Limiting Lawyer Liability in West Virginia

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LIMITING LAWYER LIABILITY
IN WEST VIRGINIA

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I. INTRODUCTION

In recent years, the number of malpractice claims against attorneys and their partners has increased significantly. In fact, a recent law school graduate can expect to be sued three times during her or his career. Furthermore, the dollar amount of malpractice judgments has increased, as have malpractice insurance premiums. Moreover, the average malpractice loss of $1.3 million has risen to approximately $7.9 million.

Most law firms continue to be organized as general partnerships across the United States. Generally, partners are jointly and severally liable for all obligations of the partnership, including the wrongful acts or omissions of another partner acting in the ordinary course of partnership business. Recent changes in lawyer malpractice liability and the availability of limited liability business organizations now provide lawyers with both the opportunity and incentive to limit their liability for their partners’ malpractice, or in some cases, other firm obligations. Limited liability business organizations include professional corporations, professional limited liability companies, and registered limited liability partnerships. Accordingly, lawyers should consider the use of limited liability organizations in an effort to limit personal liability and to protect their personal assets. In West Virginia, attorneys desiring to limit their liability have the option of operating as a professional corporation (PC), a professional limited

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2 Id. at 349.

3 Id. at 365; see also Jennifer J. Johnson, Limited Liability for Lawyers: General Partners Need Not Apply, 51 BUS. LAW. 85 (1995).


6 W. VA. CODE § 47B-3-6 (1996).

limited liability company (PLLC), or a registered limited liability partnership (LLP). This note primarily addresses the limited liability protection potentially afforded by the PLLC and the LLP in West Virginia, the formation procedure, and the factors that firms should consider prior to forming a LLP or PLLC.

II. LIMITED LIABILITY BUSINESS ENTITIES

Ethics rules prohibit lawyers from prospectively shielding themselves from liability for their own conduct. Thus, "limited liability" in the context of a law firm refers to "(i) personal liability for the general business debts of the firm, such as bank loans, computer purchases, and office leases; (ii) personal liability for torts unrelated to the practice of law; or (iii) vicarious liability for malpractice or other wrongful acts committed by those with whom the lawyer is associated." None of the limited liability entities shield the lawyer from liability for his or her personal acts. Furthermore, none of the entities shield the firm or its assets from liability.

A. The Professional Corporation

Virtually every state, with the possible exception of Kentucky, permits lawyers to organize and practice as a professional corporation. The professional corporation may not be the most advantageous business entity for law firms.

10 Rule 1.8(h) of the Rules of Professional Conduct, provides in pertinent part: "A lawyer shall not make an agreement prospectively limiting the lawyer’s liability to a client for malpractice unless permitted by law and the client is independently represented in making the agreement." West Virginia Rules of Professional Conduct Rule 1.8(h) (1988).
11 Johnson, supra note 3, at 91-92.
12 Id.; see also John T. Ballantine and Thomas E. Rutledge, Kentucky Supreme Court Rejects the Use of LLCs, LLPs, and PSCs by Attorneys, Ky. Bench & Bar, Winter 1996, at 21.
15 Rosencrantz, supra note 1, at 357.
Attorneys organized as a PC may be subject to double taxation.\textsuperscript{16} As a result, PC shareholders may lose as much of fifty percent of each pre-tax dollar earned.\textsuperscript{17} Furthermore, in some states, shareholders of professional corporations are not shielded from vicarious liability for legal malpractice or torts.\textsuperscript{18} West Virginia explicitly permits lawyers to form professional corporations.\textsuperscript{19} In addition, West Virginia does not require a minimum amount of malpractice insurance or escrowed deposit, unlike the requirements of the PLLC or LLP statutes.\textsuperscript{20} Whether lawyers as shareholders of a professional corporation practicing in West Virginia would be protected from vicarious liability has not been determined by the Supreme Court of Appeals of West Virginia.\textsuperscript{21} Some state courts have refused to limit a shareholder’s liability for malpractice,\textsuperscript{22} while other state courts have protected the shareholders of the PC from vicarious liability resulting from the malpractice of another associated lawyer.\textsuperscript{23}

\textbf{B. The Limited Liability Partnership}

In 1996, the West Virginia legislature authorized the use of the Registered Limited Liability Partnership (LLP) for use by professionals.\textsuperscript{24} Furthermore, the Supreme Court of Appeals of West Virginia has authorized lawyers to form LLPs.\textsuperscript{25}

\begin{itemize}
  \item \textsuperscript{16} \textit{Id.} The effects of double taxation can often be ameliorated through the use of an “S” election or through the payment of reasonable salaries. See I.R.C. §§ 1361 and 1362 (1994).
  \item \textsuperscript{17} Rosencrantz, \textit{supra} note 1, at 357.
  \item \textsuperscript{19} W. VA. CODE § 30-2-5a (1993 & Supp. 1997).
  \item \textsuperscript{21} Maxey, \textit{supra} note 18, at 967.
  \item \textsuperscript{22} Id.
  \item \textsuperscript{23} Id.
  \item \textsuperscript{24} W. VA. CODE § 47B-3-6(c) (1996).
  \item \textsuperscript{25} See \textit{WEST VIRGINIA RULES OF PROFESSIONAL CONDUCT Rule 5.7} (1996).
\end{itemize}
The LLP first appeared in Texas in 1991. Many law firms may prefer the LLP over the PLLC because of the familiarity with the partnership entity and partnership management.

