

***Limited Liability Partnership and Liability Capping
Legislation for the Practice of Law in Selected Places***

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Executive Summary

Nature of limited liability partnership and liability capping legislation

1. A limited liability partnership (LLP) is a vehicle for doing business, combining the limited liability feature of a limited company and the flexibility of the internal organization of a general partnership. LLPs of both the United Kingdom (UK) and the State of New York (NY) in the United States render the privilege of limited liability to the innocent members/partners, so as to insulate their personal assets from claims incurred by the faults of other members/partners.
2. The Professional Standards Act 1994 of New South Wales (NSW) is the first liability capping legislation in Australia. It enables occupational associations to establish their own professional standards schemes, requiring members to insure and implement strategies for the protection of the parties concerned in exchange for their liability capped at a specified level. The cap is to provide "*some guarantee of payment for the vast majority of claimants*".

Eligibility

3. The LLP option is open to all types of business in the UK, whilst, in NY, the LLP structure is limited to around 40 licensed professionals. The liability capping option in NSW is limited to members of the occupational associations which have set up their own professional standards schemes, including the Solicitors Professional Standards Scheme (Solicitors Scheme).
4. In both the UK and NY, a solicitors' LLP must be owned and run by lawyers. The Law Society of England and Wales further requires that a legal practice, before rendering services through an LLP, must obtain its recognition as a recognized body and have at least one member who is "*qualified to supervise*".

Liability

5. In both the UK and NY, an LLP is liable for the wrongful acts and omission of its members/partners to the same extent as the members/partners so acting in the ordinary course of the business of the LLP.
6. The statutes in both the UK and NY provides that members/partners of an LLP are liable for their own faults, but not for each other's acts or omissions solely by virtue of being a member/partner of that LLP.
7. The liability capping legislation of NSW gives a blanket cover to the professionals under their respective professional standards schemes, no matter whether they have personal involvement in the wrongful act or not. Under the Solicitors Scheme, the maximum liability for each claim depends on the number of principals in the legal practice.

8. The NY Partnership Law expressly provides a full shield for the innocent partners of an LLP, so that they are not liable directly or indirectly (by way of contribution and indemnification) for any liability, whether arising in tort or contract. The UK LLP Act has no provision on whether innocent members of an LLP may be liable indirectly by contribution to make good losses of working capital after the LLP has satisfied a claim out of the LLP's capital.
9. Upon the winding up of an LLP, the members/partners of an LLP in both the UK and NY are not obliged to contribute anything when the liquidator seeks contribution to enforce third party claims.
10. The Partnership Law of NY provides that a partner of an LLP is personally and fully liable for any wrongful act committed by any person under his or her "*direct supervision and control*". Both the UK LLP Act and the NSW liability capping legislation have no provision on this issue.

Safeguards

11. In both the UK and NY, there is no compulsory insurance requirement in their respective LLP statutes. In contrast, the NSW Professional Standards Act 1994 requires professionals to hold insurance against occupational liability under each professional standards scheme and the insurance policy must comply with standards determined by the occupational association concerned.
12. The Law Society of England and Wales requires that a solicitors' LLP must have compulsory top-up insurance apart from the minimum qualifying insurance, considering that clients or third parties may have limited assets against which to claim. The Solicitors Scheme of NSW requires that a solicitor must have the benefit of insurance for an amount not less than his or her limited liability. The NY State Bar Association does not have any compulsory insurance requirement.
13. In the UK, a large number of provisions of the company and insolvency law apply to LLPs, so as to preserve the LLP assets which can be claimed by third parties and to disclose sufficient information for third parties to assess the risk they assume in dealing with LLPs. The safeguards imposed by the NY statutes emphasize the disclosure element, and have no measure to preserve the LLP assets. NSW promotes greater self-regulation through the complaints system and risk management, in order to improve the standard of professional services and protect the interests of the public.
14. The UK is the only place studied which may require an LLP member to pay back the withdrawals made during the two years prior to the commencement of winding up, if it is proved that the member knew or believed that the LLP was, or would be unable to pay its debts.
15. While both the UK and NY statutes require an LLP to submit regular reports of non-financial information, only the UK requires an annual report on financial information to be filed and applies the accounting and auditing requirements for companies to LLPs, including solicitors' LLPs.

16. Both the UK and NY statutes require that the name of an LLP must reveal its limited liability status. The NY law requires that an LLP has to publish a notice of its registration in two newspapers. The Professional Standards Act 1994 of NSW requires a person whose occupational liability is capped to notify that fact on all documents given to a client or prospective client.
17. In the UK, the Law Society of England and Wales requires that where a law firm converts from a partnership to an LLP, it has to notify its clients, either before the change or soon afterwards. In NY, there is no duty for a law firm to inform its clients about the change in liability status, although it is customary to do so.

Limited Liability Partnership and Liability Capping Legislation for the Practice of Law in Selected Places

Chapter 1 - Introduction

1.1 Background

1.1.1 The Panel on Administration of Justice and Legal Services of the Legislative Council (LegCo), at its meeting on 22 November 2004, requested the Research and Library Services Division (RLSD) to conduct a research on the forms of business structures to limit liability for the practice of law in selected places.

1.1.2 The Panel agreed that the research should examine the operation of limited liability partnerships (LLPs) and the safeguards to protect the parties concerned and members of the public.

1.2 Scope of research

1.2.1 Some places have the formation of LLPs restricted to professional services, whilst some have LLPs open to all types of business. The State of New York (NY) of the United States (US), being one of the former, restricts the adoption of LLPs to licensed professionals, including lawyers. On the other hand, the business structure of LLPs is available to all types of business in the United Kingdom (UK) when Parliament passed the LLP statute in 2000 for England, Wales and Scotland. In Australia, some states have adopted legislation capping liability for professionals. The State of New South Wales (NSW) was the first state in Australia to introduce such legislation in 1994. The legislation enables occupational associations to establish their own professional standards scheme, requiring members to insure and implement strategies for the protection of the parties concerned in exchange for capped liability.¹

1.2.2 This research studies how solicitors limit their liability through LLPs or professional standards schemes in the following places:

- (a) England and Wales of the UK;
- (b) NY of the US; and
- (c) NSW of Australia.

¹ The Law Society of New South Wales set up its professional standards scheme in 1996.

1.2.3 The selected places are examined in the following aspects:

- (a) background of the adoption of LLPs/liability capping legislation;
- (b) nature of LLPs;
- (c) eligibility and applicability;
- (d) scope of liability limitation; and
- (e) regulation and safeguards to protect the interests of the parties concerned and members of the public.

1.2.4 This report explores the general rules and conditions of the operation of LLPs/professional standards schemes, which are applicable to both solicitors and other professionals, and studies the specific rules, if any, applicable to solicitors only.

1.3 Methodology

1.3.1 This research adopts a desk research method, which involves Internet research, literature review and analysis, and correspondence with the relevant authorities in the places studied.

Chapter 2 - Basic Concepts

2.1 Business structures and liabilities of members

General partnership

2.1.1 A partnership is a relationship which subsists between persons carrying on a business in common with a view to profit. Unlike an incorporated company, a partnership has no legal personality of its own. In the eyes of the law, a partnership is just a way of describing the individual partners who make up the partnership.

2.1.2 A form of partnership is a general partnership in which two or more co-owners engage in business for profit, with each partner having unlimited personal liability for losses. In a general partnership, a partner is not only liable for the liabilities caused by his or her own actions, but also jointly and severally liable for the liabilities incurred by other partners. In other words, a partner is liable jointly with his or her co-partners and also severally for all the liabilities of the general partnership. If a claim is made and substantiated, a partner is liable to meet the claim in full irrespective of his proportion of personal responsibility, and his or her personal assets will be at risk when the assets of the partnership or professional indemnity insurance, if any, are not sufficient to cover those liabilities.

2.1.3 General partnership is regarded by the public as the type of business structure providing the optimal protection to members of the public, because partners are not protected by limited liability and the claimants can always go after the personal assets of each partner to meet his or her claim.

2.1.4 The characteristic of "*unlimited liability*" ensures that the partners maintain a direct interest in the affairs of the partnership and conduct of its partners, especially in small practices where the partners are likely to work in the same location. For large practices, they may have offices in several places, and thus partners may not be able to keep track of all aspects and transactions of the partnership. Nonetheless, under a general partnership, partners still have to share the liabilities for the negligence of those partners whom they may barely know or meet.

2.1.5 The advantage of the partnership structure is that the business affairs of a partnership are entirely private. Although legislation may provide a set of default provisions for partnerships, partnership agreements can always be drawn up to override the default provisions. A partnership agreement is a private confidential document providing the flexibility in which the partners can determine how the internal structure and relationship between partners and between partners and the partnership are governed. In addition, there is no obligation to register financial or membership information at a public registry.

Limited partnership

2.1.6 A limited partnership consists of general partners, who are fully liable for partnership liabilities, and limited partners whose liability of contributing capital is limited to the amount of financial contribution, provided that they do not take part in the management of the business.

Limited liability partnership

2.1.7 A limited liability partnership (LLP) is a hybrid of a partnership and a company. Some places have LLPs more in common with a company, while LLPs in some other places contain features more in line with general partnerships.

