

A Limit on Liability for Your Partner's (Allegedly) Bad Behavior

AUTHOR: SANDBERG PHOENIX

Attorneys are well aware a law firm's partner(s) can take actions that may result in liability for all partners of the firm. Limited liability partnerships (LLPs) may offer some additional protection in this area by precluding personal liability for the acts of another limited liability partner.

In New Jersey, a recent case confirms that courts there cannot convert LLPs into general partnerships in an attempt to hold a partner personally liable for the actions of another partner. This additional protection may offer some motivation to adopt an LLP model, at least in states like New Jersey that offer and uphold this protection.

Case Background

John Ward and John Olivo founded Ward & Olivo, L.L.P., an intellectual property law firm, as a limited liability partnership ("W&O"). They maintained a professional liability insurance policy, which New Jersey statutes and court rules require if attorneys wish to practice law there in the form of an LLP.

In 2009, plaintiff Mortgage Grader retained W&O to sue various parties for patent infringement. On June 30, 2011, partners Ward and Olivo stopped actively practicing law as W&O and began winding up the law practice by collecting outstanding legal fees. W&O's professional liability policy expired on August 8, 2011; W&O did not purchase a "tail" insurance policy to cover the remaining time period. Later, when partner Olivo's legal advice allegedly harmed Mortgage Grader's patent rights, Mortgage Grader filed a legal malpractice claim against W&O and partners Olivo and Ward individually.

Trial Court's Decision

The trial court determined W&O had not ceased practicing law before the liability policy expired, because W&O continued collecting outstanding legal fees. No surprise there.

The kicker, however, was that the trial court also held W&O became a general partnership once its liability policy expired (the court essentially imposed this holding as discipline for failing to maintain liability insurance). Partner Ward argued the trial court acted without authority when it converted the LLP into a general partnership.

The Appellate Division Steps In

The Superior Court of New Jersey, Appellate Division held the relevant New Jersey statute clearly expressed the legislature's intent that partners of an LLP be shielded from liability for a fellow partner's acts. Under the statute, the LLP's status remains effective until the LLP itself cancels its status. Only in the absence of this LLP status does New Jersey hold that all partners are jointly and severally liable for all partnership obligations.

At the same time, the plain language of New Jersey's court rules states an LLP must maintain malpractice insurance for attorneys to practice law as an LLP. The rules enumerate specific sanctions against LLPs for failing to maintain malpractice insurance (e.g., "any violation by the LLP shall be grounds for the Supreme Court to terminate or suspend the LLP's right to practice law or otherwise to discipline it").

The Appellate Division held the plain language of the statute and rules do not permit a trial court to convert an LLP into a general partnership; therefore, the trial court could not make any such conversion. Other forms of discipline are available to the trial court, such as censure or disbarment, but this kind of corporate conversion was and is not an available remedy in New Jersey.

The Take-Away

This blog entry is not intended to suggest that partners ignore the acts of their fellow partners when operating as an LLP (or in any other form, for that matter). Our profession, like others, is replete with stories and anecdotes about one or more partners' poor judgment or bad behavior affecting the organization as a whole—and often, no ethical violation or discipline is involved, other than the discipline of the marketplace.

The story of partners Ward and Olivo and their LLP, W&O, does confirm, however, that courts in New Jersey cannot convert an LLP into a general partnership. The LLP protection will remain in place, as the legislature there intended and directed.

At the same time, this story reminds us courts do not look kindly on attorneys failing to comply with practice rules. Be sure to follow any specific requirements set forth in statutory or court rules for the type of corporate structure your firm has in place (e.g., LLC, LLP, LP, PC, etc.). Additionally, by all means **maintain malpractice insurance!** Do so at all times: from the inception of a practice until it is wound up (if ever). Failure to maintain such insurance may result in numerous penalties, and may also result in personal liability in some jurisdictions, even though such a result did not happen in this particular case out of New Jersey.

By Tyler Thompson

Thompson, T. Ind or type unknown