As a member of an LLP, a partner is still liable for his own "omissions, negligence, wrongful acts, misconduct or malpractice, or that of any person under the partner's direct supervision and control." However, the LLP partner will not be personally liable "directly or indirectly for debts, obligations, and liabilities" of the partnership arising from omissions, negligence, wrongful acts, misconduct or malpractice committed while the partnership is an LLP and, in the course of partnership business by another partner, employee, agent or representative of the partnership. The statute does not relieve a partner in an LLP from the general obligations of the firm beyond vicarious liability imposed for a partner's malpractice. Furthermore, the LLP must carry at least $1,000,000 of liability insurance which protects the partnership and partners from liability for omissions, negligence, wrongful acts, misconduct and malpractice. In lieu of carrying such insurance, the LLP may deposit in escrow or provide a letter of credit in the same amount to cover any judgment against it or its partners.

To form an LLP, the partnership must file with the Secretary of State with a fee of $250. The LLP must also pay $500 annually as a maintenance fee to the

26 Johnson, supra note 3, at 106.

27 Unlike a PLLC, a LLP is not a new form of entity. It is a general partnership. By selecting a LLP format, a firm may be able to continue using its existing partnership agreement. A PLLC, on the other hand, will likely necessitate a new "operating agreement." Because the operating agreement sets forth the members' rights and responsibilities, this difference offers an opportunity to raise management and firm structure issues and may, thus, bring up issues that would not be brought up in the LLP context.

28 W. VA. CODE § 47B-3-6(d) (1996).

29 W. VA. CODE § 47B-3-6(c) (1996).

30 Id.


33 W. VA. CODE § 47B-10-1(c) (1996). In addition, the filing must include a statement of registration which contains the name of the partnership; its principal office address; if its principal office is located outside of West Virginia, the address of a registered office and of a registered agent for service of process in West Virginia; a brief statement of the partnership business; and any other matters that the partnership wishes to include. W. VA. CODE § 47B-10-1(a) (1996). The registration must be signed by at least one of the partners authorized to execute a registration. W. VA. CODE § 47B-10-1(b)
Secretary of State.\textsuperscript{34} The filing must include the name of the partnership; the address of its principal office; a brief statement of the partnership's business; and "any other matters that the partnership determines to include."\textsuperscript{35} Firms wishing to practice as registered limited liability partnerships need not register with the state bar.\textsuperscript{36} Upon registration, the name of the partnership must contain the words "Registered Limited Liability Partnership" or the abbreviation "L.L.P." or "LLP" at the end of the partnership name.\textsuperscript{37}

C. The Professional Limited Liability Company

In 1992, West Virginia was one of the first ten states to adopt laws providing for limited liability companies.\textsuperscript{38} While the 1992 Act may have been important, pioneering legislation, the rapid evolution of the use of limited liability companies left many questions unanswered. For example, the 1992 Act was silent on whether professionals could utilize the LLC format.\textsuperscript{39} Moreover, the 1992 Act did not allow West Virginia LLCs to utilize favorable IRS guidance that was issued subsequent to its passage.\textsuperscript{40} In an effort to address these, and other issues, on March 9, 1996, the West Virginia Legislature adopted Senate Bill 338 (the "1996 Act"), which adopted the Uniform Limited Liability Company Act ("ULLCA") and added specific provisions expressly extending the limited liability company provisions to professionals.\textsuperscript{41} Furthermore, on September 5, 1996, the Supreme Court of

\textsuperscript{34} W. VA. CODE § 47B-10-1(e) (1996). "The fee must be accompanied by a notice as provided by the secretary of state or any material changes in the information contained in the partnership registration." \textit{Id.}

\textsuperscript{35} W. VA. CODE § 47B-10-1(a) (1996).


\textsuperscript{37} W. VA. CODE § 47B-10-4(e) (1996).

\textsuperscript{38} See W. VA. CODE § 31-1A-1 et seq. (1992) (the "1992 Act").

\textsuperscript{39} See Maxey, \textit{supra} note 18, at 967.

\textsuperscript{40} See Rev. Proc. 95-10, 1995-1 C.B. 501.