2.1.8 A feature common for LLPs in various places is that they offer a vehicle for doing business with limited liability for members of the firm and an internal organization based on that of partnership rather than companies.² In essence, the partners are not liable to any liabilities solely by reason of being an LLP partner and hence their personal assets are protected from creditors of the LLP. However, they remain personally liable for their own negligence and wrongdoing. Two other common features are that LLPs have to register according to the statutory requirements and the LLP status must be notified to the general public.

2.1.9 The detailed features of LLPs in various places differ substantially in legal form, in the types of business allowed to be conducted under LLPs, and in the extent and nature of safeguards provided to clients and other parties dealing with LLPs.

2.1.10 Broadly speaking, LLPs are provided with more safeguards than general partnerships to protect the interests of clients and relevant third parties. Some of these safeguards are similar to those required of limited companies. However, LLPs are not bound by those aspects of company legislation which are related to the separation of ownership and management.

2.1.11 An LLP is different from a company in a number of ways:

- (a) it does not have shares or shareholders;
- (b) it has members/partners (members for LLPs in the UK and partners in the US) but not directors, and there is no separation of ownership and management;
- (c) it has neither share capital nor capital maintenance requirements;

² Department of Trade and Industry, the United Kingdom. (1997).

- (d) it does not have a memorandum and articles which are public documents governing the key facts of the company and the mutual relationship between the members/partners and the company; and
- (e) the agreement governing the mutual rights and duties between the members/partners, and between the members/partners and the LLP is a purely private document.

2.1.12 There are concerns about the shifting of the business structure of a firm from a general partnership to an LLP, albeit there is no empirical data supporting them. One of the concerns is about the impact upon the culture of a law firm.³ For instance, the practice of law in high risk areas often yields high rewards commensurate with the increased risk of liability. Partners in a general partnership usually share both the risk and risk-related gains with their fellow partners. If a shift to an LLP causes a member/partner to shoulder a higher risk of liability than others, he or she may demand a larger share of the rewards. Similarly, the risk of some members/partners may increase where the legislation provides that members/partners of LLPs have to be liable for the acts of those under their direct supervision; in particular, if some members/partners have to supervise less experienced lawyers or staff.

2.1.13 Some consider that shifting from the general partnership status to the LLP status may result in less incentive for members/partners to monitor and control the quality of work by other members/partners of the firm, as they are no longer liable for the acts of their fellow members/partners. The breakdown of internal procedures at Arthur Andersen, the accounting firm operating as an LLP, in connection with the collapse of the Enron Corporation, is often quoted as an example of such disincentive.⁴

Limited liability company

2.1.14 A limited liability company (LLC) is a business structure available in the US, but not in the UK. LLCs have different attributes according to the statutes of the respective states. For instance, in California and New Mexico, lawyers are not allowed to operate as LLCs.

³ Johnson, J. (1995).

⁴ Hamilton, Robert W. and Macey, Jonathan R. (2003).

2.1.15 The owner of an interest in an LLC is known as a member. Although LLC has the word "*company*" in its name, unlike a company, an LLC does not issue shares of stock, and is taxed as a partnership.

2.1.16 The main differences between LLPs and LLCs lie in the scope of liability limitation and the performance of the management function. Members of LLCs are protected from all types of liabilities except for those incurred by their own faults. In some states of the US, LLPs offer the same protection as LLCs; however, in others, partners of LLPs are only protected from tort liabilities of other partners, but not from other types of liabilities. In most states, members of LLCs can either designate managers or act as management themselves, while partners of LLPs always manage the business themselves. LLCs are formed by filing Articles of Organization or a similar document to the secretary of state in the respective state, whilst the partnership agreement of LLPs is a private document.

2.1.17 In NY, a single professional is allowed to register as a professional service LLC, whilst the LLP structure requires a minimum of two partners. If a law firm which practises as a partnership wishes to convert into a professional service LLC, it has to create a new entity and would no longer be subject to partnership law.

Professional corporation

2.1.18 Professional corporation is another business structure available in all states of the US. The laws governing whether a professional corporation provides for limited liability vary from state to state. In NY, members of a professional service corporation enjoy the advantage of limited liability, but they are still liable for the consequences of their own negligence and wrongdoings, and for those wrongdoings committed by staff and other members under their direct supervision and control. Similar to an LLC, if a law firm which practises as a partnership wishes to convert into a professional service corporation, it has to create a new entity and would no longer be subject to partnership law. A professional service corporation is taxed like a corporation, not as a partnership.

2.1.19 In NSW, solicitors are allowed to render legal services through incorporated legal practices, which are similar to professional corporations in the US. An incorporated legal practice must have at least one solicitor director on its board of directors. Members in an incorporated legal practice have the protection of limited liability. However, incorporated legal practices are required to make contributions to the solicitors' Fidelity Fund and to pay premiums for professional indemnity insurance in the same way as solicitors operating through other types of business structures.

Chapter 3 - The United Kingdom

3.1 Background

Emergence of limited liability partnership in the United Kingdom

3.1.1 In the UK, most professional firms are structured as partnerships. In a general partnership, partners are personally liable for all the business obligations of the partnership. Prior to the mid-1990s, some of the professions, especially the accountants, lobbied for some time to have the law on liability changed against a background of substantial claims for professional negligence.

3.1.2 Two large accountancy firms, assisted by a law firm, began steps to obtain a limited liability partnership (LLP) statute in Jersey⁵, which received Royal Assent in November 1996. *"By mid-1996 it was plain that the option of offshore registration as a Jersey LLP was being very seriously considered by a number of very large professional partnerships. It was this prospect, combined with the perceived possibility that a successful mega-claim could in due course precipitate the failure of a major firm, that led to the November 1996 decision⁶...to bring forward LLP legislation in the UK."*⁷

3.1.3 The announcement of the government's intention to introduce LLP legislation was followed by a consultation paper issued by the Department of Trade and Industry in February 1997, offering firms the ability to incorporate with limited liability whilst retaining the organizational flexibility of a partnership. A draft of the Limited Liability Partnerships Bill and the related regulations was published in 1998⁸ for further consultation.

3.1.4 The government, in its 1997 and 1998 consultation papers, stated that the objective of introducing the LLP legislation was to add to the choice of legal organizations available to businesses in Great Britain and to keep the legal framework for businesses in Great Britain up to date with good international practice. The government emphasized that LLP legislation would allow Great Britain registered firms to operate competitively with their overseas counterparts.⁹

⁵ Jersey is a parliamentary democracy and a dependency of the British Crown. It is not part of the United Kingdom, nor is it a colony. Her Majesty Queen Elizabeth II of the UK is the Head of State of Jersey. The Sovereign is represented in the Island by the Lieutenant Governor. While Jersey makes its own laws, it has pledged allegiance to the English Crown since 1066.

⁶ On 7 November 1996, Ian Lang, President of the Board of Trade, announced the UK government's intention to bring forward legislation at the earliest opportunity to make LLP available to regulated professions in the UK.

⁷ House of Commons Select Committee on Trade and Industry Report 1998. H.C. 59, para.82.

⁸ Department of Trade and Industry. (1998).

⁹ Department of Trade and Industry. (1999).

3.1.5 There were opinions opposing limiting liability for professionals. For instance, a member of the House of Lords, Lord Phillips of Sudbury, considered that the Limited Liability Partnerships Bill was unnecessary. As a practising solicitor, he opined that joint and several unlimited liability was a powerful incentive to probity among professionals. He noted that most of the input into the Bill had come from the large firms which supported the measure, but that the consumer voice had been under represented.¹⁰

3.1.6 The Limited Liability Partnerships Act 2000 (LLPs Act) was approved by Parliament on 28 June 2000. The LLPs Act and the Limited Liability Partnerships Regulations 2001 (LLPs Regulations) came into force on 6 April 2001.

Definition and nature of limited liability partnership in England and Wales

3.1.7 An LLP is a body corporate with legal personality separate from that of its members.¹¹ It is incorporated by registration with the Registrar of Companies in England and Wales under the LLPs Act. The LLP form is available to any two persons or more who carry on a lawful business with a view to profit¹².

3.1.8 It is a form of business structure combining features of a partnership and a limited company in the UK. The LLP structure offers an option for businesses to incorporate with limited liability whilst enabling them to organize themselves in a flexible manner as partnerships. Agreements between the members, and between the members and the LLP, which are confidential and not prescribed by statute¹³, govern their mutual relationships and the operation of the LLP¹⁴. An LLP is treated for tax purposes as a partnership.

3.1.9 An LLP has members rather than partners, and partnership law, generally speaking, does not apply to an LLP.¹⁵

3.1.10 Except for organizational flexibility and taxation, an LLP has more in common with a company. Its members have the privilege of limited liability. Substantial provisions of the company and insolvency laws are applicable to LLPs and protect those parties who have dealings with an LLP. In essence, the disclosure and winding up safeguards for LLPs are at least up to the level required for limited companies.

¹⁰ House of Lords Debate. Hansard 9 December 1999 cc 1432-34.

¹¹ Section 1(1) of the LLPs Act 2000.

¹² Section 1(a) of the LLPs Act 2000.

¹³ If no partnership agreement is formed, there are default rules governing the rights and duties between an LLP and its members and the members inter se under Regulation 7 of the LLPs Regulations 2001.

