled to an evidentiary hearing on his motion. Thus, the court vacated and remanded the case back to the lower court. However, the Kentucky Supreme Court granted discretionary review and a decision is still pending at the time of this publication.

C. Immigration Considerations

Any individual who is not a citizen of the United States may be subject to immigration consequences as a result of a criminal conviction, whether it stems from a guilty or no contest plea or a conviction by trial. These consequences typically depend upon the individual’s current immigration status or desired

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60. Id.
61. Id.
62. Id. at *2-3.
63. Id. at *3.
64. Id.
66. Id. at *7.
67. Id.
68. Id. at *9.
69. Id.
70. Padilla, 2006 Ky. LEXIS 214, at *1.
immigration status and the nature of the crime. Unfortunately, criminal attorneys and non-citizens often are unaware of these consequences, which can be much more severe than the actual criminal penalty imposed. As mentioned above, Kentucky does not require criminal defense attorneys to advise non-citizen clients of potential immigration consequences that may result from criminal convictions. However, given the severity of these immigration related consequences, it is important for Kentucky criminal practitioners to effectively and zealously represent non-citizen clients by becoming aware of potential immigration consequences that result from criminal convictions and making non-citizen clients aware of these consequences. Therefore, the following analysis provides a general step-by-step guide to help Kentucky criminal practitioners determine potential immigration consequences that may result from a non-citizen’s criminal conviction.

1. Determining a Client’s Immigration Status

A person’s immigration status plays a large role in determining the possible immigration consequences resulting from a criminal conviction. For example, a person’s immigration status may determine which provisions of immigration law he or she will be subject to and what forms of relief from removal or waivers of inadmissibility may be available. In determining a client’s immigration status, it is important to first ask a client if he or she is a United States citizen. If the client is not a United States citizen, then it is essential to ascertain his or her immigration status by asking some simple questions. For example, ask your client if he or she is:

1. A lawful permanent resident, more commonly known as a green card holder
2. In the United States legally on a temporary visa
3. In the United States illegally for having entered the United States without inspection, having entered the United States with fraudulent documents, or having overstayed his or her temporary visa
4. Anticipating on filing an immigration application in the near future or has any applications currently pending.

72. Id.
73. Francis, supra note 7, at 693.
74. Furatado, 170 S.W.3d at 386.
75. KRAMER, supra note 71, at 1-6, 111-137.
76. Id.
To assist the practitioner, the following is a list of possible classifications of immigration status under U.S. immigration law:

**United States Citizen:** A person is a U.S. citizen by birth in the United States or by birth to U.S. citizen parents, or becomes a U.S. citizen through a legal process called “naturalization.”

**National of the United States:** A national of the United States is a citizen of the United States or a person who is not a citizen of the United States but owes permanent allegiance to the United States.

**Non-Citizen or Alien:** A non-citizen is a person who is not a United States citizen and falls within one of the categories listed below.

- **Lawful Permanent Resident (green card holders):** A lawful permanent resident is a person who is not a U.S. citizen but is permitted to legally live and work in the U.S. permanently and indefinitely. There are a variety of ways by which non-citizens can obtain lawful permanent resident status, including through family based visa petitions and employment based visa petitions.

- **Refugee/Asylee:** A Refugee/Asylee is an individual who has been granted safe haven in the United States, because he or she has established to the United States government that he or she would suffer persecution or has suffered persecution in his or her country of origin.

- **Nonimmigrant Visa Holder:** A nonimmigrant visa holder is an individual who obtained a temporary visa that allowed him or her to legally enter and remain in the United States for a specific period of time and according to certain conditions. This includes, for example, student visas (F-1), tourist visas (B-2), temporary worker visas (such as H-1B, TN, or L-1, and diplomatic visas (G).

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78. INA § 101 (a)(22), 8 U.S.C. § 1101(a)(22) (2000). It is important to note that a national of the United States is a very limited classification. See, e.g., Perdomo-Padilla v. Ashcroft, 333 F.3d 964, 965 (9th Cir. 2003) (rejecting the idea that someone could become a national of the United States merely by being a lawful permanent resident for a long period of time, applying for naturalization, and pledging allegiance to the United States at the naturalization interview).
84. Id.
An Undocumented Person or an Illegal Alien: An undocumented person is an individual who does not have legal status under the immigration laws of the United States. This includes individuals who entered the United States without inspection, which are known as EWIs (Entry Without Inspection), as well as individuals who entered the United States with fraudulent documents.

2. Immigration Consequences Resulting from a Criminal Conviction

After determining an individual’s immigration status, it is important for criminal defense attorneys to ascertain potential immigration consequences that may result from a criminal conviction. It is only at this point that the criminal defense attorney can zealously represent the client and advise him or her as to the most intelligent alternative with respect the pending criminal matter. Depending on the crime that is charged, the facts of the individual case, and the potential immigration consequences involved, the most intelligent alternative could be going to trial or attempting to reach a plea agreement with the prosecutor.

a. Deportation

One of the harshest immigration consequences that can result from a criminal conviction is for a non-citizen to be deported from the United States. The grounds of deportability generally apply to any individual who is not a citizen or national of the United States, and includes those who have been admitted as lawful permanent residents (green card holders). Thus, the term lawful “permanent” resident is a bit of a misnomer, because contrary to popular thinking, lawful permanent resident holders can be subject to removal.

The criminal grounds of deportability are listed in the Immigration and Nationality Act at INA § 237. Although this section provides many grounds for deportation, some pertinent provisions include:

INA §§ 237(a)(2)(A)(i)-(II): convictions for one crime involving moral turpitude that is committed within five years of

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85. See Kurzban, supra note 83, at 78.
88. See generally id.
89. See Francis, supra note 7, at 701.
91. Id.
admission to the United States and for which a sentence of one year or longer may be imposed.93

INA § 237(a)(2)(A)(ii): convictions for two or more crimes involving moral turpitude that do not arise out of a single scheme of criminal conduct regardless of the sentence.94

INA § 237(a)(2)(A)(iii): convictions for aggravated felonies,95 which are defined at § 101(a)(43).96 An aggravated felony is a

94. 8 U.S.C. § 1227(a)(2)(A)(ii). “Moral Turpitude” has no specific definition and is determined by the criminal statute involved and the elements of the crime. See Kramer, supra note 71, at 190. Thus the specific conduct or the facts of the case do not determine what will constitute “moral turpitude.” Id. See, e.g., In re L-V-C-, 22 I. & N. Dec. 594, 603 (B.I.A. 1999) (defining “moral turpitude” as “an act which is per se morally reprehensible and intrinsically wrong or malum in se, so it is the nature of the act itself and not the statutory prohibition of it which renders a crime one of moral turpitude”); In re Tran, 21 I. & N. Dec. 291, 292-93 (B.I.A. 1996) (defining “moral turpitude” as “a nebulous concept, which refers generally to conduct which is inherently base, vile, or depraved, contrary to the accepted rules of morality and the duties owed between persons or to society in general”); In re Danesh 19 I. & N. Dec. 669, 670 (B.I.A. 1988) (defining “moral turpitude” as “conduct that shocks the public conscience as being inherently base, vile, or depraved, contrary to the rules of morality and the duties owed between man and man, either one’s fellow man or society in general”).
96. For specific statutory language, refer to 8 U.S.C. § 1101(a)(43) (2000 & Supp. I 2004). However, aggravated felonies include:
(A) Murder, rape, or sexual abuse of a minor;
(B) Illicit trafficking in a controlled substance;
(C) Illicit trafficking in firearms or destructive devices;
(D) Certain money laundering offenses involving funds in excess of $10,000;
(E) Enumerated federal offenses relating to explosive materials and certain firearms offenses;
(F) A crime of violence, where the term of imprisonment imposed is at least one year;
(G) A theft, burglary, or possession of stolen property offense where the term of imprisonment imposed is at least one year;
(H) Kidnapping offenses;
(I) Child pornography;
(J) Certain racketeering and gambling offenses, where a term of imprisonment of at least one year may be imposed;
(K) Offenses relating to prostitution enterprises, peonage, and slavery offenses;
(L) Federal offenses related to gathering and transmitting classified national defense information, including acts of sabotage and treason under the National Security Act;
(M) A crime involving fraud or deceit where loss to the victim(s) exceeds $10,000; or a crime of tax evasion in which the revenue loss to the Government exceeds $10,000;
(N) Alien smuggling, including harboring, transporting, and concealing;
(O) Re-entry after deportation for an aggravated felony;
(P) Falsely making, forging, counterfeiting, mutilating, or altering a U.S. passport or instrument, for which the punishment imposed is at least one year (does not include first offenses where the person assisted was alien’s spouse, child, or parent);
serious classification, which can result in harsh consequences such as automatic deportation. For example, a non-citizen in a removal proceeding, who has an aggravated felony conviction, is not eligible for bond or any relief from removal regardless of family ties or length of residence in the United States. Furthermore, even state misdemeanors can constitute aggravated felonies for immigration purposes.