\textsuperscript{41} W. VA. CODE § 31B-13-1301 (1996). In addition to attorneys, the West Virginia PLLC statute is also applicable to physicians and podiatrists, dentists, optometrists, veterinarians, engineers, osteopathic physicians and surgeons, and chiropractors. The licensing boards of each of the
Appeals of West Virginia adopted Rule of Professional Conduct 5.7, "Limited Liability Legal Practice," authorizing both the PLLC and the LLP for lawyers. Additionally, an ethics opinion issued by the West Virginia State Bar indicates that lawyers forming limited liability organizations do not violate ethical standards as established.


Rule 5.7 Limited Liability Legal Practice states:

(a) A lawyer may be a member of a law firm that is organized as a limited liability company or registered limited liability partnership (collectively, "limited liability organizations") solely to render professional legal services under the laws of West Virginia, including but not limited to, the Uniform Limited Liability Act, W. Va. Code §§ 31B-1-101 to 31B-13-1306, and the Uniform Partnership Act, W. Va. Code §§ 47B-1-1 to 47B-11-5, and may practice in or as such a limited liability organization, provided that such lawyer is otherwise licensed to practice in West Virginia and such law firm is registered pursuant to rules promulgated by the West Virginia State Bar.

(b) Nothing in this rule or the laws under which a lawyer or law firm is organized shall relieve a lawyer from personal liability for the acts, errors, and omissions of such lawyer arising out of the performance of professional legal services.

(c) Law firms wishing to practice as limited liability organizations under this rule shall comply with the rules of the West Virginia State Bar with regard to registration of limited liability organizations.

(d) A law firm organized as a limited liability organization under the laws of any other state or jurisdiction of the United States solely for the purpose of rendering professional legal services and authorized to do business in West Virginia and which has at least one lawyer licensed to practice law in West Virginia may register in West Virginia as a limited liability organization under this rule by registering pursuant to rules promulgated by the West Virginia State Bar.

The Legislature has enacted two bills potentially affecting attorneys, one authorizing registered limited liability partnerships [citations omitted] and the other adopting the Uniform Limited Liability Company Act [citations omitted]. Both of these statutes permit professionals to limit their liability for the acts of other partners or members with whom they practice if they are not directly supervising them. It is a requirement of both of these statutes that a limited liability partnership or limited liability company consisting of professionals such as lawyers carry malpractice insurance of $1,000,000.00.

The passage of these statutes raises the question of whether a lawyer may participate in a limited liability partnership or a limited liability company
Under the PLLC provisions of the 1996 Act, a member, manager, agent, or employee remains liable for his or her "negligent or wrongful act or omission in which the individual personally participated to the same extent as if the individual rendered the professional services as a sole practitioner." However, a member, manager, agent, or employee of the PLLC will not be personally liable for any debts or claims against, or the acts or omissions of the PLLC or of another member, manager, agent, or employee of the PLLC simply because of his or her affiliation with the PLLC. In short, lawyers affiliated in a PLLC will not be held liable for the acts of the other lawyers, but the lawyer will be liable for his or her own obligations.

1. Procedure to Form PLLC in West Virginia

Forming a PLLC is a relatively simple process. The PLLC must carry at least $1 million in malpractice coverage (or provide for a $1 million cash reserve without violating Rule 1.8(h) of the Rules of Professional Conduct, which provides in pertinent part:

(h) A lawyer shall not make an agreement prospectively limiting the lawyer's liability to a client for malpractice unless permitted by law and the client is independently represented in making the agreement. It is the opinion of the Lawyer Disciplinary Board that Rule 1.8(h) speaks to a lawyer's personal liability to a client, rather than the law firm's liability as a whole. Therefore, a client need not be independently represented before hiring a limited liability partnership or limited liability company for legal relationship. [The ethics opinion then notes that the position followed has also been followed by New York City, Washington, D.C., Alabama, Michigan, and Mississippi. The opinion also "does not purport to address any legal issues that may arise from the enactments" of the statutes].


45 W. VA. CODE § 31B-12-1305(b) (1996).


to cover claims). Two or more licensed lawyers may form a PLLC. Only lawyers may be members or owners of the entity. In addition, the name of the PLLC must contain the words “professional limited liability company” or the abbreviation “P.L.L.C.” or “Professional L.L.C.” The PLLC must file proposed articles of organization with the state bar with a $100 application fee. Following approval by the West Virginia State Bar, the articles of organization must also be filed with the Secretary of State accompanied by a $100 filing fee. The LLC’s articles of organization must contain (1) its name, (2) the address of its initial designated office, (3) the name and street address of the initial agent for service of process, (4) the name and address of each organizer, (5) whether the LLC is.

48 Id.; see also W. VA. CODE § 31B-13-1305(e) (1996).

49 W. VA. CODE § 31B-13-1302(a) (1996). The requirement of two members necessary to form a PLLC differs from the general rule for West Virginia LLCs, which requires only one member for formation. See W. VA. CODE § 31B-2-202(a) (1996).