¹⁴ Section 5 of the LLPs Act 2000.

¹⁵ Section 1(5) of the LLPs Act 2000.

Procedures for setting up limited liability partnership

3.1.11 An LLP must become incorporated by registration with the Registrar of Companies. Before a legal practice can operate through an LLP, the LLP must obtain recognition from the Law Society of England and Wales (Law Society) as a recognized body.¹⁶

Statutory requirements

3.1.12 To incorporate as an LLP, one needs to send a prescribed form, together with the registration fee, to the Registrar of Companies. The form sets out the name of the LLP; where the registered office of the LLP is to be situated; the address of the registered office; the name, full address and date of birth of each member of the LLP; and the names of at least two designated members (a position similar to a company secretary who is given certain formal and administrative responsibilities) or that all members are designated members. All members must sign the form. In addition, one of the proposed members or a solicitor who is not a proposed member must sign a statement of compliance that the two or more persons named in the prescribed form are associated for carrying on a lawful business with a view to profit.

Law Society of England and Wales' rules

3.1.13 Under the Solicitors' Act 1974 and the Solicitors' Incorporated Practice Rules 2004, a solicitors' LLP must not commence practice before it has become a recognized body. If it violates such regulation, all members of the LLP would commit a criminal offence.¹⁷ A recognized body is an LLP (or a company) which the Law Society has recognized¹⁸ as being a suitable body to provide "*professional services such as are provided by individuals practising as solicitors or lawyers of other jurisdictions*".

3.1.14 A recognized body must comply with the principles and requirements of solicitors' professional conduct and the Solicitors' Incorporated Practice Rules 2004, and as far as possible ensure that its members (in the case of LLPs) comply with the membership requirements set out in the Rules. A member of an LLP must take reasonable steps to ensure that the LLP complies with the Rules.

3.1.15 The Law Society may, by discretion, refuse an application if:

- (a) it is not satisfied that a member of an LLP is a suitable person to be engaged in the direction or ownership of an LLP; or

¹⁶ The Solicitors Act 1974 and the Administration of Justice Act 1985 have been amended to allow solicitors to form LLPs.

¹⁷ Sections 20-24 of the Solicitors Act 1974.

¹⁸ Section 9 of the Administration of Justice Act 1985 and the Solicitors' Incorporated Practice Rules 2004.

- (b) the Law Society considers that it is proper in the public interest not to recognize the body.

3.2 Eligibility

Access to use the limited liability partnership structure

3.2.1 The LLP structure is open to all types of business in the UK, although in the original proposal, only members of a regulated profession were allowed to set up LLPs, with the view that professional regulation would help safeguard the interests of those parties dealing with the firm.¹⁹

3.2.2 Over two-thirds of the respondents objected to the restricted access proposal,²⁰ mostly on the ground that regulation would be inconsistent with the law relating to companies where no such restriction was in place. It was also argued that it would be unfair for businesses to be excluded from the LLP status to compete with the few businesses which enjoyed a commercial benefit brought by the LLP structure.²¹ The government therefore gave up the restricted access proposal and opened access to the LLP vehicle to two or more persons carrying on any trade or profession.

Use of limited liability partnership and other business structures by legal practices

3.2.3 In the UK, lawyers can practise as sole practitioners, or through general and limited partnerships, companies (both limited and unlimited companies)²² or LLPs. According to the Law Society, there were 215 legal practices operating through LLPs as at 1 January 2005. The rest of legal practices comprised 4 226 sole practitioners, 5 284 partnerships²³, 540 limited companies and 30 unlimited companies. Most of the companies are just ancillary companies owned by mainstream practices to serve as executor and trustee companies, nominee companies or company secretarial companies.

¹⁹ Department of Trade and Industry. (1997).

²⁰ In September 1998, a draft Bill and draft regulations were published for consultation. Over 80 responses were received. The responses were published in Department of Trade and Industry. (1999).

²¹ Department of Trade and Industry. (1998).

²² Law firms have been permitted to practise through limited and unlimited companies as from 1 January 1992 by virtue of the Administration of Justice Act 1985 and the Solicitors' Incorporated Practice Rules 2004.

²³ LLPs formed in the US were classified as general partnerships in the figures as the Law Society was of the view that they did not have separate legal personality and thus treated them accordingly under the Law Society's rules. California LLPs have separate legal personality but it is illegal for them to carry on solicitors' practice in England and Wales.

Use of limited liability partnership by other professions and businesses

3.2.4 There were 7 056 LLPs registered in England and Wales as at 31 March 2004, but the number of effective LLPs stood at 5 279 after deducting those registered LLPs that were either in liquidation or on the path to dissolution.²⁴ The average number of members per LLP was approximately four, although there were some LLPs with over 200 members.²⁵

3.2.5 If the rules of a profession prevent its members from carrying on a business as employees or members of a corporation, then an LLP business formed by them will not be lawful and the Registrar of Companies will refuse its registration.²⁶ For instance, a barrister in private practice cannot be a member of a firm or be employed or engaged by any company to provide legal services directly or indirectly to the public. Therefore, he or she cannot be a member of an LLP which provides legal services.

3.2.6 Professionals, such as accountants, architects, pharmacists and doctors, are allowed to operate through LLPs. Some professionals are required to satisfy certain conditions set by their professional bodies to do so. For instance, architects who practise through LLPs have to register with the Architects' Registration Board.

Statutory requirements for setting up limited liability partnership

Eligibility

3.2.7 Members of an LLP can be an individual, another LLP, or a company but not a limited partnership or a general partnership. An LLP must notify the Companies House for any changes to its membership and its members' residential addresses. There must be at least two or more members to incorporate an LLP.

Disqualification of members

3.2.8 Part III of the LLPs Regulations applies the provisions of the Company Directors Disqualification Act 1986 (CDDA) to LLPs with appropriate modifications. Accordingly, members of LLPs are subject to the same disqualifications and penalties currently applicable to company directors.

3.2.9 Under CDDA, undischarged bankrupts are automatically disqualified from acting as members of an LLP, without the leave of the court. CDDA also grants the court power to issue a disqualification order against a person so that the person shall not, without the leave of the court, be a member of an LLP, for a specified period. A register of disqualification orders is open for public inspection at the Companies House.

²⁴ Department of Trade and Industry. (various years).

²⁵ Reply from Companies House.

²⁶ Blackett-Ord. (2002).

3.2.10 Section 6 of CDDA provides the court with the power to issue a mandatory disqualification order against a person who is or has been a member of an LLP which has become insolvent (whether while he was a director or subsequently) and that his or her conduct as a member of that LLP makes him or her "*unfit to be concerned in the management of that LLP*". Unfitness may be reflected by dishonest conduct or by conduct which is highly incompetent. The minimum period of disqualification is two years and the maximum is 15 years. Most of the disqualification orders have been made by a mandatory order.

3.2.11 There are other grounds where the court has discretionary power to issue a disqualification order²⁷, for instance, the conviction of a person of an indictable offence in connection with the promotion, formation, management, liquidation or striking off of an LLP. However, these grounds are of limited significance since only a small fraction of disqualification orders have been issued based on these grounds.

3.2.12 If a person acts in contravention of a disqualification order, he or she is guilty of a criminal offence and is liable to imprisonment or a fine or both.²⁸ He or she will further be personally liable for all the relevant debts of the LLP, which incurred at a time when he or she was acting in contravention of a disqualification order.²⁹

Law Society of England and Wales' rules for practising through limited liability partnership

3.2.13 Under the Solicitors' Incorporated Practice Rules 2004, an LLP must be owned and run by lawyers. Members of an LLP can be individual solicitors with a practising certificate or European/foreign lawyers permitted to practise under the Law Society's rules. In addition, a member can also be a company/LLP which is a recognized body and has at least one director/member who is a solicitor or a registered European lawyer³⁰ (REL).³¹

3.2.14 An LLP must also have at least one member who is "*qualified to supervise*"³², and supervision refers to "*the professional overseeing of staff and the professional overseeing of clients' matters*"³³.

²⁷ Sections 2-4, 8,9,11 of CDDA.

²⁸ Section 13 of CDDA.

²⁹ Section 15 of CDDA.

³⁰ An REL is a European Union lawyer of European nationality based in the UK. An REL is registered with the Law Society and has the right to practise in the UK on a permanent basis, i.e. with the UK as his or her normal place of work, under his or her home state professional title. An REL has in general the same rights and obligations as UK solicitors except that he or she can only appear as advocate in the higher courts provided that he or she is instructed together with a solicitor qualified to do that work or with a barrister.

³¹ Rule 13(1) of the Solicitors' Incorporated Practice Rules 2004.

³² Rule 13(2) of the Solicitors' Practice Rules 1990.

³³ Rule 13 of the Solicitors' Practice Rules 1990.

3.2.15 A member who is "qualified to supervise" can be either a solicitor or an REL who has held practising certificates for at least 36 months within the last ten years, and has completed the management training specified by the Law Society, or a recognized body which is a company/LLP with such a solicitor/REL.³⁴

3.3 Scope of liability limitation

3.3.1 The LLPs Act does not deal explicitly with the issue of liability of an LLP and its members. It is the existence of an LLP as a separate legal person from its members under section 1 of the LLPs Act, which is the key to the separation of individual liability from the liability of the LLP.