INA § 237(a)(2)(B)(i): conviction for violation of any law relating to a controlled substance. This does not apply to single offenses of simple possession of thirty grams or less of marijuana.

INA § 237(a)(2)(C): conviction under any law of purchasing, selling, using, or possessing a firearm or destructive device. This provision also includes attempts to purchase, sell, use, or possess firearms or destructive devices.

INA § 237(a)(2)(D): miscellaneous crimes such as espionage and sabotage.

(Q) Failure to appear for service of sentence where underlying offense is punishable by a term of imprisonment of at least five years;
(R) Offenses relating to commercial bribery, counterfeiting, forgery, or trafficking in vehicles whose VIN numbers have been altered, where the imprisonment imposed is at least one year;
(S) Offenses relating to obstruction of justice, perjury, subornation of perjury, or bribery of a witness, where the term of imprisonment imposed is at least one year;
(T) An offense relating to failure to appear before a court on a felony charge where the term of imprisonment which may be imposed on the underlying charge is two years or more;
(U) An attempt or conspiracy to commit an offense described above.

See KRAMER, supra note 71, at 82-83. But see Lopez v. Gonzalez, 127 S. Ct. 625, 633 (2006) (concluding that conduct made a felony under state law but a misdemeanor under the Controlled Substances Act (CSA) is not an aggravated felony for immigration purposes).


98. See id. See also INA § 236(c)(1)(B), 8 U.S.C. § 1226(c)(1)(B) (2000) (noting that a non-citizen who is deportable for an aggravated felony conviction shall be held in custody while his or her removal hearing is pending).

99. See, e.g., United States v. Simpson, 319 F.3d 81, 85-86 (2d Cir. 2002) (concluding that an offense involving an element of trafficking is an aggravated felony, regardless of whether it would be classified as a misdemeanor under state law).

101. Id.
103. Id.


INA § 237(a)(3)(B): conviction for violation of the alien registration requirements, or for fraud relating to the misuse of visas and other immigration documents.

Additionally, there are other grounds for deportability for criminal conduct even when there is no conviction. These relevant provisions include:


b. Inadmissibility

Another harsh immigration consequence that can result from a criminal conviction is inadmissibility into the United States. The grounds of inadmissibility apply to different groups of non-citizens in various contexts. For example, inadmissibility applies to undocumented non-citizens who entered the United States illegally and have no legal status when the Department of Homeland Security initiates deportation or removal proceedings against them. Inadmissibility also applies to any individual who is not a United States citizen and is seeking physical admission to the United States at a port of entry. This includes lawful permanent residents (greencard holders) and nonimmigrant visa holders who are seeking entry into the United States. The grounds of inadmissibility also apply to non-citizens who are already physically present in the United States, but are seeking to adjust their status in the United States and to become a lawful permanent resident (greencard holder).

113. See INA § 212(a), 8 U.S.C. § 1182(a).
114. Id.
115. Id.
The criminal grounds of inadmissibility are contained in INA § 212(A)(2). Although this list is not exclusive, some pertinent provisions include:

INA § 212(a)(2)(A)(i)(I): A conviction for one crime of moral turpitude. However, there are two exceptions to this provision. The “juvenile exception” involves juvenile offenses that were committed more than five years before the request for admission. The “petty offense exception” occurs where there is a possible sentence of not more than one year and the person did not receive more than a six month sentence.

INA § 212(a)(2)(A)(ii)(II): A conviction for violation of any controlled substance law. However, INA § 212(h) provides a waiver for non-citizens facing inadmissibility based on a criminal conviction for a crime of simple possession of thirty grams or less of marijuana.

INA § 212(a)(2)(B): Two or more convictions for which the aggregate sentences to confinement are five years or more.

INA § 212(a)(2)(C): When a consular or immigration officer has “reason to believe” the individual is a drug trafficker or is or has been a knowing assister, abettor, colluder, or conspirator to a drug trafficker.

Furthermore, criminal convictions may be relevant to the following grounds of inadmissibility:

INA § 212(a)(1)(A)(iii): When the individual is determined to have a physical or mental disorder that may pose or has posed a threat to the safety of the alien or others.

INA § 212(a)(1)(A)(iv): When the individual is determined to be a drug abuser or a drug addict.
INA § 212(a)(2)(D): When the individual is engaged in prostitution or commercialized vice.\textsuperscript{128}

INA § 212(a)(6)(E): When the person is engaged in smuggling aliens into the United States.\textsuperscript{129}

Although a non-citizen criminal defendant may be deportable or inadmissible based on his or her criminal conviction, there may be various forms of relief available to a non-citizen in removal proceedings\textsuperscript{130} as well as waivers of inadmissibility available to non-citizens attempting to enter the United States or adjust their status within the United States.\textsuperscript{131} The availability of relief from removal and waivers of inadmissibility often depends upon such factors as the nature and severity of the crime, the defendant’s immigration status, and a showing of hardship to a qualifying U.S. citizen or lawful permanent resident relative.\textsuperscript{132} The various types of relief from removal and waivers of inadmissibility that may be available to a non-citizen criminal defendant are beyond the scope of this article. However, it is important to note that the granting of relief from removal or waivers of inadmissibility is left in large part to the non-reviewable discretion of the U.S.C.I.S. or an immigration judge.\textsuperscript{133}

Therefore, it is recommended that criminal practitioners not place too much reliance on the availability of relief from removal and waivers of inadmissibility when advising their non-citizen clients regarding pending criminal matters.\textsuperscript{134}

c. Naturalization

A criminal conviction can also prevent a non-citizen from being able to become a citizen of the United States.\textsuperscript{135} Before one can apply for naturalization, the non-citizen must be a lawful permanent resident for the requisite statutory period.\textsuperscript{136} The statutory period is generally five years,\textsuperscript{137} unless the non-citizen is married to a U.S. citizen in which case the statutory period is only three years.\textsuperscript{138} In addition to being a lawful permanent resident for the requisite statutory period, a non-citizen applying for naturalization must demonstrate that he or she is a person of “good moral character” during the requisite statutory period.

\textsuperscript{128} 8 U.S.C. § 1182(a)(2)(D).
\textsuperscript{131} The waivers of inadmissibility are provided in INA § 212 (h); 8 U.S.C. § 1182(h).
\textsuperscript{132} For a more in-depth discussion on waivers of inadmissibility and relief from removal see KURZBAN, supra note 83, at 755-804.
\textsuperscript{134} Id.
immediately preceding the application for naturalization. However, criminal conduct may affect a non-citizen’s ability to establish the necessary “good moral character” for naturalization.

One way an individual may be deemed ineligible for citizenship in United States is if he or she has been convicted of an “aggravated felony.” If a person is deemed to have been convicted of an aggravated felony, a lawful permanent resident is permanently barred from being able to show the requisite “good moral character” for a United States citizenship. The aggravated felony definition is contained in INA § 101(a)(43) and includes twenty-one provisions that encompass hundreds of offenses. For example, the aggravated felony definition lists many offenses such as murder, rape, sexual abuse, and illicit trafficking of controlled substances. In a crime of violence, if a sentence of at least one year is imposed (regardless of suspension), a crime will be classified as an aggravated felony.

Additionally, a person who has two or more convictions for gambling offenses or lives off the proceeds of illegal gambling is precluded from a finding of “good moral character.” Habitual drunkards are also precluded from establishing “good moral character.” Furthermore, any criminal conviction that results in imprisonment for an aggregate of 180 days or more during a specified period will preclude a finding of “good moral character” regardless of the nature of the offense or offenses. Thus, any individual involved in any of these offenses may be prohibited from becoming a United States citizen.

However, it is important to note that the U.S.C.I.S. has broad discretion in determining whether or not an applicant for naturalization has “good moral character.” Additionally, it is important to be aware that the determination of a non-citizen’s moral character is not limited to the five or three year statutory period. Therefore, the court or the U.S.C.I.S. may look beyond the five or

140. See INA § 101(f), 8 U.S.C. §1101(f). The offense must take place during the period that “good moral character” is required. Id.
142. Id.
144. Id. The “aggravated felony” definition applies retroactively to convictions entered prior to the enactment of the 1996 laws. Id.
145. INA § 101(a)(43)(F), 8 U.S.C. § 1101(a)(43)(F) (2000 & Supp. I 2004); see also United States v. Tejeda-Perez, 199 F.3d 981, 983 (8th Cir. 1999) (receiving a sentence of one to fifteen years for second-degree theft constituted an aggravated felony even though the prison sentence was suspended).
three year statutory period when determining whether an applicant has "good moral character." However, looking at prior conduct is only permissible if "the conduct of the applicant during the statutory period does not reflect that there has been reform of character from an earlier period or if the earlier conduct and acts appear relevant to a determination of the applicant's present moral character." Thus, reliance on acts outside of the statutory period should be related to the applicant's current conduct.