50 See generally Rule of Professional Conduct 5.4(d): Professional Independence of a Lawyer. A lawyer shall not practice with or in the form of a professional corporation, association, or limited liability organization authorized to practice law for a profit, if:

(1) a nonlawyer owns any interest therein, except that a fiduciary representative of the estate of a lawyer may hold the stock or interest of the lawyer for a reasonable time during administration;

(2) a nonlawyer is a corporate director or officer thereof or a manager of a professional limited liability company; or

(3) a nonlawyer has the right to direct or control the professional judgment of a lawyer.

WEST VIRGINIA RULES OF PROFESSIONAL CONDUCT Rule 5.4(d) (1996); see also W. VA. CODE § 31B-13-1302(b) (1996).


52 State Bar Rules, supra note 36, at ¶ 3(a).


to be a term LLC and, if so, the term specified,\(^5\) (6) whether the LLC is to be manager-managed, and, if so, the name and address of each initial manager;\(^5\)\(^9\) and (7) whether one or more of the members of the LLC are to be liable for its debts and obligations.\(^6\) The articles of organization may also recite operating agreement provisions.\(^6\)\(^1\) The 1996 Act requires the LLC to file a report annually with the Secretary of State.\(^6\)\(^2\)

Although the statute does not require an operating agreement,\(^6\)\(^3\) law firms will likely want to prepare written operating agreements.\(^6\)\(^4\) Preparation of the operating agreement is crucial for several reasons. First, an operating agreement, like a partnership agreement, establishes the members' rights and responsibilities with respect to the entity's business. Moreover, the 1996 Act provides a detailed series of rules which apply unless overridden by an operating agreement.\(^6\)\(^5\)

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\(^6\)\(^1\) See W. VA. CODE § 31B-2-203(b) (1996). If members are considering placing information in the articles of organization which are not required by statute, the members should be aware that such matters will become public record. Moreover, if such additional information is placed in the articles of organization, the articles, in addition to the operating agreement, would need to be amended should members desire to change provisions. \textit{Id.}

\(^6\)\(^2\) W. VA. CODE § 31B-2-211 (1996). The annual report must include the name of the company and the state or country where organized; the address of its designated office and the name and address of its agent for service of process within West Virginia; the address of its principal office; and the names and business addresses of any managers. The annual report is due to the Secretary of State before April 1 in the year following the calendar year in which the company was organized. \textit{Id.}

\(^6\)\(^3\) W. VA. CODE § 31B-1-103 (1996).

\(^6\)\(^4\) An operating agreement under the 1996 act may be oral or in writing. In the absence of an operating agreement, the default provisions of the 1996 LLC act apply. W. VA. CODE § 31B-1-103(a) (1996).

\(^6\)\(^5\) W. VA. CODE § 31B-1-103(b) (1996). This section provides nonwaivable provisions under the 1996 Act. The statute provides that the operating agreement may not eliminate the duty of loyalty as defined by section 4-409(b) or section 6-603(b)(3); or the obligation of good faith and fair dealing under section 4-409(d). Furthermore, the operating agreement may not unreasonably restrict a right to information or access to records under section 4-408; or reduce the duty of care under section 4-409(c) or section 6-603(b)(3). The right to expel a member under section 6-601(6) and the requirement to wind up the limited liability company's business under sections 8-801(b)(4) or (b)(5) may not be varied. The operating agreement may not restrict the rights of a person other than a manager, member, and transferee of a member's distributional interest, under the statute. On the other hand, the statute does provide methods by which LLC members can modify the various requirements.
example, in a member managed PLLC, if the members do not provide their own rules, the default rules generally will cause the PLLC to dissolve on the death of any member unless a majority of the remaining members vote to continue the business after the death of that member.66 While many firms may desire this rule, others may not particularly because dissolution can have negative tax and business consequences. Thus, the applicability of the default rules must be carefully considered by each firm forming a PLLC.

2. West Virginia State Bar Application Requirements

Generally, the state bar application to become a PLLC must provide the name and residence of each member,67 two copies of the proposed Articles of Organization,68 the name and address for the manager or managers,69 and a certificate of insurance or evidence that the firm complies with the statutory deposit requirements.70 The application must be accompanied by a fee of $100 and must be signed under oath by the manager or managers of the PLLC.71 Upon receipt of the application, the West Virginia State Bar must act within 30 days.72 If the state bar determines the application is proper, the bar will notify both the applicant and the Secretary of State.73 If the bar denies the application, the bar must indicate the reasons in writing to the applicant and notify the Secretary of State.74


67 State Bar Rules, supra note 36, at ¶ 3(a)(1).

68 State Bar Rules, supra note 36, at ¶ 3(a)(2).

69 State Bar Rules, supra note 36, at ¶ 3(a)(3).

70 State Bar Rules, supra note 36, at ¶ 3(a)(4).

71 State Bar Rules, supra note 36, at ¶ 3(b).

72 See State Bar Rules, supra note 36, at ¶ 3(d). However, if the applicant fails to respond to any requests for additional information or for clarifications, the state bar need not act within the 30 days. Id.