Liability of limited liability partnership

3.3.2 An LLP has a legal personality of its own. Each member of an LLP is an agent of the LLP³⁵, and therefore the LLP is bound by the actions of its members. In other words, the LLP is liable for the wrongful acts and omission of its members to the same extent as the members so acting.³⁶ However, an LLP is not bound where a member acts beyond his or her authority and the third party knows that he or she has no authority to act, or the third party does not know or believe him or her to be a member of the LLP.³⁷

3.3.3 It is open to the LLP to limit its liability by agreement with a client, but "The Guide to the Professional Conduct of Solicitors (1999)" prohibits limitation of the LLP's liability below the compulsory minimum level of insurance cover under the indemnity rules, i.e. currently £1 million (HK\$14.27 million) per claim.

Liability of individual members

Liability for other members' wrongdoings

3.3.4 The LLPs Act does not expressly confer limited liability upon the members of LLPs. As an LLP is a separate legal person from its members, the normal laws of obligations (i.e. legal duty) confine liability to the LLP itself and separate the individual liability of the members from the liability of the LLP. Individual members are not liable for each other's acts simply by virtue of being a member of the LLP.

³⁴ If the practice does not exercise or assume responsibility for any right of audience, a Registered Foreign Lawyer (RFL) who has practised as a lawyer for at least 36 months within the last 10 years and has completed the management training specified by the Law Society is also qualified to supervise.

³⁵ Section 6(1) of the LLPs Act.

³⁶ Section 6(4) of the LLPs Act.

³⁷ Section 6(2) of the LLPs Act.

3.3.5 In addition, the law relating to partnership does not apply to an LLP, and, therefore, a member of an LLP is not in general liable in contract or tort, by virtue of being a member of the LLP, for acts of his or her fellow members.

3.3.6 Members of an LLP are not liable for the debts and obligations of the LLP subject to certain statutory qualifications, particularly sections 214 and 214A of the Insolvency Act 1986. Section 214 provides that if an LLP has continued trading when a member of that LLP previously knew or ought to know that it had no reasonable prospect to avoid going into liquidation, the liquidator may apply for a court order to declare that the LLP member has to make contribution to cover the debts or obligations concerned³⁸. Section 214A provides that, on the application of the liquidator, withdrawals made by a member of an LLP may be subject to clawback if it is proved that at the time of the withdrawal, the member knew or had reasonable grounds for believing that the LLP was, or would be unable to pay its debts.

3.3.7 If an LLP is left with only one member for more than six months, it may be wound up by the court³⁹ and the limited liability status will be lost.⁴⁰

Indirect liability by contribution

3.3.8 Whilst members of an LLP are protected from direct liability not arising from their own faults, they may still bear liability in an indirect way. After an LLP has satisfied a claim out of its assets, the capital accounts of all the individual members would be reduced. The LLP legislation has no provision on whether innocent members of that LLP may be compelled to contribute to make good losses of capital. While the payments to cover the shortfalls are technically "*contributions*", they are nevertheless indirect payments to satisfy a claim. The issue of the obligation of members to contribute working capital to an LLP is to be regulated by the agreement reached among the members.⁴¹

Liability for one's own wrongdoings

3.3.9 Members of an LLP are not protected from liability incurred in their own right, either in contract or in tort.

³⁸ However, the court should not make such a declaration if it is satisfied that the person took every step with a view to minimizing the potential loss to the LLP's creditors as he ought to have taken.

³⁹ Section 122 of the Insolvency Act 1986 as amended by Schedule 3 of the LLPs Regulations.

⁴⁰ Section 24 of the Companies Act 1985, as applied by the LLPs Regulations.

⁴¹ Morse, G. et al. (ed.) (2002).

Liability for supervision

3.3.10 Although the LLPs Act does not provide that a member of an LLP is liable for the negligent or wrongful act committed by any person under his or her direct supervision, the Law Society states⁴² that it would be dangerous to assume that the LLP status protects solicitors from the consequences of "*negligent supervision*". The Law Society explains that it depends on the circumstances and whether a duty of care and actual negligence can be demonstrated.

Liability in the winding up of limited liability partnership

3.3.11 Unlike a partner in a partnership, members of an LLP are not obliged to contribute anything upon its winding up when the liquidator seeks contribution to enforce third party claims, apart from two main exceptions.

3.3.12 Firstly, the LLPs Regulations apply a new version of section 74 of the Insolvency Act to LLPs. In the event of an LLP being wound up, past and present members contribute to the assets of the LLP only to the extent that they have agreed with other members or with the LLP. However, they are not obliged to agree to contribute anything. Secondly, on the application of the liquidator, withdrawals of the LLP's properties made by the members during the two years prior to the commencement of winding up may be subject to clawback, if it is proved that at the time of the withdrawal, the members knew or had reasonable grounds for believing that the LLP was, or would be unable to pay its debts.

3.4 Safeguards

3.4.1 A large number of provisions of the Companies Act 1985 and the Insolvency Act 1986 are applicable to LLPs with modifications, with the intention of retaining equality in general between the way directors of companies and members of LLPs are treated.

Insurance

Statutory requirements

3.4.2 A proposal of a minimum bond or compulsory insurance requirement was raised in the consultation paper⁴³, but was rejected in that the government considered it difficult to specify a sum which would provide a sufficient guarantee for creditors without turning it to be a disincentive to firms considering the LLP option.

⁴² The Law Society of England and Wales. (1999).

⁴³ Department of Trade and Industry. (1997). For instance, every Jersey LLP is required to have in place a £5 million (HK\$71.35 million) financial provision by a bank or insurance company. If the provision is not available on winding up, the partners would be liable to the full extent of their assets in the event of an insolvency.

Law Society of England and Wales' rules

3.4.3 Before a law firm applies to the Law Society to obtain recognition as a recognized body, it must arrange to have a £1 million (HK\$ 14.27 million) minimum qualifying insurance for the LLP under rule 4 of the Solicitors' Indemnity Insurance Rules. The amount required is the same for general partnerships. The compulsory insurance covers not only the LLP itself, but also its members, employees and consultants. The minimum qualifying insurance must be provided by a qualifying insurer⁴⁴.

3.4.4 In addition to the qualifying insurance, all LLPs and limited companies must have compulsory top-up insurance to protect their clients or third parties from having too few assets against which to claim.⁴⁵ The top-up insurance must be a minimum of £500,000 (HK\$7,135,000) per claim or £2 million (HK\$28.54 million) per year on an aggregate basis. The amount of top-up insurance for LLPs is the same as that for law firms operating through limited companies. The top-up insurance must be arranged before one can apply for the LLP recognition.

3.4.5 For law firms in other forms of business structures, the top up cover is purely voluntary. According to the Law Society, large law firms, regardless of their business structures, all have vast top-up cover on a purely voluntary basis.

3.4.6 Apart from insurance, an LLP is required to pay a Compensation Fund⁴⁶ contribution on first recognition as a recognized body and every three years thereafter, when recognition is renewed. The contribution is currently £400 (HK\$5,708). Solicitor members and REL members of an LLP must also pay an annual Compensation Fund contribution when applying for their practising certificates on a yearly basis.⁴⁷ The Compensation Fund provides assistance to clients who have suffered financial loss as a result of a solicitor's dishonesty or who are suffering hardship as a result of a solicitor's failure to account for money he or she has received,⁴⁸ but does not pay for any loss arisen from the negligence of a solicitor. The grant made is normally not more than £1 million (HK\$14.27 million).

⁴⁴ A "qualifying insurer" means any authorized insurer which has entered into an agreement with the Law Society to meet the minimum terms and conditions set by the Law Society. For instance, there must be no avoidance of the policy for any reason, including dishonesty or non-payment of the premium (although there may be a right of recovery against the insured).

⁴⁵ Appendix 5 of the Solicitors' Indemnity Insurance Rules.

⁴⁶ The Compensation Fund is maintained pursuant to section 36 of the Solicitors Act 1974.

⁴⁷ RFL members of an LLP have to pay as well but the level depends on whether the RFLs are based in England and Wales or overseas.

⁴⁸ The application must be made within six months after the loss was or should have been discovered.

Disclosure of limited liability status

Statutory requirements

3.4.7 The Companies Act 1985⁴⁹ requires an LLP to paint or affix its name on the outside of every office or place in which its business is carried on, in a conspicuous position and in letters reasonably legible.

3.4.8 The name of an LLP must comply with Part I of the Schedule of the LLPs Act. The name of an LLP must end with the expression "*limited liability partnership*", or the abbreviation "*llp*" or "*LLP*". If an LLP has a registered office in Wales, its name must end with the above expression or abbreviation in English or its Welsh equivalent.

3.4.9 Under the Companies Act 1985⁵⁰, an LLP must put its full corporate name on the following:

- (a) business letters;
- (b) notices and other official publications;
- (c) bills of exchange, endorsements, cheques and orders for money or goods; and
- (d) the LLP's bills, invoices, receipts and credit notes.

3.4.10 The Companies Act 1985⁵¹ also requires an LLP to put the following particulars on its business letters and order forms:

- (a) the LLP's registered number;
- (b) the LLP's place of registration;
- (c) the address of the LLP's registered office; and
- (d) the fact that it is an LLP unless this is spelled out in full in the LLP's name.