Furthermore, if the U.S.C.I.S. is unable to deny an application for naturalization because an applicant’s crime does not result in a statutory bar to establishing good moral character, it can still place the applicant in removal proceedings based upon a criminal conviction, such as a conviction for an aggravated felony. Therefore, the U.S.C.I.S. may then deny the application for naturalization once the removal proceedings have commenced. Accordingly, it is important to be aware that a crime that may not result in a statutory bar to naturalization may still result in the denial of the naturalization application if the crime renders that individual removable.

D. What Constitutes a "Conviction" for Immigration Purposes?

In addition to determining potential immigration consequences, a criminal defense attorney of a non-citizen should consider whether a criminal conviction will constitute a "conviction" for immigration purposes. What may constitute a criminal conviction for immigration purposes may not always constitute a conviction under state law or traditional thinking. The definition of a "conviction" is provided in INA § 101(a)(48)(A) as follows:

The term "conviction" means, with respect to an alien, a formal judgment of guilt of the alien entered by a court or, if adjudication of guilt has been withheld, where (i) a judge or jury has found the alien guilty or the alien has entered a plea of guilty or nolo contendere or has admitted sufficient facts to warrant a finding of guilt, and (ii) the judge has ordered some form of punishment, penalty, or restraint on the alien's liberty to be imposed.

152. Id.
153. 8 C.F.R. § 316.10(a)(2) (2006); see also United States v. Hovsepian, 359 F.3d 1144, 1166-67 (9th Cir. 2004) (en banc) (concluding that an applicant cannot be denied naturalization based solely on prior criminal conduct not within the statutory period).
156. INA § 318, 8 U.S.C. § 1429.
157. Id.
160. Id.
It is important to note that under this definition of “conviction,” a non-citizen does not need to spend any time in jail. Thus, a “conviction” may include a suspended sentence that is conditioned on probation. Because several provisions of the INA, such as the grounds for inadmissibility and deportability are dependent upon the length of a sentence, attorneys representing non-citizen clients should be aware that a suspended sentence will not be honored by immigration law.

1. Expunged Convictions Remain Convictions for Immigration Purposes

As a general rule, a conviction that has been expunged, dismissed, canceled, vacated, discharged, sealed, or removed pursuant to a post-conviction rehabilitative state procedure remains a conviction for immigration purposes. In re Roldan-Santoyo, a first-time offender and citizen of Mexico pled guilty to possession of a controlled substance. Pursuant to Idaho’s rehabilitative statute, the conviction was vacated and the case was dismissed upon termination of the respondent’s probation. Despite the expungement procedure, the Board of Immigration Appeals (BIA) concluded that the respondent’s conviction constituted a final conviction for immigration purposes pursuant to INA § 101(a)(48)(A). Therefore, the respondent was subject to deportation. The BIA determined that it no longer recognized state rehabilitative statutes in determining whether a conviction exists for immigration purposes. However, the BIA limited its decision to circumstances where the non-citizen has been “the beneficiary of a state rehabilitative statute which purports to erase the record of guilt.” Therefore, the BIA concluded that its decision does not apply to situations where a conviction is “vacated by a state court on direct appeal, wherein the court determines that vacation of the conviction is warranted on the merits, or on grounds relating to a violation of a fundamental statutory or constitutional right in the underlying criminal proceedings.”

161. See INA § 101(a)(48)(B), 8 U.S.C. § 1101(a)(48)(B) (2000) which states that: Any reference to a term of imprisonment or a sentence with respect to an offense is deemed to include the period of incarceration or confinement ordered by a court of law regardless of any suspension of the imposition or execution of that imprisonment or sentence in whole or in part.
162. Id.
166. Id. at 513-14.
167. Id. at 514.
168. Id. at 528.
169. Id.
170. Id. at 521.
172. Id.
However, two years later, the Ninth Circuit in *Lujan-Armendariz v. I.N.S.* overruled in part the decision of *In re Roldan-Santoyo*.173 In *Lujan-Armendariz*, the Ninth Circuit concluded that an individual’s first-time simple drug possession offense that is expunged by a state rehabilitative statute cannot be considered a “conviction” if the defendant would have been accorded treatment under the Federal First Offender Act (FFOA) in a federal court proceeding.174 Although the Ninth Circuit has limited the application of *In re Roldan-Santoyo*, the BIA in *In re Salazar-Regino* concluded that it would follow the *Lujan-Armendariz* decision in cases arising in the Ninth Circuit, but would apply *In re Roldan-Santoyo* in all other jurisdictions.175 Thus, the BIA will apply *In re Roldan-Santoyo* to cases arising out of the Sixth Circuit.176

2. Post Conviction Relief and Vacaturs of Judgment

As a general rule, if a conviction is vacated on the merits, it is not a conviction for immigration purposes.177 *In re Rodriguez-Ruiz*, the respondent, who was a native and citizen of Mexico, became a lawful permanent resident of the United States.178 After remaining in the United States for three years, he pled guilty to sexual abuse in the third degree.179 However, his conviction was later vacated pursuant to Article 440 of the New York Criminal Procedure Law.180 The BIA considered whether to terminate the removal proceedings for the respondent because the conviction that the proceeding was based on had been terminated by a New York state court.181 In distinguishing this case from *In re Roldan-Santoyo*, the BIA concluded that the court’s order to vacate the conviction did not constitute a state action that purported to “expunge, dismiss, cancel, vacate, discharge, or otherwise remove a guilty plea.”182 Accordingly, the BIA concluded that vacating the conviction did not constitute a conviction for immigration purposes and thus terminated the removal proceedings against the respondent.183

The motive of the court in vacating a conviction can also play a role in determining whether a criminal conviction will constitute a “conviction” for

173. 222 F.3d 728 (9th Cir. 2000).
174. Id. at 749. The Ninth Circuit’s holding was reaffirmed and clarified in *Chavez-Perez v. Ashcroft*, 386 F.3d 1284 (9th Cir. 2004). *Chavez-Perez* determined that *Lujan-Armendariz* only applies to those individuals who would have been eligible for relief under federal law and have received relief under state law. Id.
176. See, e.g., *Urisky v. Gonzales*, 399 F.3d 728 (6th Cir. 2005).
178. Id. at 1378.
179. Id.
180. Id at 1379.
181. Id.
182. Id.
immigration purposes. In light of *In re Rodriguez-Ruiz*, if a conviction is vacated solely to avoid immigrations hardships, the conviction will not be eliminated for immigration purposes. For example, in *Pickering v. Gonzales*, the petitioner, a native and citizen of Canada, pled guilty to the unlawful possession of Lysergic Acid Diethylamide (LSD) after being indicted in Ontario, Canada in 1980. In 1991, the petitioner entered the United States. In 1996, the petitioner received a pardon for his LSD conviction, which was later quashed in 1997. After his conviction was quashed, the petitioner filed an application for an adjustment of status to become a lawful permanent resident. The application was denied and proceedings were initiated to remove the petitioner from the United States based on his LSD conviction.

The BIA determined that the petitioner was removable because his LSD conviction was quashed solely “to avoid adverse immigration consequences.” The Sixth Circuit concluded that:

> the BIA correctly interpreted the law by holding that, if a court vacates an alien’s conviction for reasons solely related to rehabilitation or to avoid adverse immigration hardships, rather than on the basis of a procedural or substantive defect in the underlying criminal proceedings, the conviction is not eliminated for immigration purposes.

However, the Sixth Circuit concluded that the BIA relied upon an incomplete record to determine that the Canadian court quashed the petitioner’s conviction solely for immigration purposes. Thus, the Sixth Circuit concluded that the record did not provide sufficient evidence for the BIA to determine that the petitioner was deportable. Therefore, the Sixth Circuit reversed and remanded the case to the BIA for an entry to terminate the deportation proceedings. Because *Pickering* was reversed for factual grounds, the legal proposition set forth by the BIA is still good law.