73 Id.

74 Id.
3. Conversion of a General Partnership to a PLLC

The 1996 Act provides specific procedures for converting a general partnership to a LLC. While "[t]he Internal Revenue Service has indicated that [when the members' interest in the business remain the same before and after the conversion], the conversion of a general partnership to an LLC is generally not a significant tax event." No conversion should be made without first consulting a tax advisor.

4. Conversion of a Corporation to a PLLC

The 1996 Act does not provide for the conversion of a corporation to a PLLC. For federal income tax purposes, such a conversion would be viewed as a liquidation of the corporation. If the corporation has earnings and profits or appreciated assets, the liquidation would be a taxable event. Accordingly, a corporation should never be converted to a PLLC without consulting a tax advisor prior to such conversion.

III. COMPARISON OF LIMITED LIABILITY ENTITIES

Basically, the PLLC, the LLP, and the PC are formed for the same reason -- to limit the individual partner's liability for the liabilities incurred by the firm. However, many differences between the three entities exist that merit consideration. For tax reasons, the PLLC and LLP may be more attractive to law firms

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77 For example, in certain cases, conversion could lead to the loss of the ability to use the cash method of accounting (potentially accelerating income and/or creating "phantom income") or could prevent the business from deducting certain payments to retiring partners. For a detailed discussion of the federal income tax consequences of converting a partnership to an LLC see David A. Miller, The Federal Income Tax Consequences of Converting a Partnership into a LLC, 3 JOURNAL OF LIMITED LIABILITY COMPANIES (Fall, 1996).


80 See I.R.C. §§ 331, 336.

81 Lorensen, supra note 47, at 14.
because of the combination of pass-through treatment of income with limited liability. For example, S Corporations cannot make an I.R.C. Section 754 election nor can the S Corporation make tax deferred distributions of appreciated property or obtain basis for borrowing by the S Corporation. Additionally, unlike a PLLC or LLP, an S Corporation must make a timely “S” election and must meet all the requirements of Subchapter S of the Internal Revenue Code, which limits the number of shareholders to 75. Furthermore, an S Corporation may have only one class of stock. While these requirements are not particularly onerous, they do impose an additional administrative burden.

Law firms may prefer the LLP over the PLLC because of the familiarity of operating as a partnership. However, law firms should at least consider the following two general factors in contemplating the PLLC or LLP.

* PLLCs generally afford lawyers substantially greater liability protection than LLPs. For example, members of an LLC are shielded from contract claims that might not be covered by an LLP’s insurance policy and therefore, can be asserted against an LLP’s general partners jointly and severally.

* LLPs generally raise less significant tax issues than do LLCs (especially for larger firms). For example, larger firms may have difficulty maintaining cash basis accounting for income tax purposes and may face uncertainty in deducting payments to retiring partners.

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82 Admittedly a PC also may, if a timely selection is made, provide pass-through tax treatment. Such tax treatment, however, is generally not as favorable as the partnership tax treatment given to properly formed PLLCs and LLPs.


86 Lorensen, supra note 47, at 14.

87 Id. at 14-15.
IV. CONSIDERATIONS IN CONVERTING TO A LIMITED LIABILITY ENTITY

A. Client Notification

Although West Virginia’s PLLC and LLP statutes are silent regarding the notification of clients upon conversion to either of these limited liability enterprises, some states require explicit notification. Yet, other states require only that the name be changed to give notice. For example, The District of Columbia Bar Association ruled that “upon client inquiries, a summary of the limited liability features of the new entity must be provided.” For this purpose, it would suffice to describe the limited liability features” that the applicable statute provides. For example, under this opinion, the actual language provided by the applicable statute would be sufficient to inform clients of the effect of the firm’s business entity change on limiting potential liability.

B. Possible Changes in Employment Relationship

Lawyers converting to the PLLC may possibly face a “variety of issues relating to the various federal equal employment opportunity statutes.” Although several of the equal employment opportunity laws explicitly protect employees from discrimination by their employers, partners generally are not covered by the statute. However, it is unclear whether the equal employment opportunity laws will cover “members” of a PLLC. Courts have held inconsistently as to whether shareholders of a professional corporation are protected by the equal employment

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89 Johnson, supra note 3, at 121.