3.4.11 If an LLP uses a trading name, it must put its full corporate name, the principal place of business and a list of the LLP's members (or, where there are more than 20 members, there should be a statement that the list is open to inspection at the principal place of business) on its business letters and other documents.⁵²

⁴⁹ Section 348 of the Companies Act 1985, as applied by the LLPs Regulations.

⁵⁰ Section 349 of the Companies Act 1985, as applied by the LLPs Regulations.

⁵¹ Section 351 of the Companies Act 1985, as applied by the LLPs Regulations.

⁵² Section 4 of the Business Names Act 1985, as applied by the LLPs Regulations. Other documents include notepapers, orders for goods and services, invoices, receipts and demands for payment.

Law Society of England and Wales' Rules

3.4.12 The name of an LLP must comply with section 1(c) of the Solicitors' Publicity Code 2001, which prohibits the use of a name which is misleading. The LLP must notify the Law Society immediately if it changes its name.

3.4.13 Under section 2 of the Solicitors' Publicity Code 2001, an LLP's notepaper must include the words "*regulated by the Law Society*" and a list of its members or a statement that the list is open to inspection at its office.

3.4.14 In addition, the Law Society requires that where a partnership converts to an LLP, the law firm has to notify its clients for whom the firm is currently acting, or for whom money or documents are being held, either before the change or soon afterwards.⁵³ However, clients' consent is not required for the conversion.

Non-financial reporting*Statutory requirements*

3.4.15 In general, an LLP has to deliver to the Registrar of Companies successive annual returns within 28 days after the anniversary of the incorporation of the LLP. If an LLP fails to deliver an annual return in time, the LLP and its designated members are guilty of an offence and may be fined.

3.4.16 The annual return has to contain the following:

- (a) the address of the registered office of the LLP;
- (b) the names and usual residential addresses of the members of the LLP, and the names of those members who are designated members; and
- (c) if any register of debenture holders is not kept at the registered office of the LLP, the address of the place where it is kept.

Law Society of England and Wales' rules

3.4.17 The Law Society has to be notified of the registered office and practising addresses of the LLP, the names and professional qualifications of all members of the LLP, and all subsequent changes.

⁵³ The Law Society (1999). Principle 3.11.

Financial reporting

3.4.18 Provisions of Part VII of the Companies Act 1985, with appropriate modifications, impose accounting and auditing requirements on LLPs similar to those for limited companies. An LLP has a duty to keep proper accounting records for three years, from the date on which it is formed. The annual accounts, together with a copy of the auditor's report on those accounts, must be sent to every member of the LLP⁵⁴ and must be filed with the Registrar of Companies⁵⁵ so that the accounts are available for public scrutiny.

3.4.19 Qualified small and medium-sized LLPs may deliver abbreviated accounts to the Registrar of Companies.⁵⁶ The requirements of the abbreviated accounts are different between small and medium-sized LLPs.⁵⁷ At least two of the following conditions must be satisfied to be qualified as a small or medium-sized LLP for submitting abbreviated accounts⁵⁸:

Table — Eligibility requirements for delivering abbreviated accounts

	Small-sized LLP	Medium-sized LLP
Annual turnover	£5.6 million net or less (HK\$79.91 million)	£ 22.8 million net or less (HK\$325.36 million)
	£6.72 million gross or less (HK\$95.89 million)	£27.36 million gross or less (HK\$390.43 million)
Balance sheet total	£2.8 million net or less (HK\$39.96 million)	£11.4 million net or less (HK\$162.68 million)
	£3.36 million gross or less (HK\$47.95 million)	£13.68 million gross or less (HK\$195.21 million)
Average number of employees	50 or fewer	250 or fewer

⁵⁴ Section 238(1) of the Companies Act 1985.

⁵⁵ Section 242 of the Companies Act 1985.

⁵⁶ Sections 246 and 246A of the Companies Act 1985.

⁵⁷ The abbreviated accounts of a small-sized LLP must include the abbreviated balance sheet and notes; and a special auditor's report (unless the LLP is also claiming audit exemption). The abbreviated accounts of a medium-sized LLP must include the abbreviated profit and loss account; the full balance sheet; a special auditor's report and notes to the account.

⁵⁸ The web site of Companies House. Available from: <http://www.companies-house.gov.uk>.

3.4.20 The auditing requirement may be exempted if the turnover of an LLP is £5.6 million (HK\$79.91 million) or less and the balance sheet total is £2.8 million (HK\$39.96 million) or less⁵⁹.

3.4.21 An LLP may be fined for not filing LLP documents and the penalties are the same as those for limited companies.⁶⁰ In addition, the designated member of the LLP may also be liable for a fine⁶¹ and may even be disqualified from being a designated member as a result.

Preservation of assets in the course of winding up

3.4.22 The provisions of the Insolvency Act 1986 apply to LLPs through the LLPs Regulations in the same way as for companies. In addition, a new "clawback" provision — section 214A is inserted into the Insolvency Act 1986 to discourage members of an LLP from withdrawing capital, including payment equivalent to a company dividend, while the business is or is about to become insolvent, so as to preserve the assets of the LLP available for distribution to creditors in the event of liquidation.

3.4.23 Section 214A provides that, on the application of the liquidator, withdrawals made by a member of the LLP during the two years prior to the commencement of winding up may be subject to clawback if it is proved that at the time of the withdrawals, the member knew or had reasonable grounds for believing that the LLP was, or would be unable to pay its debts. The maximum contribution that a member of the LLP may be ordered to make is up to the amount he or she has withdrawn within those two years before the commencement of the winding-up.

3.4.24 However, the court may not be able to declare in favour of the liquidator, unless it is proved that the member knew or ought to have known that there was no reasonable prospect that the LLP would avoid going into insolvent liquidation.⁶² The burden of proof rests on the liquidator so as not to deter members of viable LLPs from trading through temporary financial difficulties.

Complaints and disciplinary systems

3.4.25 The LLPs Act does not impose any complaints and disciplinary system requirements on LLPs.

⁵⁹ Section 249A(3) of the Companies Act 1985.

⁶⁰ Section 242A of the Companies Act 1985. The civil penalties are between £100 (HK\$1,427) and £1,000 (HK\$14,270) depending on how late the accounts are delivered.

⁶¹ Up to £5,000 (HK\$73,600) for each offence.

⁶² Section 214A (5) of the Insolvency Act 1986.

Risks management strategies

3.4.26 The LLPs Act does not require LLPs to take any specific risk management strategies.

3.5 Impact

Clients and other parties concerned

3.5.1 Although one might expect clients to react unfavourably to the operation of law firms through LLPs and to see LLPs as representing an attack on their rights and a retreat from professional values, the Law Society states that business clients on the whole appear to view LLPs as being forward-looking and abreast of good business practice. The Law Society takes the view that because the liability of LLPs is backed in the same way as general partnerships by compulsory insurance and the Solicitors' Compensation Fund, it makes no difference to clients and third parties in respect of making claims against a law firm, whether it is operated through an LLP or not. However, the Law Society admits that the ability of the claimant to get his or her claim in full may be affected because, if a claim exceeds the firm's insurance cover and the LLP's assets are exhausted, the claimant cannot claim against the personal assets of individual lawyers of that LLP. Apart from that, trade creditors, such as suppliers, could be disadvantaged, in the event of the LLP becoming insolvent, by the limitation of liability status.

Solicitors

3.5.2 The Law Society considers that the insurance premiums for LLPs are not lower than those for general partnerships, because the risk to LLPs (and hence to the insurer) is no less. Instead, it believes that the premiums are likely to be higher, because the qualifying insurers have to agree to stringent terms with the Law Society, and an insurer might find it more difficult to enforce payment of the final premium in the event that an LLP ceases to practise.

3.5.3 The Law Society is of the view that the statutory requirement to file financial information will accelerate the breaking down of the culture of secrecy about law firms' financial affairs.

Chapter 4 - The State of New York

4.1 Background

Emergence of limited liability partnership in the United States

4.1.1 The first LLP statute of the US was enacted in the State of Texas (Texas) in 1991 in response to the massive failure of banks and savings and loans associations in the 1980s. More than one-third of all the bank failures during the crisis occurred in Texas. Claimants were not able to cover all the losses from the principal wrongdoers. Claims were then filed against those professional firms of accountants and lawyers who had represented the failed financial institutions, for their malpractice insurance and wealthy partners' personal assets.⁶³ Under partnership laws, partners, no matter whether they have anything to do with the claimed act, are personally liable for any liability that exceeds their firms' assets.

4.1.2 Among the professional firms lobbying for limited liability, a law firm in Texas drafted a bill limiting the personal liability of innocent partners from malpractice claims. The original proposal, which only applied to professional partnerships, was viewed as a "*help-a-lawyer bill*"⁶⁴ and was rejected by the legislature of Texas. The bill was later revised to extend the limited liability partnership (LLP) structure to all types of business and subsequently approved by the Texas legislature.