184. *See* *Pickering v. Gonzales*, 454 F.3d 525, 527 (6th Cir. 2006).
185. *Id.*
186. *Id.* at 526.
187. *Id.*
188. *Id.* at 527.
189. *Id.*
190. *Pickering*, 454 F.3d at 527.
191. *Id.* at 528.
192. *Id.* at 527.
193. *Id.* at 528.
194. *Id.* at 532.
195. *Id.*
196. *Pickering*, 454 F.3d at 532.
3. An Adjudication of Juvenile Delinquency Is Not a Conviction for Immigration Purposes

For immigration purposes, an adjudication of juvenile delinquency will not constitute a “conviction.”197 However, not all statutes involving juveniles will protect juveniles from immigration consequences.198 For example, the Sixth Circuit in *Uritsky v. Gonzales* distinguished juvenile delinquency proceedings from youthful offender proceedings.199 According to the Sixth Circuit, juvenile delinquency proceedings do not constitute convictions for immigration purposes, whereas youthful offender proceedings do constitute convictions for immigration purposes.200

In *Uritsky*, a seventeen-year old non-citizen appealed a decision from the BIA subjecting him to removal from the United States.201 The petitioner pled guilty to one count of third degree sexual conduct for having intercourse with a fourteen-year old.202 As a result, the petitioner received a sentence of probation and a designation of “youthful trainee” under Michigan’s Holmes Youthful Trainee Act.203 The Sixth Circuit determined that an alien’s designation and sentencing as a youthful trainee under Michigan’s program was more of a rehabilitative expungement than a finding of juvenile delinquency.204 Because the court determined that proceedings “akin” to expungements are “convictions” for immigration purposes, it concluded that the petitioner’s designation as a “youthful trainee” constituted a conviction within the meaning of INA §101(a)(48)(A).205 Accordingly, the Sixth Circuit affirmed the BIA’s decision ordering the petitioner removed from the United States.206

4. The Effect of Criminal Pardons

There are only limited circumstances in which a criminal pardon will prevent a non-citizen from facing immigration consequences.207 Specifically, INA § 237(a)(2)(A)(v) provides that:

> clauses (i), (ii), (iii), and (iv) shall not apply in the case of an alien with respect to a criminal conviction if the alien subsequent to the criminal conviction has been granted a full and unconditional pardon by

197. See *KRAMER*, *supra* note 71, at 42-43.
198. See, e.g., *Uritsky v. Gonzales*, 399 F.3d 728 (6th Cir. 2005).
199. *Id.* at 735.
200. *Id.*
201. *Id.* at 729.
202. *Id.*
203. *Id.*
204. See, e.g., *Uritsky*, 399 F.3d at 731.
205. *Id.*
206. *Id.* at 735.
First, it is important to be aware that a pardon must be “full and unconditional.” Additionally, it is important to note that INA § 237(a)(2)(A)(v) only applies to the crimes listed in INA §§ 237(a)(2)(A)(i)-(iv), which includes crimes of moral turpitude, aggravated felonies, multiple criminal convictions, and high speed flight from an immigration checkpoint. Noticeably absent are a variety of crimes including convictions for any law relating to a controlled substance.

The BIA in In re Jung Tae Suh determined that a full and unconditional pardon would not waive a non-citizen’s removability unless his crime involved a crime specifically set forth in INA § 237(a)(2)(A)(v). In this case, the respondent had previously received a pardon from the state of Georgia for a conviction of sexual battery. However, because this section is not specifically set forth in INA § 237(a)(2)(A)(v), the BIA concluded that the respondent’s pardon did not waive his removability for a crime of domestic violence or child abuse under INA § 237(a)(2)(E)(i). The court noted that because § 237(a)(2)(A)(v) does not provide a comparable provision that would cover pardons for other convictions such as acts of domestic violence or child abuse, it would not read implicit waivers into the statute. Accordingly, the respondent’s pardon did not waive his removability for his conviction of sexual battery.

208. Id.
214. Id. at 626.
216. See In re Jung Tae Suh, 23 I. & N. Dec. at 627. The BIA also noted other convictions that were not provided for in INA § 237(a)(2)(A)(v). Id. Specifically, the BIA noted that “[o]ther removable offenses, such as controlled substance violations under section 237(a)(2)(B), certain firearm offenses under section 237(a)(2)(C), and violations of protection orders under section 237(a)(2)(E)(ii), are similarly not covered by the pardon waiver of section 237(a)(2)(A)(v) of the Act.” Id.
217. Id. at 628.
III. PROPOSAL FOR KENTUCKY

A. Zealously Representing Your Client and a Duty to Make Non-Citizen Criminal Defendant’s Aware of Immigration Consequences

In determining what will constitute effective assistance of counsel of non-citizen criminal defendants, courts have adopted various standards. A view held by many states, including Kentucky,\(^\text{218}\) is that attorneys do not have a duty to investigate or advise non-citizen clients of immigration consequences that could result from a criminal conviction.\(^\text{219}\) Some states take this approach while adding the requirement that the attorneys must not misinform clients of immigration consequences.\(^\text{220}\) Even though attorneys still have no duty to inform non-citizen clients of immigration consequences under this approach, attorneys cannot give wrong advice regarding immigration consequences.\(^\text{221}\) Additionally, other courts have adopted the standard in which attorneys must investigate and advise non-citizen clients of potential immigration consequences resulting from a criminal conviction.\(^\text{222}\) Furthermore, other jurisdictions take the approach that

\(^\text{218. Fuartado, 170 S.W.3d at 386.}\)


\(^\text{220. See, e.g., Downs-Morgan v. United States, 765 F.2d 1534, 1541 (11th Cir. 1985) (determining that an attorney’s misrepresentation of the risk of deportation could constitute ineffective assistance of counsel); People v. Correa, 485 N.E.2d 307, 312 (Ill. 1985) (advising a non-citizen that a guilty plea would not have immigration consequences without conducting appropriate research was ineffective assistance of counsel); Morales v. State, 910 S.W.2d 642, 646-647 (Tex. Ct. App. 1995) (concluding that counsel’s erroneous advice about defendant’s possible sentence without informing the defendant of the deportation consequences resulting from guilty plea did constitute ineffective assistance of counsel).


\(^\text{222. See, e.g., People v. Soriano, 240 Cal. Rptr. 328, 335-36 (Cal. Ct. App. 1987) (determining that attorneys have a duty to investigate immigration consequences that could result from the criminal case once the attorney is aware of the alienage of the client); People v. Pozo, 746 P.2d 523, 529 (Colo. 1987) (concluding that the obligation to advise non-citizen defendants of immigration consequences is conditioned upon the attorney’s knowledge that the client is a non-citizen or whether there was sufficient information to reasonably believe the defendant was a non-citizen); Lyons v. Pearce, 694 P.2d 969, 974-77 (Or. 1985) (determining that although the court does not have to advise non-citizen defendants of immigration consequences, defense counsel does...}
the trial court must advise non-citizen defendants of possible immigration consequences before entering a plea. 223

Because Kentucky does not require either attorneys or trial court judges to advise non-citizens of potential immigration consequences that could result from a criminal conviction, 224 non-citizen defendants do not know or fully understand the possible immigration consequences they may face when determining the most intelligent alternative in their pending criminal matter. As previously stated, these immigration consequences, such as deportation, inadmissibility, and ineligibility for naturalization, are often times much more severe than any criminal penalty the non-citizen may face. 225 Therefore, to protect its non-citizen residents, many of whom are in the United States legally, it is necessary for Kentucky to adopt a new standard that will help non-citizen defendants understand the potential immigration consequences that could result from a criminal conviction.

At the very minimum, the Kentucky Supreme Court should affirm the Kentucky Court of Appeals’ decision in Padilla. 226 In Padilla, the court concluded that giving wrong advice regarding deportation could constitute ineffective assistance of counsel. 227 However, the Kentucky Supreme Court granted certiorari and the case is pending on appeal. 228

Affirming the Kentucky Court of Appeals’ decision in Padilla would provide minimal protection for non-citizen criminal defendants. 229 However, as Padilla only places a duty on a criminal attorney to not misinform a client regarding potential immigration consequences, 230 the likely result may be that criminal attorneys will remain silent regarding potential immigration

have a duty to do so); see also, Minn. Rule Crim. Pro. 15.01 (2001) (requiring a defense attorney to first advise the defendant of potential immigration consequences and then requiring the court to determine whether the attorney has informed the defendant of the immigration consequences).

223. See CAL. PENAL CODE § 1016.5 (West 1985); CONN. GEN. STAT. ANN. § 54-1 (West 2001); D.C. CODE ANN. § 16-713 (2005); FLA. R. CRIM. P. 3.172(c)(8); GA. CODE ANN. § 17-7-93(G) (Michie 2004); HAW. REV. STAT. ANN. § 802E-2 (Michie 1993); ME. R. CRIM. P. 11(b), (h); MD. RULE 4-2429; MONT. CODE ANN. § 46-12-210 (2005); N.C. GEN. STAT. § 15A-1022 (2003); OHIO REV. CODE ANN. § 2943.031 (West 2006); OR. REV. STAT. § 135.385 (2005); R.I. GEN. LAWS § 12-12-22 (2002); WASH. REV. CODE ANN. § 10.40.200 (West 2002); WIS. STAT. ANN. § 971.08 (West 1998).