90 Id.


93 Id.

94 Id.
opportunity laws.95

C. Tax Considerations96

Under the recently promulgated Simplification of Entity Classification Rules, also commonly know as “Check-the-Box” rules,97 LLCs and LLPs now may opt to be classified as either a partnership or corporation for federal income taxation purposes.98

Any business entity that is not required to be treated as a corporation for federal tax purposes (referred to in the regulation as an eligible entity) may choose its classification under the rules of § 301.7701-3. Those rules provide that an eligible entity with at least two members can be classified as either a partnership or an association, and that an eligible entity with a single member can be classified as an association or can be disregarded as an entity separate from its owner.99

Previously, Treasury Regulations required that to be classified as a partnership, the PLLC could have no more than two of the following corporate characteristics: (a) limited liability; (b) centralization of management; (c) free transferability of interests; and (d) continuity of life.100

95 *Id.* at 122-3.

96 See generally David A. Miller, *The Federal Income Tax Consequences of Converting a Partnership into an LLC*, 3 *JOURNAL OF LIMITED LIABILITY COMPANIES* 71 (Fall 1996). Furthermore, firms should consult a tax advisor prior to converting to a limited liability organization. Lorenzen, supra note 47, at 14.


99 *Id.*

Under West Virginia taxation law, corporations, partnerships and PLLCs are subject to the business franchise tax. The business franchise tax is imposed on associations for the privilege of conducting business in West Virginia.

D. Lack of Precedent

Because the PLLC form is relatively new, very little common law exists in interpreting the statutes. Questions exist as to whether corporate or partnership common law provisions will be applied in the event of a dispute. Courts probably will apply partnership law and/or corporate law in interpreting the LLC statutes. However, “courts should do so cautiously since there are important differences between LLCs and partnerships, limited partnerships and corporations.”

For example, an LLC is not exactly like a limited partnership since LLC statutes provide by default for direct member management. Even if the LLC opts out of member management and provides for centralized management by managers, the firm still differs from a limited partnership in that all members and managers have limited liability and there is no “control rule” conditioning the limited liability of non-managing members. This may impact other LLC default rules. For example it arguably follows from the greater participation of LLC members in management that LLC managers' default fiduciary duties need not be as intense as those of general partners in limited partnerships.

Additionally, the concept of “piercing the corporate veil” may be applicable to the


102 Id.

103 Johnson, supra note 3, at 144.

104 See Rosencrantz, supra note 1, at 361-2.


106 Id.

107 Id.
The ULLCA contains language indicating that the failure of the LLC to observe formalities should not cause liability to be imposed on individual members. Furthermore, some courts have applied corporate law precedent to both the LLC and the LLP.

E. Firms Engaged in Multi-state Practice

1. West Virginia Limited Liability Firms Practicing Outside West Virginia

Firms engaged in multi-state practice must consider whether the liability shield of the limited liability organization will protect its members where the firm practices outside the state of formation. Many states with LLC and LLP statutes “provide full faith and credit will be given to the provisions of statutes in the state of organization.” Yet, some states “expressly preclude professionals from utilizing” limited liability entities. Thus, concern exists for firms wishing to practice as a limited liability organization in a state that has expressly denied lawyers the right to do so. Without statutory authorization, foreign limited liability entities may face “uncertain common law choice-of-law rules.” Furthermore, the “innocent” law firm members could possibly be subjected to the vicarious liability for which the limited liability organizations was formed to

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109 See W. VA. CODE § 31B-3-303(b) (1996).

110 Taurus Advisory Group v. Sector Management, No. CV 960150830, slip op. at 2 (Conn. Super. Ct. Aug. 29, 1996), available on WESTLAW 1996 WL 502187 (noting that parties appeared to accept “the analogy of a limited liability company to a corporation whereby the members are similar to stockholders” and that “[c]ourts have used this construction with limited liability partnerships...”.)

111 Johnson, supra note 3, at 141.

112 Id.

113 Sheldon I. Banoff, Setting Up a Multistate Professional Practice as an LLC, 2 J. OF LIMITED LIABILITY COMPANIES 66 (Fall 1995). For example, some state statutes prohibit law practice except to the extent of authorization by the licensing authorities.

114 Johnson, supra note 3, at 141-2.

115 Johnson, supra note 3, at 143-4.
avoid.\textsuperscript{116}

Provided the state in which the law firm wishes to practice has recognized the PLLC or LLP, the foreign law firm must register in the foreign state under that state’s requirements.\textsuperscript{117} Failure to register may result in a penalty, but alone, generally would not result in a loss of the liability shield.\textsuperscript{118} Furthermore, the law firm should look beyond the foreign state’s statute authorizing the limited liability organization to ensure that its entity will be recognized by that state’s courts.\textsuperscript{119} A law firm must also review the insurance requirements of the foreign state, because the insurance requirements may vary.\textsuperscript{120}

2. Outside Limited Liability Firms Practicing in West Virginia

a. Limited Liability Companies

Firms organized under foreign limited liability company statutes may apply for a certificate of authority to transact business in the state.\textsuperscript{121} The application, accompanied by a $150 fee\textsuperscript{122} must provide the name of the foreign company;\textsuperscript{123} the name of the state or country of organization;\textsuperscript{124} the street address of its principal place of business;\textsuperscript{125} the address of its initial designated office in West Virginia;\textsuperscript{126} the name and street address of its initial agent for service of process in West Virginia.