4.1.3 Following the adoption of the LLP legislation in Texas, the big multi-state law firms persuaded other states, especially the major commercial states, to authorize the formation of LLPs. NY amended its Partnership Law to include provisions for enabling the formation of "*registered limited liability partnerships*" ("*registered LLPs*" and interchangeable with "*LLPs*") in 1994. All the states of the US currently adopt the LLP business structure with varied details⁶⁵ and allow law firms to operate through LLPs.⁶⁶

Definition and nature of limited liability partnership in the State of New York

4.1.4 "*Registered LLP*"⁶⁷ means "*a partnership without limited partners operating under an agreement governed by the laws*" of NY, registered under section 121-1500 of the NY Partnership Law and complying with the requirements⁶⁸ for naming an LLP. As "*partnership*" is defined as "*an association of two or more persons to carry on as co-owners a business for profit*" and includes "*a registered LLP*", a sole practitioner cannot register as an LLP.

⁶³ Hamilton, Robert W. (1995).

⁶⁴ Ibid.

⁶⁵ Martin, Alson R. (2001).

⁶⁶ Donn, Allan G. (2004).

⁶⁷ Section 2 of the NY Partnership Law.

⁶⁸ The requirements are under section 121-1501 of the NY Partnership Law.

4.1.5 Registered LLP is not a new entity but "*the same entity that existed before the registration and continues to be a partnership*".⁶⁹ It is taxed as a general partnership. There is no separate LLP legislation and the Partnership Law applies to registered LLPs except for provisions stated to be otherwise. The mutual rights and duties of the partners in relation to the registered LLP are determined by the private agreement between them. The law does not expressly provide that a registered LLP has a separate legal personality.⁷⁰ However, the NY State Bar Association is of the view that registered LLPs have a separate legal personality from its partners.

Procedures for setting up limited liability partnership

4.1.6 In order to register as an LLP, a partnership has to file with the Division of Corporations of the Department of State a registration which sets forth a number of items, including⁷¹:

- (a) the name of the LLP;
- (b) the address of the principal office of the partnership;
- (c) the profession or professions to be practised by such partnership and a statement that it is eligible to register as an LLP (to make sure that the business is described in a manner consistent with the permissible business categories);
- (d) if the registration of the partnership is to be effective on a date later than the time of filing, the proposed effective date; and
- (e) if all or specified partners of the LLP are to be liable in their capacity as partners for all or specified debts, obligations or liabilities of the LLP (see paragraph 4.3.12).

⁶⁹ Section 121-1500(d) of the NY Partnership Law.

⁷⁰ Whether an LLP is a separate legal entity or not has long been a disputed issue in the US. Academics believe that the limited liability feature of an LLP has made it fit closer under classification as a separate legal entity. See Bromberg, R. and Ribstein L. (2000) and Martin, Alson R. (2001). However, the Law Society of England and Wales is of the view that an LLP formed under the laws of NY has no separate legal personality and is simply a collection of partners carrying on business together. Therefore, LLPs formed in NY are treated as general partnerships in the UK and allowed to operate in England and Wales as general partnerships.

⁷¹ Section 121-1501 of the NY Partnership Law.

4.1.7 After filing such registration or amendment to the registration, a certified copy of the registration and of each amendment has to be filed by the LLP with the licensing authority⁷² within 30 days.⁷³ Any changes to the statement after registration must be filed with the Department of State no later than 90 days after the change or after a partner becomes aware of it.⁷⁴

4.2 Eligibility

Access to use the limited liability partnership structure

4.2.1 Most states in the US allow all types of business to use the LLP structure. However, NY is one of the two states⁷⁵ that restrict the LLP option to professionals only. Under the NY Partnership Law, only general partnerships whose partners are "licensed professionals" may apply to operate as LLPs.⁷⁶ The term "professionals"⁷⁷ means attorneys, counsellors-at-law⁷⁸, licensed physicians, as well as individuals authorized to practise those professions designated in the New York Education Law. No LLP may render a professional service except through individuals authorized by law to render such professional service as individuals.⁷⁹

4.2.2 In order to be eligible to register as a NY LLP, an entity must be organized first as a general partnership. Three kinds of general partnerships (without limited partners) are eligible to register as LLPs⁸⁰:

- (a) a partnership each of whose partners is authorized by law to render a professional service in NY; or
- (b) a partnership is authorized by, or holds a licence issued by the licensing authority; or
- (c) a related LLP which is not a professional partnership itself, but is affiliated with a limited liability business entity which renders professional services and the related LLP itself renders services related or complementary to those professional services.

⁷² "Licensing authority" refers to the Regents of the University of the State of New York or the State Education Department for all professions licensed under title eight of the Education Law, and the Appellate Division of the Supreme Court for the profession of law.

⁷³ Section 121-1500(p) of the NY Partnership Law.

⁷⁴ Section 121-1500(j) of the NY Partnership Law.

⁷⁵ The other state is the State of California.

⁷⁶ Section 121-1500 of the NY Partnership Law.

⁷⁷ Section 2 of the NY Partnership Law.

⁷⁸ According to the NY State Bar Association, there is no substantial difference between an "attorney" and a "counsellor-at-law".

⁷⁹ Section 121-1500(n) of the NY Partnership Law.

⁸⁰ Section 121-1500(a) of the NY Partnership Law.

Use of limited liability partnership and other business structures for legal practices

4.2.3 Lawyers in NY may practise in the form of sole proprietorships, professional service corporations⁸¹, professional service limited liability companies⁸², LLPs, or professional partnerships. However, limited partners are not allowed to take part in professional partnerships or LLPs, including law firms, in NY⁸³.

4.2.4 An empirical study⁸⁴ conducted in mid-2002 showed that 21% (1 113 firms) of NY's 5 202 law firms (only main offices were counted in this survey) operated as LLPs, whilst 38% as general partnerships and 29% as professional corporations.⁸⁵ For large law firms (with more than 50 lawyers), the tendency was to organize as an LLP (63% of 98 large law firms) or a general partnership.

Use of limited liability partnership by other professions and businesses

4.2.5 Apart from lawyers, the legislation in NY provides limited access to the LLP option for around 40 other licensed professions in the areas of health, architecture and the like (See paragraph 4.2.1).

Statutory requirements for setting up limited liability partnership

Eligibility

4.2.6 There must be two or more partners to form an LLP and the partner can be an individual, a general partnership, an LLP, or a corporation. Each partner has to be a licensed professional or a licensed professional firm (either domestic or foreign), including an LLP, a professional service LLC or a professional service corporation.

⁸¹ In NY, a professional service corporation is a corporation organized under the business corporation law, which is authorized by the licensing authority to render professional services.

⁸² It is organized under article XII of the NY Limited Liability Company Law.

⁸³ Section 121-1500 of the NY Partnership Law.

⁸⁴ Hillman, Robert W. (2003). The survey was based on the Martindale-Hubbell Database available on LexisNexis. The database, being claimed to be the most complete listing of lawyers and law firms, is a voluntary directory, and includes only those law firms that choose to appear in it. In addition, the survey did not count branch offices. A law firm with multiple offices was counted as a single firm.

⁸⁵ The rest of the law firms were in the form of LLCs (3%) or sole proprietorships (9%).

Disqualification of partners

4.2.7 The NY Partnership Law does not have any provision on the disqualification of a partner of an LLP. Nevertheless, an LLP may dissolve if any partner turns bankrupt.⁸⁶ A court does not have the authority to disqualify a certain partner of an LLP, but it may order the dissolution of an LLP if, on application by any partner, the court is satisfied that⁸⁷:

- (a) a partner has been declared incompetent in any judicial proceeding or is shown to be of unsound mind; or
- (b) a partner becomes in any other way incapable of performing his or her part of the partnership contract; or
- (c) a partner has been guilty of such conduct as tends to affect prejudicially the carrying on of the business; or
- (d) a partner wilfully or persistently commits a breach of the partnership agreement, or otherwise so conducts himself or herself in matters relating to the partnership business that it is not reasonably practicable to carry on the business in partnership with him or her.⁸⁸

New York State Bar Association's rules for practising through limited liability partnership

4.2.8 The Lawyers' Code of Professional Responsibility published by the NY State Bar Association restricts ownership of any law firm, including LLPs and general partnerships, to those individuals and entities authorized to practise law.

4.3 Scope of liability limitation

Liability of limited liability partnership

4.3.1 A partner of an LLP is an agent of the LLP for the purpose of its business, and the act of every partner for carrying on the business of the LLP binds the LLP. An LLP is liable to the same extent as a partner who has, by his or her acts or omissions, caused any loss or injury of a third party, or any penalty in the ordinary course of the business of the LLP, or with the authority of his or her co-partners.⁸⁹

⁸⁶ Section 62 of the NY Partnership Law.

⁸⁷ Section 63 of the NY Partnership Law.

⁸⁸ The court may also decree a dissolution if the business of the partnership can only be carried on at a loss or other circumstances render a dissolution equitable.

⁸⁹ Section 24 of the NY Partnership Law.

4.3.2 However, an LLP is not bound if the partner so acting has in fact no authority to act for the partnership in the particular matter, and the person with whom he or she is dealing has knowledge of the fact that he or she has no such authority.⁹⁰

Liability of individual partners

Partial and full shield against liability for other partners' wrongdoings

4.3.3 NY was one of the two states⁹¹ which first extended the liability shield to the level enjoyed by corporations since Texas adopted the first US legislation on LLP in 1991. What Texas offered in 1991 was a partial shield, with innocent partners being protected only from tortious liability for malpractice claims against other fellow partners. Under a partial shield, partners are liable for commercial debts and contract liabilities arising from the wrongdoings of each other.