224. Fuertado, 170 S.W.3d at 386.

225. See, e.g., Fong Haw Tan v. Phelan, 333 U.S. 6, 10 (1948) (“[D]eportation is a drastic measure and at times the equivalent of banishment of exile. It is the forfeiture for misconduct of a residence in this country. Such a forfeiture is a penalty.”) (citation omitted); Bridges v. Wixon, 326 U.S. 135, 164 (1945) (Murphy, J., concurring) (“The impact of deportation upon the life of an alien is often as great if not greater than the imposition of a criminal sentence. A deported alien may lose his family, his friends and his livelihood forever, Return to his native land may result in poverty, persecution and even death”). See supra Part II.C.i-ii, Part II.D.i-v.


227. Id. at *4.


229. See generally Padilla, 2006 Ky. App. LEXIS 98, at *2. 230. Id.
consequences when representing a non-citizen client. In short, the criminal attorney has no incentive under Padilla to investigate and advise their client as to potential immigration consequences, while the criminal attorney would clearly stand something to lose by attempting to advise the client regarding potential immigration consequences. Moreover, Padilla places the burden on the non-citizen defendant to first inquire about potential immigration consequences. Thus, this approach requires the lay defendant to spot and inquire about complex legal issues. Furthermore, “[r]equiring a class of defendants, who may have the least amount of familiarity of all defendants with the American legal system, to identify legal issues on behalf of the professional on whom they are relying to do just that is an obfuscation of professional duty.” Therefore, non-citizen criminal defendants are not adequately being represented under this approach.

Because the Kentucky Supreme Court has already determined that attorneys have no duty to inform non-citizen clients about potential immigration consequences that could result from a criminal conviction, a more appropriate approach might be for the Kentucky legislature to enact legislation similar to that of Ohio. Under section 2943.031 of the Ohio Revised Code, a trial court must provide a specific advisement to non-citizen criminal defendants regarding possible immigration consequences prior to accepting a guilty plea or a no contest plea. If the record does not reflect a warning, a conviction may be set aside and the guilty or no contest plea may be withdrawn. Furthermore, if the

231. See Francis, supra note 7, at 726.
232. Id.
233. Id.
234. Id.
235. Id.
236. Id.
237. Fuertado, 170 S.W.3d at 386.
238. See OHIO REV. CODE ANN. § 2943.031 (West 1997). Other jurisdictions have taken this approach as well. See supra note 223.
239. OHIO REV. CODE ANN. § 2943.031(A). The court is required to give the following advisement:
   If you are not a citizen of the United States, you are hereby advised that conviction of the offense to which you are pleading guilty (or no contest, when applicable) may have the consequences of deportation, exclusion from admission to the United States, or denial of naturalization pursuant to the laws of the United States.
   Id.
240. OHIO REV. CODE ANN. § 2943.031(D). This applies only to pleas entered after the enactment of the statute (Oct. 2, 1989). Id. In interpreting section 2942.031(A) of the Ohio Revised Code, the court in Ohio v. Francis stated the following:
   [i]f some warning of immigration-related consequences was given at the time a noncitizen defendant’s plea was accepted, but the warning was not a verbatim recital of the language in R.C. 2942.031(A), a trial court considering the defendant’s motion to withdraw the plea under R.C. 2943.031(D) must exercise its discretion in determining whether the trial court that accepted the plea substantially complied with R.C. 2943.031(A).
defendant requests additional time to consider his or her plea after the court’s advisement is given, the court shall allow the defendant to have additional time.241

Adopting an approach similar to the advisement provided in section 2943.031 of the Ohio Revised Code would help to inform non-citizen criminal defendants that adverse immigration consequences may result from entering pleas.242 Furthermore, if requested, it would give non-citizen criminal defendants an opportunity to receive more time to determine what immigration consequences may result from entering a plea after becoming aware that there might be potential immigration consequences.243 Additionally, adopting this approach would allow a non-citizen defendant to have the opportunity to set aside his conviction and withdraw his plea if the defendant enters a plea without receiving the advisement by the court.244

While enacting new legislation that requires trial court judges to give an immigration-related advisement prior to accepting a guilty or no contest plea is a step towards preventing harsh immigration results, attorneys should still be held to a higher standard.245 A better standard of representation for criminal defense attorneys would be to place an affirmative duty on attorneys to investigate and advise non-citizen criminal defendants of potential immigration consequences resulting from criminal convictions.246 Although immigration consequences are collateral to entering a guilty plea,247 the consequences are often times much more severe than the criminal penalties, which cannot be said for other collateral consequences a criminal defendant may face.248 Therefore, failing to provide non-citizen defendants with the opportunity to discover the possible immigration consequences of his or plea until it is too late is a harsh and unfair result.

820 N.E.2d 355, 364 (Ohio 2004). See also In re Adamiak, 23 I. & N. Dec. 878, 881 (B.I.A. 2006) (concluding that a conviction vacated under section 2943.031 of the Ohio Revised Code for the trial court’s failure to advise a non-citizen defendant of the possible immigration consequences of a guilty plea is no longer a valid conviction for immigration purposes). However, note that the court in In re Adamiak distinguished its case from Pickering v. Gonzales, 454 F.3d 525, 527 (6th Cir. 2006). Id. at 879. The court in Pickering concluded that “if a court vacates an alien’s conviction for reasons solely related to rehabilitation or to avoid adverse immigration hardships, rather than on the basis of a procedural or substantive defect in the underlying criminal proceedings, the conviction is not eliminated for immigration purposes.” 454 F.3d at 527. Although In re Adamiak involved immigration consequences, the conviction was vacated due to the court’s procedural defect for failure to advise the defendant of possible immigration consequences of his guilty plea.

241. OHIO REV. CODE ANN. § 2943.031(A).
242. See id.
243. See id.
244. See id.
245. See Francis supra note 7, at 728.
246. Id.
247. See Fuartado, 170 S.W.3d at 386.
248. See supra note 6.
Therefore, Kentucky should reconsider its decision in *Fuartado*\(^{249}\) and require defense attorneys to first determine the immigration status of all clients, and then require attorneys to advise non-citizen criminal defendants of potential immigration consequences.\(^{250}\) At the very least, if the defense attorney is unaware of what immigration consequences might result from a criminal conviction, he or she should have a duty to either consult an immigration attorney or refer the client to an immigration attorney who can properly advise the client.\(^{251}\) Accordingly, Kentucky should adopt a new standard that would ensure that non-citizen criminal defendants are properly being advised.

**IV. CONCLUSION**

While Kentucky does not require attorneys to advise non-citizen criminal defendants of potential immigration consequences that may result from a criminal conviction,\(^ {252}\) the above analysis provides a step-by-step process to help Kentucky criminal practitioners to effectively and zealously represent non-citizen criminal defendants.\(^ {253}\) As evidenced by the cases and the interpretation of the INA in this survey, non-citizen defendants may face harsh results if they are not properly advised of potential immigration consequences that could result from criminal convictions.\(^ {254}\) Accordingly, to effectively and zealously represent non-citizen criminal defendants, attorneys should not only determine the immigration consequences that could result from a criminal conviction, but attorneys should also advise their clients of potential immigration consequences.

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249. *Fuartado*, 170 S.W.3d at 386.
250. See Francis *supra* note 7, at 727.
251. *Id*.
252. See Fuartado, 170 S.W.3d at 386.
253. See supra Part II.C.i-ii, Part II.D.i-iv.
254. *Id*. 
ERISA PREEMPTION: A SURVEY OF THE KENTUCKY COURTS’ INTERPRETATION OF THE SIXTH CIRCUIT’S PREEMPTION ANALYSIS

by John R. Kirk+ and Marguerite J. Slagle∗

I. INTRODUCTION

The Employee Retirement Income Security Act (“ERISA”)1 was passed in 1974 for the purpose of promoting “the interests of participants in employee benefit plans and their beneficiaries.”2 In an attempt to bring a level playing field to the employee benefits area, Congress included a preemption provision in ERISA to usurp the numerous state and federal laws that had existed prior to ERISA.3 In general, ERISA § 514(a) preempts all state laws that “relate to any employee benefit plan,” with certain enumerated exceptions.4 Important exceptions include state insurance, banking, securities laws, some criminal laws, and domestic relations orders that meet ERISA’s specific qualification requirements.5 Determining the meaning of the vague “relate to” language is often the linchpin of ERISA litigation.6

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2. Id. at § 1001(b) stating
   It is hereby declared to be the policy of this chapter to protect interstate commerce and the interests of participants in employee benefit plans and their beneficiaries, by requiring the disclosure and reporting to participants and beneficiaries of financial and other information with respect thereto, by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing for appropriate remedies, sanctions, and ready access to the Federal courts.
4. Id. (stating that the statute “shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan described in section 1003(a) of this title and not exempt under section 1003(b)”).
Since 1981, the Supreme Court has decided over twenty cases dealing with ERISA preemption. A key issue in many of these cases is the meaning of the phrase “relate to.” In the cases since 1981, the Court has found or rejected ERISA preemption in many varied contexts with varying rationales. Due to this, practitioners can not be blamed for not immediately seizing upon the change in precedent.