\textsuperscript{116} Id. Thus, in the event the shield of limited liability is not upheld by a court, the vicarious liability principles of general partnership law would apply.

\textsuperscript{117} Id.

\textsuperscript{118} See W. VA. CODE § 31B-10-1008 (1996).

\textsuperscript{119} See generally Ballantine and Rutledge, \textit{Kentucky Supreme Court Rejects}, supra note 12.

\textsuperscript{120} Banoff, supra note 13 at 70.

\textsuperscript{121} W. VA. CODE § 31B-10-1002(a) (1996).

\textsuperscript{122} Id.

\textsuperscript{123} W. VA. CODE § 31B-10-1002(a)(1) (1996).

\textsuperscript{124} W. VA. CODE § 31B-10-1002(a)(2) (1996).

\textsuperscript{125} W. VA. CODE § 31B-10-1002(a)(3) (1996).

\textsuperscript{126} W. VA. CODE § 31B-10-1002(a)(4) (1996).
Virginia;\textsuperscript{127} whether the company is a "term" company;\textsuperscript{128} if the company is manager managed, the names and addresses of each initial manager;\textsuperscript{129} whether the members are to be liable for debts and its obligations under a provision similar to West Virginia Code section 31B-3-303(c).\textsuperscript{130} In addition to the application, the foreign LLC must deliver a certificate of existence or similar record authenticated by the appropriate official of the state of organization.\textsuperscript{131} In addition, foreign PLLCs, must also submit an application to the West Virginia State Bar for prior approval to provide legal services.\textsuperscript{132} In addition to the application requirements, the foreign PLLC must provide a summary of the "procedures and policies which it has in place in order to prevent the unauthorized practice of law in West Virginia by any member, manager, or employee," who is not licensed to practice in West Virginia.\textsuperscript{133} In addition, the foreign PLLC must designate at least one licensed West Virginia attorney who "shall be responsible for compliance" by the PLLC with the West Virginia Rules of Professional Conduct.\textsuperscript{134} The state laws of foreign LLC's organization "govern its organization and internal affairs and the liability of its managers, members, and their transferees."\textsuperscript{135}

b. Limited Liability Partnerships

Prior to conducting business in West Virginia, a foreign registered LLP must comply with statutory and administrative registration which governs the

\textsuperscript{127} W. VA. CODE § 31B-10-1002(a)(5) (1996).

\textsuperscript{128} W. VA. CODE § 31B-10-1002(a)(6) (1996).

\textsuperscript{129} W. VA. CODE § 31B-10-1002(a)(7) (1996).

\textsuperscript{130} W. VA. CODE § 31B-10-1002(a)(8) (1996).

\textsuperscript{131} W. VA. CODE § 31B-10-1002(b) (1996).

\textsuperscript{132} State Bar Rules at ¶ 3.

\textsuperscript{133} State Bar Rules at ¶ 3(e).

\textsuperscript{134} State Bar Rules at ¶ 3(e). The responsible West Virginia attorney must also certify that to the best of his or her knowledge and belief, the foreign PLLC complies with the West Virginia Rules of Professional Conduct and has satisfactory policies and procedures in place to prevent the unauthorized practice of law in West Virginia by any person associated with the company.

\textsuperscript{135} W. VA. CODE § 31B-10-1001(a) (1996).
practice of law. Notice must also be filed with the West Virginia Secretary of State. Further, the name of the foreign registered LLP must contain the words “Registered Limited Liability Partnership” or “LLP,” or “L.L.P.” as the last word of the partnership name. The LLP must also meet the $1,000,000 liability insurance or deposit requirements. Law firms practicing as LLPs need not file any documentation or register with the West Virginia State Bar. The internal affairs of the foreign LLP practicing in West Virginia, including the liability of partners for debts, obligations and liabilities, will be governed by the jurisdiction in which the LLP is registered.

F. Effect of Limited Liability on Firm Culture

The shift from the traditional law firm’s general partnership structure “could have a major impact upon the culture of a law firm.” For example, firm members may need to rethink their compensation structures with limited liability in mind. The practice of law in high risk areas such as regulated industries often yields higher rewards commensurate with the increased risk of liability. Partners now practicing in these areas usually share the risk related gains with their partners who share in the risk. If a shift to a limited liability enterprise causes a firm member to individually shoulder the increased risk of liability, he or she may


137 W. VA. CODE § 47B-10-4(d)(ii) (1996). The application must contain the name of the partnership; the address of its principal place of business; if the principal place of business is located outside West Virginia, the address of a registered office and the name and address of a registered agent for service of process within West Virginia, which the LLP must maintain; any other matters the LLP wishes to include; and a brief statement of the business in which the partnership engages. The notice is valid for two years. Upon the conclusion of two years, the LLP must file a new notice. Id.