4.3.4 By 2000, more than half of the states in the US adopted a full shield model,⁹² including Texas⁹³. The full shield provided by the NY legislation protects innocent partners from being liable for all tort and contract claims, no matter whether those liabilities are direct or indirect. Section 26(b) of the NY Partnership Law states that a partner of an LLP is not liable "*directly or indirectly (including by way of indemnification, contribution or otherwise), for any debts, obligations or liabilities of, or chargeable to, the registered LLP or each other; whether arising in tort, contract or otherwise*" solely by reason of being such a partner as long as that partner is not personally negligent or the supervisor of someone who is personally negligent.

4.3.5 The NY Partnership Law has the phrase "*whether arising in tort, contract or otherwise*" because malpractice may be pleaded as tort or contract. Under the old Texas LLP legislation, if a client pleaded the claim as one arising from a breach of an implied warranty which was part of his or her contract with the law firm, it was not clear whether all the partners of the law firm would be liable. The NY legislation has clarified this point and extended its protection to contract claims.

Indirect liability by contribution or indemnification

4.3.6 A partnership is required by law in NY to indemnify partners for personal liability incurred in the course of partnership business, and the partners are required to contribute to the partnership assets any sum necessary to satisfy partnership obligations or to pay their respective share of partnership losses.

⁹⁰ Section 20 of the NY Partnership Law.

⁹¹ Minnesota was the other state which adopted the full shield model in 1994.

⁹² Martin, Alson. (2001).

⁹³ Bromberg, R. and Ribstein L. (2000).

4.3.7 The obligations of indemnification and contribution raise the possibility of having innocent partners of an LLP being liable to make indirect payments to satisfy a malpractice claim in the name of indemnification or contribution.⁹⁴ For instance, partners personally liable for a malpractice claim may seek indemnification from the LLP and its innocent partners, arguing that the obligation to indemnify the partner arises from the partnership relationship instead of from the malpractice or negligence itself.

4.3.8 If the LLP satisfies a claim out of its assets, the capital accounts of all the individual partners are reduced. Individual partners may be compelled by the partnership or the other partners to make contributions to the partnership. These payments are technically "*contributions*", but are actually indirect payments to satisfy a malpractice claim. The NY LLP legislation is phrased as such to eliminate this possibility and protect LLP partners from indirect liability "*by way of indemnification, contribution or otherwise*" for claims.⁹⁵ Nonetheless, partners of an LLP may agree to contribute under the partnership agreement of the LLP.

Liability for one's own wrongdoings

4.3.9 A partner of an LLP is "*personally and fully liable and accountable for any negligent or wrongful act or misconduct committed by him or her*".⁹⁶

Liability for supervision

4.3.10 A partner of an LLP is personally and fully liable and accountable for any negligent or wrongful act or misconduct committed "*by any person under his or her direct supervision and control while rendering professional services on behalf of such registered LLP*"⁹⁷. There is no statutory definition on "*direct supervision and control*". Additionally, there is no statutory guidance on whether a claimant needs to establish that a partner is negligent in his or her supervision.

Liability in the winding up of limited liability partnership

4.3.11 While partners of a general partnership have to contribute the amount necessary to satisfy the liabilities of the partnership upon its dissolution, the NY Partnership Law exempts partners of an LLP from such obligation.⁹⁸

⁹⁴ Hamilton, Robert W. (1995).

⁹⁵ Section 26(b) of the NY Partnership Law.

⁹⁶ Section 26 (c) of the NY Partnership Law.

⁹⁷ Section 26 (c) of the NY Partnership Law.

⁹⁸ Sections 26(b) and 71(d) of the NY Partnership Law.

Option to withdraw from the shield of limited liability

4.3.12 The NY statute allows that if a majority of partners in an LLP agree, all or specified partners may be liable in their capacity as partners for all or specified debts, obligations or liabilities of the LLP.⁹⁹ Such an agreement may be modified or revoked by a majority of partners as well, and this arrangement does not affect the liability of partners prior to that modification or revocation.¹⁰⁰

4.4 Safeguards

Insurance

Statutory requirements

4.4.1 There is no statutory minimum insurance requirement for LLPs in NY, leaving the issue to statutes or rules dealing with individual professions.

4.4.2 In some other states, there is a requirement of minimum insurance. For instance, Texas has chosen an arbitrary amount of US\$100,000 (HK\$778,800). California has the insurance amount based on the number of partners and requires, for law firms operating as LLPs, a minimum insurance amount of US\$100,000 (HK\$778,800) per lawyer up to a maximum of US\$7.5 million (HK\$58.41 million) for claims asserted in any one calendar year.

New York State Bar Association's rules

4.4.3 There is no compulsory insurance requirement for LLPs or its partners.

Disclosure of limited liability status

Name of registered limited liability partnership

4.4.4 Under section 121-1501 of the NY Partnership Law, the name of each registered LLP must contain without abbreviation the words "*Registered Limited Liability Partnership*" or "*Limited Liability Partnership*" or the abbreviations "*R.L.L.P.*", "*RLLP*", "*L.L.P.*" or "*LLP*".¹⁰¹ There is no statutory requirement for an LLP to put its full name or the abbreviations on the stationery, business cards or other documents of the LLP.

⁹⁹ Section 26(d) of the NY Partnership Law.

¹⁰⁰ Ibid.

¹⁰¹ Section 121-1501 of the NY Partnership Law.

Publication of notice

4.4.5 Within 120 days after the effective date of the registration of an LLP, a copy of the items specified in the application of registration or a copy of a notice containing those items has to be published once in each week for six successive weeks, in two newspapers of the county in NY in which the principal office of the LLP is located. One of the two newspapers chosen has to be published in the city or town in which the principal office within NY is intended to be located.¹⁰²

4.4.6 Failure to publish such notice or to file such proof within the 120-day period prohibits the LLP from maintaining any action or special proceeding in NY. However, the failure of publish such notice or to file such proof does not impair the validity of any contract or act of the LLP.

New York State Bar Association's rules

4.4.7 According to the NY State Bar Association, there is no duty for an LLP law firm to inform its clients individually that the law firm is converted from a general partnership into an LLP, although it is customary to do so and ethical considerations would suggest that stationery, business cards and other items carrying the name of the partnership be modified to reflect its name.

Non-financial reporting

Statutory requirements

4.4.8 Each LLP has to, within 60 days prior to its fifth anniversary of the effective date of its registration and every five years thereafter, furnish a statement to the Department of State setting forth a number of items, including:

- (a) the name of the LLP;
- (b) the address of the principal office of the LLP; and
- (c) a statement that it is eligible to register as an LLP.

¹⁰² Section 121-1500(a) of the NY Partnership Law.

4.4.9 If the statement is not timely filed, the Department of State may proclaim that the registration to be revoked 60 days after mailing to the LLP a notice of the failure to file the statement.¹⁰³ Upon publication of the proclamation in the state register, the registration is deemed revoked. The concerned partnership may file a certificate of consent with that statement or certifying that the statement has been filed, and pay the statutorily required fees to reinstate its LLP status. Upon reinstatement, the limited liability status is available to the partners for the lapse period.

New York State Bar Association's rules

4.4.10 The NY State Bar Association does not require law firms operating through LLPs to file an annual report or update the changes in names of partners or other particulars of the LLPs with the Association.

Financial reporting

4.4.11 The NY Partnership Law does not impose any financial disclosure requirement on LLPs and does not require LLPs to keep or disclose any accounting records.

Preservation of assets in the course of winding up

4.4.12 The NY Partnership Law does not provide that the capital withdrawn by partners of an LLP while the business is or is about to become insolvent may be clawed back in the event of insolvency.

¹⁰³ Section 121-1500(g) of the NY Partnership Law.

Complaints and disciplinary systems

4.4.13 The NY Partnership Law¹⁰⁴ provides that an LLP, other than those authorized to practise law, must be under the supervision of the Regents¹⁰⁵ of the University of the State of New York¹⁰⁶. These LLPs are subject to disciplinary proceedings and penalties in the same manner and to the same extent as are provided with respect to individuals and their licences relating to the applicable profession. The Board of Regents, which oversees the State Education Department and its Office of the Professions (OP), licenses individuals in 44 professions defined in the Education Law and takes final action on all professional disciplinary matters. OP investigates and prosecutes professional misconduct in all professions except law and medicine¹⁰⁷.

4.4.14 The Appellate Division of the New York State Supreme Court regulates and disciplines lawyers in NY.¹⁰⁸ It has ultimate authority over lawyers' conduct in its jurisdiction, and may impose discipline ranging from public censure to suspension of the licence to practise or even the permanent loss of the licence if the charges are sustained. All lawyers, practised through LLPs or otherwise, are expected to follow the rules of ethics, known as the Code of Professional Responsibility, which have been adopted by the Appellate Division.

Risk management strategies

4.4.15 There is no statutory provision requiring LLPs to take risk management strategies.

4.5 Impact

4.5.1 The NY State Bar Association states that it does not have information on the impact of law firms practising as LLPs on lawyers themselves and their clients.