The District Court for the Western District of Kentucky in *McMurtry v. Wiseman*, summed up the varied history of ERISA when it stated:

> The issue of ERISA preemption is a complicated and complex matter. Numerous courts have considered the issue, including the United States Supreme Court on numerous occasions…. ERISA has not changed, but decisions interpreting preemption have evolved, so to speak. Certainly in the early years of ERISA, preemption was almost automatic. Nevertheless, even in the early 1990’s courts were recognizing that certain state law tort claims were not preempted. As courts have examined the duty alleged to have been breached and the overall purpose of ERISA, more state law claims have been found not to be preempted.

Many would argue that preemption case law has not changed course from the very expansive interpretations of *Shaw v. Delta Airlines, Inc.*, and *Ingersoll-Rand Co. v. McClendon*. However, this article suggests there has been a significant change in the Sixth Circuit’s approach to ERISA preemption with its decision in *Penny/Ohlmann/Nieman, Inc. v. Miami Valley Pension Corp* (“PONI”).

As will be discussed in this article, the Federal District Courts of Kentucky have had their own trouble interpreting the various rulings from the Sixth Circuit and the Supreme Court. It appears that courts sitting in Kentucky have adopted a narrower approach to preemption similar to the approach the Sixth Circuit promulgated in *PONI* and its progeny, but it still may be too soon to tell.

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8.  *See id.*
9.  *Id.*
13.  399 F.3d 692, 697 (6th Cir. 2005) (“More recently, however, the Supreme Court has narrowed the preemptive scope of ERISA, moving away from the broadest meaning of the provision.”).
14.  *See Pentech Infusions, Inc. v. Anthem Health Plans of Kentucky, Inc.*, 387 F. Supp. 2d 712, 714 (W.D. Ky. 2005) (stating that “many cases from other circuits and even within the sixth circuit present a confusing picture of ERISA jurisdiction”).
II. HISTORY OF ERISA PREEMPTION IN THE COURTS

A. Conflict Preemption

When a state law conflicts with ERISA, the state law is preempted by ERISA.\(^\text{15}\) Conflict preemption arises where compliance with both federal and state law is physically impossible or where “[state] law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.”\(^\text{16}\) The purpose of ERISA was “to eliminate the multiplicity of regulation that hampered the efficient administration of benefit plans and replace it with a uniform administrative scheme and standard procedures for claims processing and benefit disbursement.”\(^\text{17}\) For that reason, section 514(a) states that ERISA “supersede[s] any and all State laws insofar as they may now or hereafter relate to any employee benefit plan.”\(^\text{18}\) All claims that “relate to” an employee benefit plan are conflict preempted, unless it falls within an exception of section 514.\(^\text{19}\)

Generally, when considering the removal of a case from state court, courts rely on the “well-pleaded complaint rule,” which provides that a federal court has jurisdiction if the plaintiff’s complaint establishes that the cause of action arises under federal law.\(^\text{20}\) This allows the court to look beyond the titles and language used in the complaint to describe the cause of action to see if, in truth,
the action is one under ERISA. Federal courts do not have jurisdiction, even if federal preemption is raised as a defense, if a party’s complaint presents only a state law cause of action that does not “relate to” ERISA.

B. Complete Preemption

If a claim could be brought under ERISA § 502(a), then the state law action is completely preempted. As the Sixth Circuit stated in Cromwell v. Equicor-Equitable HCA Corporation, “[i]t is not the label placed on a state law claim that determines whether it is preempted, but whether in essence such a claim is for the recovery of an ERISA plan benefit.” Complete preemption is an exception to the well-pleaded complaint rule. Under the doctrine of complete preemption, Congress may preempt an area of the law so completely that any complaint raising claims in that area is federal in character, and therefore necessarily presents a basis for federal court jurisdiction. Essentially, the only area of law that remains is federal, as “any claim purportedly based on that pre-empted state law is considered, from its inception, a federal claim, and therefore arises under federal law.”

The Supreme Court’s earliest decisions recognized ERISA’s broad preemptive scope because, “[t]he breadth of § 514(a)’s pre-emptive reach is apparent from that section’s language. A law ‘relates to’ an employee benefit plan, in the normal sense of the phrase, if it has a connection with or reference to such a plan.” Under this broad common-sense meaning, a state law may “relate to” a benefit plan, and is thereby pre-empted, even if the law is not specifically designed to affect such plans, or the effect is only indirect. Although the Supreme Court acknowledged that “[s]ome state actions may affect employee benefit plans in too tenuous, remote, or peripheral a manner to warrant

21. See generally Franchise Tax Bd. of State of Cal., 514 U.S. at 9-11. See also Warner v. Ford Motor Co., 46 F.3d 531, 533-534 (6th Cir. 1995) (explaining that the plaintiff’s complaint pleaded a state age discrimination claim against the employer and was therefore not an action to recover benefits under the early retirement plan which would be governed by ERISA).
22. See Caterpillar Inc., 482 U.S. at 392-93.
24. See, e.g., Ingersoll-Rand Co. v. McClendon., 498 U.S. 133, 144 (1990) (explaining that Congress intended § 502(a) to be the sole and exclusive remedy for ERISA rights; see also Massachusetts Mut. Life Ins. Co. v. Russell, 473 U.S. 134, 146 (noting that the six enforcement provisions found in § 502(a) of the statute “provide strong evidence that Congress did not intend to authorize other remedies”).
25. 944 F.2d 1272, 1276 (6th Cir. 1991).
27. See Caterpillar Inc., 482 U.S. at 393 (citing Metropolitan Life Ins. Co., 481 U.S. at 65 (holding that Congress intended ERISA § 502(a) to be the sole and exclusive remedy for ERISA rights; see also Metropolitan Life Ins. Co. v. Taylor, 481 U.S. 58, 63-64 (1987).
28. Id. (citing Franchise Tax Bd. of State of Cal., 463 U.S. at 24).
29. Shaw, 463 U.S. at 96-97.
a finding that the law ‘relates to’ the plan,” 31 it continued to broadly interpret ERISA’s preemptive purpose.32

However, in New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co., the Supreme Court attempted to define this line when it acknowledged that, the term “relate to” could not be read to “extend to the furthest stretch of its indeterminacy, then for all practical purposes pre-emption would never run its course, for ‘[r]eally, universally, relations stop nowhere.’” 33 The court further stated that:

[In]for the same reasons that infinite relations cannot be the measure of pre-emption, neither can infinite connections. We simply must go beyond the unhelpful text and the frustrating difficulty of defining its key term, and look instead to the objectives of the ERISA statute as a guide to the scope of the state law that Congress understood would survive.34

This shift prompted many circuit courts to take a different view on ERISA preemption.

