Risk Managing Limited Liability Forms of Practice

With the Supreme Court's recent approval of limited liability forms of practice new risk management and professional responsibility issues come into play. Under the new rules an attorney remains personally liable to clients for the attorney's own acts, errors, and omissions, and those of any attorney directly supervised - but is not vicariously liable for other firm lawyer malpractice. To aid in converting to a limited liability form of practice we offer a compilation of risk management questions with at few suggestions for your evaluation on how best to proceed. Until Kentucky's limited liability forms of practice laws and rules are interpreted it is not possible to recommend specific actions with authority. *(For information on limited liability practice see the article "Supreme Court Approves Limited Liability Forms of Practice for Kentucky Lawyers" in our Winter 2000 newsletter at www.lmick.com.):*

Notice: How should clients be notified that the firm's form of practice limits liability? Is it necessary to get express consent to limited liability from clients for limited liability to be effective?

When a firm converts to a limited liability form of practice notice of the change should be given to current clients. Some commentators take the position that, unless the limitation is in writing in clear and precise terms, vicarious liability is not avoided. Furthermore, without express consent to the change a client may later argue that the limitation was not effective. This could be troublesome both for current partners and partners leaving a firm believing they need not worry about vicarious liability for on-going matters at the time of departure.

New clients of a limited liability practice should be notified of the liability limitation in a letter of engagement in clear and precise terms to be sure that vicarious liability is avoided. The ABA Standing Committee on Ethics and Professional Responsibility in a lawyer friendly opinion allows a less stringent approach to new client notification if legislation approves the use of initials:"Criterion No. 2 in Formal Opinion 303 required that restrictions on liability as to other lawyers in the organization be made apparent to the client. While a minority of this committee is concerned that the use of initials, without more, is not sufficient to make the limitation of liability apparent to the client, most of the committee members are of the view, based upon the legislative approval of the use of initials and the relative unimportance, today, of the lawyer's business form for clients, that the use of initials, without more, is adequate to meet ethical criteria. The majority is of the view that the abbreviation places clients on notice that their lawyer is practicing in a particular business form, and encourages them to inquire if they are in doubt as to its implications for them. When faced with such inquiries from clients, of course, a lawyer must clearly explain the limitation of liability features of his firm's business organization. The Committee cannot and does not express any opinion as to whether, as a matter of law, the use of initials is sufficient to shield the partners of a lawyer held liable for malpractice from vicarious tort liability.

As an aside, we note that the use of a statutorily required or permitted abbreviation on letterhead, professional and media announcements, and in other public contexts, satisfies the requirements of Model Rules 7.1 and 7.5(a) that a lawyer's public communications

not be "misleading" or "deceptive." *Cf* ABA Formal Opinion 94-3 88 (1994) ("Relationships Among Law Firms"). Limited liability partnerships are indeed partnerships, and thus there is no actual or implied misrepresentation when a firm describes itself as such." (Formal Opinion 96-401, Lawyers Practicing in Limited Liability Partnerships, 8/2/96)

The safest notice procedure is to give detailed notice of liability limitations to clients in writing that they acknowledge by signing.

Internal Firm Issues: Firms should consider how these questions will be managed.

Shared Profits v. Shared Risk: High risk areas of practice usually produce the most firm income. Should partners or shareholders in lower risk practice areas share in the proceeds, but not the liability? Should a firm have a policy of inter-partner or shareholder contribution to equalize risk? If so, has the firm reinstated vicarious liability?

Supervisory Responsibility and Mentoring: Will lawyers decline to serve on management and executive committees to avoid supervisory personal liability on all firm's matters? Will lawyers be reluctant to mentor new lawyers? How do the professional responsibility rules on supervisory responsibility affect liability issues (Rule 5.1 Responsibilities of a Partner or Supervisory Lawyer, Rule 5.2 Responsibilities of a Subordinate Lawyer, and Rule 5.3 Responsibilities Regarding Nonlawyer Assistants)? Should a firm have a policy of inter-partner or shareholder contribution to cover these special situations?

Cooperation Among Firm Lawyers: Will lawyers be reluctant to assist another lawyer in the firm on a complex matter or perform file and opinion review of matters they are not handling? What about rainmakers handing off a new client to another firm lawyer without further active representation? Is the rainmaker personally liable for the matter? The client will in all likelihood think so. Should a firm have a policy of inter-partner or shareholder contribution to cover these special situations?

Sophisticated Clients: Should the sophisticated client asking for personal guarantees of all the firm lawyers be given special treatment?

Multi-State Practice: Most Kentucky firms are engaged in multi-state practice to some extent.

Not all states permit limited liability forms of practice. Those that do may have laws that conflict with Kentucky's or impose conditions such as financial responsibility requirements. Before entering another state be sure to know what the implications of limited liability practice are in that state. Make sure you are eligible for limited liability status or have an insurance program that protects you if limited liability is voided in a court action in the other jurisdiction.