140 State Bar Rules at ¶ 2.


142 Johnson, supra note 3, at 139.
demand a higher share of rewards.143

Furthermore, because of the potential liability for supervising attorneys, the question of "[f]airness ... could arise among firm members when some members supervise less experienced lawyers and others do not."144

G. Insurance

Lawyers converting to a new business entity must also examine their firm’s insurance coverage.145 Limited liability provisions generally do not diminish a firm’s need for malpractice insurance.146 In effect, the limited liability provisions would kick in only after the firm’s and the malpracticing lawyer’s assets have been exhausted.147 Thus, a firm organized as a P.C., PLLC, or LLP, still must continue to carry insurance.148 Frequently, insurance carriers require amendments to policies reflecting the firm’s status and name change.149 Furthermore, larger firms “whose arrangements may involve London-based insurance companies,” must ascertain whether by becoming a PLLC or LLP, they would “forgo rights they may have under the United Kingdom’s Policyholders Protection Act.”150

In addition, the insurance policy of an LLP must contain a provision or endorsement where the insurer waives or agrees not to assert as a defense the liability protection afforded by the statute.151 A law firm contemplating changing

143 Johnson, supra note 3, at 139-40 (footnote omitted).

144 Id at 140.


146 Id.

147 Id.

148 Id. In West Virginia, both the PLLC and LLP must carry at least one million dollars in malpractice insurance or place the same amount in a reserve acceptable under the statue. W. VA. CODE § 46B-10-5 (1996).

149 Id. Presumably, this issue affects only a few, if any, West Virginia law firms. It does, however, "represent the type of obscure and perhaps unique, insurance-related question that might not be noted or addressed by many firms in the absence of consultation with their insurance representatives." Id.

150 Id. supra note 145, at 92.

its business organization should consult its insurance carrier prior to the conversion to assure that the obvious and the more technical issues "are addressed in a timely manner."\textsuperscript{152}

V. CRITICISM OF LIMITED LIABILITY\textsuperscript{153}

Critics of limited liability entities for lawyers generally contend that lawyers will be less likely to supervise the work of other lawyers in the firm because the incentive of avoiding unlimited liability for a partner's malpractice no longer exists under the LLP or PLLC.\textsuperscript{154} However, because of the diversification and specialization of lawyers within firms, this theory is somewhat lacking in credibility. For example, one cannot assume that a tax lawyer in a Charleston, West Virginia office, has the expertise, experience, or ability to supervise her partner who is a patent attorney in Washington, D.C., and vice versa. Under traditional partnership law, the Charleston partner would be jointly and severally liable for the torts committed by the Washington partner.\textsuperscript{155} Furthermore, proponents argue that lawyers in a limited liability organization will not decrease the amount of monitoring because of a desire to protect their financial interests and their reputations as well as the possibility of higher malpractice insurance premiums.\textsuperscript{156}

VI. CONCLUSION

Although the imposition of vicarious personal liability could occur even if the law firm is organized as a limited liability entity, law firms must be aware that as a general partnership, the liable law firm has no argument against the imposition of vicarious personal liability. As a PLLC or LLP, the law firm at the very least has support against the imposition of vicarious liability. As a result, lawyers should consider changing the organizational form of their law practice to one of the limited liability entities created by the West Virginia Legislature. Although the process by which firms may convert to a limited liability organization is relatively easy, the lawyer must consider the potential ramifications and areas of concern prior to making such a change. Perhaps, a balancing test between the law firm's desire to

\textsuperscript{152} See generally Christophe, supra note 145.

\textsuperscript{153} For a complete discussion of criticism of limiting lawyer liability, see Murphy, supra note 5, at 201.

\textsuperscript{154} Murphy, supra note 5, at 216-17.

\textsuperscript{155} See generally Rosencrantz, supra note 1, at 370.

\textsuperscript{156} Id. at 376.
limit personal liability for the firm’s obligations and the potential ramifications of the change in organization would be appropriate. Larger firms organized as partnerships should not be misguided by the argument that changing to a limited liability organization will decrease the amount of supervision given to other lawyers within the firm. Quality consciousness and client demand for quality work product should ensure adequate supervision.

In choosing between which limited liability organization best fits each particular firm, lawyers must consider the potential tax ramifications, client concerns, the potential change in the firm culture, as well as the other factors noted herein. Moreover, firms involved in a multi-state practice or firms that plan to cross state lines must be aware of potential conflicts of law and of the possibility that members of the firm may not be shielded from personal liability in the foreign state.

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