C. Courts’ Views on ERISA Preemption

Since the Travelers decision in 1995, several other Federal Circuit Courts have attempted to interpret the various Supreme Court rulings. For instance, the Second Circuit has stated:

Our preemption analysis in Diduck, however, is no longer consistent with prevailing Supreme Court precedent. Indeed, several of our sister circuits have noted that Travelers occasioned a significant change in preemption analysis, and required careful reconsideration of any preexisting precedent dependent on the expansive view of “related to” that held sway before it.35

The Third Circuit also recently fell in line when it stated:

By the mid-1990s, however, it had become clear that the “relates to” standard was one without conceptual limits, and given the Court’s general “assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress,” it balked at the specter of a preemptive vortex that could swallow virtually any state remedial law.36

31. Shaw, 463 U.S. at 100 n.21 (citing American Telephone and Telegraph Co. v. Merry, 592 F.2d 118, 121 (2d Cir. 1979)).
32. See generally, Pilot Life Ins. Co., 481 U.S. at 47.
33. Travelers, 514 U.S. at 655.
34. Id. at 656.
Relying on *Travelers*, the Seventh Circuit stated, “[t]hus, while the Trustees’ claim obviously ‘relates to’ the Plan at some level, the Supreme Court has made it clear that federal courts are to go ‘beyond the unhelpful text’ of § 1144(a) and evaluate preemption challenges in light of ERISA’s overall ‘objectives.’” 37 Likewise, the Ninth Circuit recognized the change brought by *Travelers* when it noted that “[w]hile this section suggests that the phrase ‘relate to’ should be read broadly, the Supreme Court has recently admonished that the term is to be read practically, with an eye toward the action’s actual relationship to the subject plan.” 38

III. THE SIXTH CIRCUIT’S *PONI* DECISION

In 2005, the Sixth Circuit again had to interpret the various Supreme Court decisions on ERISA preemption. 39 In *PONI*, the employer (PONI) had two retirement plans for its employees, each managed by a different company. 40 Unbeknownst to the employer, the plans violated the IRS top-heavy rules for seven years, and the employer was heavily fined. 41 The employer alleged both managing firms breached their respective service contracts. 42 The lower court held that PONI’s contract claims were preempted by ERISA, and the employer appealed. 43

The Sixth Circuit reviewed the prior decisions of the Supreme Court, and its own ERISA precedent, 44 before deciding on its course of action. 45 The Court recognized:

In its earlier cases, the Supreme Court noted that “[t]he pre-emption clause is conspicuous for its breadth,” and “deliberately expansive, and designed to establish pension plan regulation as exclusively a federal concern.” More recently, however, the Supreme Court has narrowed the preemptive scope of ERISA, moving away from the broadest meaning

40. *Id.* at 695.
41. *Id.* at 695-96 (stating that a “plan is considered top-heavy when too great a percentage of the assets are dedicated to key employees, defined as officers earning above a specified compensation level or employees with high salaries and sufficient ownership interests”).
42. *Id.* at 696.
43. *Id.* at 696-97.
44. *Id.* at 702. See, e.g., Wright v. Gen. Motors Corp., 262 F.3d 610, 615 (6th Cir. 2001) (holding that reference to plan benefits may be “simply a reference to specific, ascertainable damages [the plaintiff] claims to have suffered as a proximate result of [the defendant’s conduct]”); see Smith v. Provident Bank, 170 F.3d 609, 615-17 (6th Cir. 1999) (holding that a common law breach of fiduciary duty was preempted by ERISA because Congress established the exclusive means by which fiduciary duties would be enforced. The court noted that where “an ERISA plan’s relationship with another entity is not governed by ERISA, it is subject to state law”).
45. *Penny/Ohlmann/Nieman Inc.*, 399 F.3d at 697-702.
of the provision. The Court has stated that the phrase “insofar as they . . . relate” contains words of limitation that were purposefully written into the statute. If the term “relate to” was allowed to reach to its most logical extension, “pre-emption would never run its course.” The effect of such a broad reading “would be to read Congress’s words of limitation as mere sham, and to read the presumption against pre-emption out of the law whenever Congress speaks to the matter with generality.”

Based on its review of these prior decisions, the Sixth Circuit adopted the more constricted and analytical approach to applying preemption principles promulgated by the Supreme Court, and concluded that “[t]herefore, in interpreting ERISA’s preemption clause, a court ‘must go beyond the unhelpful text and the frustrating difficulty of defining its key term, and look instead to the objectives of the ERISA statute as a guide to the scope of the state law that Congress understood would survive.’”

Prior to PONI, the Sixth Circuit previously recognized “that the Supreme Court does not require that state laws have absolutely zero effect on ERISA plans” to avoid preemption and rejected a “per se rule for pre-emption based on mere reference” to an ERISA plan. However, the court in PONI first adopted a comprehensive methodology for distinguishing preempted and non-preempted claims based on ERISA’s objectives. Persuaded by the Fourth Circuit’s approach, the PONI court concluded that:

ERISA preempts state laws that (1) “mandate employee benefit structures or their administration;” (2) provide “alternate enforcement mechanisms;” or (3) “bind employers or plan administrators to particular choices or preclude uniform administrative practice, thereby functioning as a regulation of an ERISA plan itself.” Congress did not intend, however, for ERISA “to preempt traditional state-based laws of general applicability that do not implicate the relations among the traditional ERISA plan entities, including the principals, the employer, the plan, the plan fiduciaries, and the beneficiaries.” Since the Travelers decision, the Supreme Court has reiterated the approach of looking to the objectives of ERISA to guide its preemption decisions.

46. Id. at 697. (internal citations omitted). See also California Div. of Labor Standards Enforcement v. Dillingham Constr., N.A., Inc., 519 U.S. 316, 335 (1997) (Scalia, J., concurring) (noting that “applying the ‘relate to’ provision according to its terms was a project doomed to failure, since, as many a curbstone philosopher has observed, everything is related to everything else”).

47. Penny/Ohlmann/Nieman Inc., 399 F.3d at 698 (citing Travelers, 514 U.S. at 656).


49. Id. at 760. The court rejected preemption on the grounds that “the SBT [Michigan’s Single Business Tax] has only a peripheral effect on an ERISA plan.” Id. at 755.

50. See Penny/Ohlmann/Nieman Inc., 399 F.3d at 698.

51. Id (internal citations omitted).
The court held that ERISA preempted the state-law claims against the fiduciary service provider because its trustee and record keeping duties arose from the terms of the ERISA plan.\(^{52}\) The contract at issue was the ERISA plan itself, so the claim was preempted.\(^{53}\) However, the claim against the non-fiduciary provider was not preempted, because the contract to provide record-keeping duties was separate and distinct from the ERISA plan.\(^{54}\) Further, the provider was not a traditional ERISA entity because it was not a fiduciary and merely provided record-keeping services.\(^{55}\)

This significant change in ERISA preemption analysis was noted in Toledo Blade Newspaper Unions-Blade Pension Plan v. Investment Performance Services, LLC\(^ {56}\) when it stated that:

> The Sixth Circuit has recently noted the Supreme Court’s narrowing of ERISA’s preemptive scope, which the Supreme Court had previously described as “conspicuous for its breadth” and “deliberately expansive.” As the Sixth Circuit has explained, the Supreme Court now instructs that the words “relate to” must not be taken to their “most logical extension,” or else “pre-emption would never run its course,” because, as Justice Scalia has noted, “‘everything is related to everything else.’”\(^ {57}\)

This tighter construction of ERISA preemption in PONI contrasted sharply with the Sixth Circuit’s fairly recent observation in Marks v. Newcourt Credit Group, Inc.\(^ {58}\) In Marks, the plaintiff alleged his employer breached his employment contract by terminating him and denying him severance benefits including monies under the ERISA plan.\(^ {59}\) Marks sought the amount of funds he was entitled to under the ERISA plan, but not the ERISA funds themselves as damages.\(^ {60}\) The lower court held that Marks’ claim was preempted, and Marks appealed.\(^ {61}\)

The Sixth Circuit noted that, “[i]n keeping with the Supreme Court’s recognition of the broad scope of ERISA preemption, the Sixth Circuit ‘has repeatedly recognized that virtually all state law claims relating to an employee benefit plan are preempted by ERISA.’”\(^ {62}\) The court then acknowledged that state law claims are not preempted when the “effect on employee benefits plans

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52. Id. at 700.
53. Id at 699.
54. Id. at 700.
55. Id.
56. 373 F. Supp. 2d 735 (N.D. Ohio 2005).
57. Id. at 744 (citations omitted).
58. 342 F.3d 444 (6th Cir. 2003).
59. Id. at 448-49.
60. Id. at 453.
61. Id. at 448-49.
62. Id. at 452 (citing Cromwell v. Equicor-Equitable HCA Corp., 944 F.2d 1272, 1276 (6th Cir. 1991)).
is merely tenuous, remote or peripheral." The court determined that Marks merely referenced the plan to determine the amount of damages caused by the breach of his employment contract. The alleged breach was irrespective of the plan, and therefore was not preempted.

Although the earlier Marks opinion referenced a broader scope of preemption, the Sixth Circuit arrived at a holding consistent with the PONI opinion when it held that “[b]ecause this conduct may constitute a breach of Marks’s employment contract irrespective of the plan, the breach of contract claim is not preempted.” The Sixth Circuit reiterated in PONI that “[t]he mere fact that an employee benefit plan is implicated in the dispute, however, is not dispositive of whether the breach-of-contract claims are preempted.” In PONI, the existence of a contract separate from the ERISA plan did not trigger preemption against the non-fiduciary defendant. However, the obligations of the fiduciary defendants arose “from the plan itself, and thus the breach-of-contract claim is necessarily a claim that a fiduciary breached the terms of the ERISA plan.” Despite the broader preemption scope discussed in Marks, the Sixth Circuit made it clear in PONI that it adopted a narrower approach to preemption.

The Sixth Circuit threw another curve into the analysis for preemption shortly after its PONI decision in Briscoe v. Fine. Relying on Aetna Health Inc. v. Davila, a more recent Supreme Court decision which reaffirmed that ERISA preempts state laws that provide an alternative remedy to an ERISA cause of action, the Sixth Circuit noted that although PONI did not cite Davila, “[o]ther circuits . . . have read the expansive language in Davila as holding that ‘when a state law claim may fairly be viewed as an alternative means of recovering benefits allegedly due under ERISA, there will be preemption.’” In Briscoe, the Court reviewed whether a former employee’s claim that the corporate employer’s former officers and directors and third-party plan administrator breached their duty to employees “by failing to disclose the overall

63.  Id.
64.  Id. at 453.
65.  Id.
66.  The Marks opinion was issued on September 4, 2003, and the PONI opinion was issued on March 4, 2005. 342 F.3d at 444; 399 F.3d at 692. Both addressed breach of contract claims.  Id.
67.  See Penny/Ohlmann/Nieman Inc., 399 F.3d at 697-99.
68.  Marks, 342 F.3d at 453.
69.  Penny/Ohlmann/Nieman Inc., 399 F.3d at 699.
70.  Id. at 697.
71.  Id at 699.
72.  See Marks, 342 F.3d at 453.
73.  Penny/Ohlmann/Nieman Inc., 399 F.3d at 698.
74.  444 F.3d 478 (6th Cir. 2006).
76.  Briscoe, 444 F.3d at 498.
financial condition” of corporation was preempted. The court held that the claims were not preempted by ERISA because the employees could have alleged such breach of duty even if the corporation had never sponsored an ERISA covered plan. In reviewing whether the defendants breached their fiduciary duty in not disclosing the financial condition of the ERISA plan, the court again found no preemption. Once more, the Sixth Circuit showed its willingness to adopt a more restrictive approach.

IV. PREEMPTION IN KENTUCKY AFTER PONI

The Kentucky courts appear to analyze ERISA preemption under PONI’s narrower approach. For example, a district court case from the Western District of Kentucky, is instructive. In Forbes, the court examined the plaintiff’s claims for monetary damages resulting from numerous alleged breaches of ERISA’s fiduciary provisions. The court, ruling soon after the PONI decision, stated that “[t]he Sixth Circuit Court of Appeals has recently given some guidance on whether a cause of action relates to an employee benefit plan.” Quoting PONI, the court further stated that “Congress did not intend, however, for ERISA ‘to preempt traditional state-based laws of general applicability that do not implicate the relations among the traditional ERISA plan entities, including the principals, the employer, the plan, the plan fiduciaries, and the beneficiaries.” The court found that the plaintiff’s allegations did “implicate the relationship among traditional plan entities” and therefore all of her claims were preempted by ERISA.

Paysource, Inc. v. Triple Crown Financial Group, an Eastern District of Kentucky decision is also instructive. In Paysource, the plaintiff’s complaint asserted state law claims for “(1) breach of contract, (2) breach of fiduciary duty, (3) conversion, (4) fraud, (5) accounting, and (6) declaratory judgment” against the brokers the plaintiff paid to arrange its employee benefit coverage. When the plaintiff learned that its employees claims were not being paid and coverage was not being purchased, Paysource filed suit.

77. Id. at 500.
78. Id.
79. Id. at 498.
80. Id. at 501.
81. See Penny/Ohlmann/Nieman Inc., 399 F.3d at 697-99.
83. Id. at *2.
84. Id. at *1.
85. Id. at *2 (quoting LeBlanc v. Cahill, 153 F.3d 134, 147 (4th Cir. 1998) and Penny/Ohlmann/Nieman Inc., 399 F.3d at 698).
86. Id. at *2.
88. Id. at *1-2.
89. Id. at *1.
contended that the claims were preempted by ERISA, and the court determined that:

[P]laintiff’s claims against [defendant] are not preempted by ERISA. First, the Plan makes absolutely no mention of the . . . defendants, and the court need not consult the Plan in connection with plaintiff’s claims against them. [Plaintiff’s] claims arise, not from the Plan, but from separate oral agreements and representations allegedly made by [defendant]. Thus, plaintiff’s claims do not arise from an ERISA plan. 90

Relying heavily on PONI, the court further held that the plaintiff’s costs to cover its employees were not a claim for benefits, but merely a reference to the damages suffered. 91

The Kentucky district court again relied heavily on the PONI analysis in Hall v. MLS Nat’l Med. Evaluations, Inc. 92 In Hall, the court found that ERISA did not preempt a state-law claim merely because the plaintiff sought to recover benefits he would have received from a non-ERISA entity had it not submitted a false report. 93 After reviewing the facts and applying the four factor test adopted in PONI, the court stated:

The defendants in this case are not among the traditional Plan entities. They do not exercise management, authority, or control over the Plan or its assets. Nor do [plaintiff]’s claims implicate any of the Plan entities. Rather, [plaintiff] alleges that the defendants transmitted a false report to the Plan administrator, and that this report caused the Plan administrator to terminate his benefits. [plaintiff] does not seek redress for the wrongful denial of benefits under the terms of the Plan. Instead, he alleges that the defendants breached an independent duty not to transmit fraudulent information. Such claims are not preempted by ERISA. 94

The Kentucky district courts have also relied on Briscoe after applying the PONI analysis. 95 In Overall v. Sykes Health Plan Services, Inc., the Western District of Kentucky Court concluded that the plaintiff’s fraud and breach of contract claims arose solely from the plan administration. 96 The plaintiff, who was denied insurance coverage due to defendants’ administration errors, filed suit to recover the benefits he believed he was entitled to under the Plan. 97 Citing Briscoe, the court found the plaintiff’s claims to be preempted because:

90. Id. at *3.
91. Id. at *4.
93. Id. at *5-7.
94. Id. at *5-6. (citing Briscoe, 444 F.3d at 498).
96. Id. at *2-4.
97. Id. at *4.
Here, Plaintiff is merely relabeling his ERISA claims for an alleged error in the administration of his benefits as breach of contract and fraud claims. He seeks benefits he was denied as a result of an alleged error and other misconduct by SHPS, in addition to other damages. Plaintiff has not pointed to any violation of a legal duty independent of ERISA. Any duty that SHPS owed to Plaintiff arose out of the existence and nature of the plan itself. As he is merely attempting to bring his current claims as an alternative means of recovering benefits he claims he was entitled to under the Plan, those claims are preempted.98

_McMurtry v. Wiseman_,99 a district court decision from the Western District of Kentucky, is also instructive. In _McMurtry_, the court found that ERISA did not preempt state law claims of fraud and negligent misrepresentation against an insurance agent who misrepresented facts and induced the plaintiff to purchase a disability plan.100 The plaintiff pursued the agent of the insurance provider who had an independent duty not to misrepresent the policy.101 The court found that the subject claims were traditional areas of state law not specifically referenced within ERISA, and that under the _PONI_ and _Briscoe_ analysis, the claims only affected relations of one ERISA entity, the beneficiary.102 The court found that the claims did not affect the structure, administration or type of benefits provided under the ERISA plan because the claim was based solely on the inducement to enroll in the plan, and not to recover under the plan.103 Even with the guidance of _PONI_ and decisions by other circuits, the court stated:

Here, the Court has found that certain state law claims are not preempted in the case. However, as noted, the Court believes this to be a very close determination. Reasonable minds could differ on the conclusion reached by this Court. This finding by the Court certainly is not conclusive one way or the other as to whether the Defendants violated the standard of care in this case.104

V. CONCLUSION

Over the years, the Supreme Court has struggled to define the scope of ERISA preemption.105 Recent decisions seem to indicate that the court will no longer grant broad preemptive power to ERISA.106 The Court now acknowledges

98. _Id._ (internal quotes and citations omitted).
100. _Id._ at 777-78.
101. _Id._ at 763.
102. _Id._ at 776.
103. _Id._ at 767.
104. _Id._ at 778.
105. _See_, e.g., _Travelers_, 514 U.S. 645.
106. _See generally id._
that ERISA has limits, and is currently attempting to define those limits.\textsuperscript{107} The Sixth Circuit has embraced this shift and seems quite willing to define and recognize state claims that are not preempted by ERISA.\textsuperscript{108} Kentucky courts appear to follow this trend of finding minimal to no preemption by carving limited exceptions.\textsuperscript{109} Until the Supreme Court provides more guidance, this approach is likely to continue.


\textsuperscript{108} See Marks, 342 F.3d at 453.