¹⁰⁴ Section 121-1500(m) of the NY Partnership Law.

¹⁰⁵ Established by the NY State Legislature, the Regents of the University of the State of New York are responsible for the general supervision of all educational activities within the State, presiding over the University and the New York State Education Department.

¹⁰⁶ The University of the State of New York is a broad term encompassing all the institutions, both public and private, offering education in the State.

¹⁰⁷ A registered LLP authorized to practise medicine is subject to the pre-hearing procedures and hearing procedures as are provided with respect to individual physicians and their licences in the public health law.

¹⁰⁸ Complaints against attorneys are directed to the Appellate Division's Attorney Grievance and Disciplinary Committee in the county where the attorneys' offices are located.

4.5.2 According to the NY State Bar Association, the limited liability status of a law firm does not affect its liability or the availability of its assets to pay a debt. In addition, the limited liability status of a law firm does not change its need for insurance to protect its own assets. In the case of a partner of an LLP, he or she still has the need to protect himself or herself for those claims to which the limited liability status is not applicable.

Chapter 5 - New South Wales

5.1 Background

Emergence of liability capping legislation for professionals

5.1.1 NSW was the first state in Australia to introduce legislation capping professional liability, resulting in the enactment of the Professional Standards Act in 1994. Although all the Australian States and Territories, except for Tasmania, have passed similar legislation, only NSW and Western Australia have professional standards schemes operating at the moment.

5.1.2 The liability capping legislation was developed in the late 1980s and early 1990s¹⁰⁹ against the background of a dramatic rise in professional negligence claims and insurance premiums. In the second reading of the Professional Standards Bill in 1994, the then Attorney General explained the problem to the NSW Legislative Council¹¹⁰:

"Developments in the law have opened up new fields of liability and compensation payments have increased by sharp increments. Increasingly, plaintiffs are looking to their professional advisers as a source of recovery of loss. The general perception is that professionals have financial substance and hold professional indemnity insurance...the fact is that for many professionals insurance is now unavailable or unaffordable to levels commensurate with their exposure and liability."

5.1.3 As an alarming number of professional practitioners chose to reduce their insurance cover or go uninsured, the NSW government was of the view that in theory an aggrieved client could be awarded unlimited damages, but in reality he or she had no certainty of recovery. The then Attorney General further pointed out that a de facto cap on liability was already operating -- the capacity of a professional to meet a valid claim was actually limited by the level of indemnity insurance and the professional's personal assets. There was also anecdotal evidence from professional bodies suggesting that professionals tried to meet the high financial risk with an excessive degree of caution, with detrimental effect on clients.

5.1.4 The NSW government addressed the problem by introducing the Professional Standards Bill, which enabled occupational associations to establish their own professional standards scheme, requiring members to insure and implement risk management strategies in exchange for having their liability capped at a certain level.

¹⁰⁹ The Attorney General's Department released a paper in 1989 which outlined the problem of increasing claims and insurance premiums. In 1990, a discussion paper entitled "Professional Liability, Insurance and Risk Management" outlined a proposal to cap the liability of professionals.

¹¹⁰ NSW Legislative Council Hansard. 14 September 1994, pp.2933-2935.

5.1.5 Each occupational association may determine whether it will put forward a scheme for its members. The first professional standards scheme – the Solicitors Professional Standards Scheme (Solicitors Scheme) was set up by the Law Society of New South Wales (NSW Law Society) in 1996.

Business structures of legal practices

5.1.6 There were 5 331 legal practices in NSW as at 1 November 2004 and 3 666 of them operated as partnerships¹¹¹. The rest were either solicitor corporations¹¹² or incorporated legal practices.

5.1.7 Since 1 July 2001, NSW legal service providers have been permitted to incorporate.¹¹³ Nonetheless, only around 7%, i.e. 389 legal practices in NSW were incorporated legal practices as at 1 November 2004. Incorporated legal practices can limit their corporate liability, but they are also required to meet insurance requirement under the Legal Profession Act.¹¹⁴

5.1.8 There is no provision for the formation of LLP, but NSW has adopted the Professional Standards Act 1994, which allows solicitors and other professionals to cap their liability at a certain level.

5.1.9 The NSW Law Society has more than 14 000 members, approximately 11 000 of whom are private practitioners. The number of solicitors participating in the Solicitors Scheme was 8 618 in 2004.¹¹⁵ The Solicitors Scheme also applies to the partners and employees of those covered by the scheme.

Nature of professional standards scheme

5.1.10 The Professional Standards Act 1994 and the professional standards schemes established accordingly do not distinguish between negligent and innocent partners for the sake of capping liability. Each professional standards scheme provides a cap on liability for all eligible professionals, no matter whether they are directly involved in the claimed act or not.

¹¹¹ Out of the 3 666 partnerships, 3 044 were sole practitioners.

¹¹² There were only 54 solicitor corporations, which are company-like structures with no limited liability. Solicitor corporations can no longer be created under the Legal Profession Act 1987.

¹¹³ Division 2A of Part 3 of the Legal Profession Act 1987 as amended in 2000.

¹¹⁴ Section 47K of the Legal Profession Act 1987 as amended.

¹¹⁵ Professional Standards Council. (2004).

5.1.11 The amount of liability will not exceed the set ceiling under a professional standards scheme. The purpose is to provide certainty to both the professionals under the schemes and their claimants, so that professionals know the limit of their liability, and claimants understand how far their losses can be covered in a valid claim. In exchange for this certainty, the professionals under the professional standards scheme have to insure and implement risk management strategies for the protection of the parties concerned, and to enhance their professional standards of services through better self-regulation.

Procedures for setting up professional standards scheme

5.1.12 An occupational association intending to set up a professional standards scheme has to apply with the Professional Standards Council (PSC), which is a statutory body formed¹¹⁶ under the Professional Standards Act 1994. It is governed by part-time members appointed by the Attorney General of NSW. Its main role is to approve and monitor professional standards schemes.

5.1.13 Whilst PSC is evaluating the application, it must publish a notice in a daily newspaper circulating in NSW explaining the nature and significance of the proposed scheme, and inviting comments and submissions within a specified time¹¹⁷. It may conduct a public hearing as well.

5.1.14 Before approving a proposed scheme, PSC must consider the following¹¹⁸:

- "(a) All the comments and submissions made to PSC;*
- (b) The position of persons who may be affected by limiting the occupational liability of members of the occupational association concerned;*
- (c) The nature and level of claims relating to occupational liability made against members of the occupational association concerned;*
- (d) The risk management strategies of the occupational association concerned;*
- (e) The means by which those strategies are intended to be implemented;*
- (f) The cost and availability of insurance against occupational liability for members of the occupational association concerned; and*
- (g) The standards determined by the occupational association concerned in relation to insurance policies."*

¹¹⁶ It was formed in 1995.

¹¹⁷ The time given should not be less than 21 days after the publication of the notice.

¹¹⁸ Section 10 of the Professional Standards Act 1994.

5.1.15 The scheme approved by PSC is submitted to the Attorney General of NSW, who may authorize the publication of the approved scheme in the Gazette.¹¹⁹ Written notice of the making of the scheme has to be laid before each House of Parliament of NSW within 14 sitting days after the day on which it is published in the Gazette.¹²⁰

5.1.16 Either House of Parliament may pass a resolution disallowing the professional standards scheme in the same way that a statutory rule may be disallowed.¹²¹ A person who is or is reasonably likely to be affected by the scheme published may also apply to the Supreme Court for an order that the scheme is void.¹²²

5.1.17 An occupational association with a professional standards scheme pays an annual fee to PSC. In NSW, the fee is calculated at the rate of AUS\$35 (HK\$200.6) per member covered by the professional standards scheme.

5.1.18 A professional standards scheme remains in force for a period not exceeding five years from its commencement. For the legal profession, the Solicitors Scheme was established on 5 December 1996 and renewed on 22 November 2000. The present Solicitors Scheme will remain in force until 21 November 2005.

5.1.19 The NSW government may direct PSC to review the operation of the professional standards scheme concerned. PSC may also conduct a review on its own initiative. A review may be conducted in order to decide whether a professional standards scheme should be amended or revoked, or whether a new scheme should be made. PSC may prepare an amendment to or revocation of a professional standards scheme.¹²³ Before the amendment or revocation, PSC must consider the same set of factors as that for approving a proposed professional standards scheme.

5.2 Eligibility

Access to establish professional standards scheme

5.2.1 Only an occupational association may prepare a professional standards scheme and apply for approval. An occupational association is *"a body corporate which represents the interests of persons who are members of the same occupational group or related occupational groups, and the membership of which is limited principally to members of that occupational group or those occupational groups"*.¹²⁴

¹¹⁹ The scheme commences on a date specified in the approved scheme or two months after the date of its publication in the Gazette.

¹²⁰ Section 13 of the Professional Standards Act 1994 and section 40 of the Interpretation Act 1987.

¹²¹ Section 41 of the Interpretation Act 1987.

¹²² Section 15(1) of the Professional Standards Act 1994.

¹²³ Sections 16 and 16A of the Professional Standards Act 1994.

¹²⁴ Section 4 of the Professional Standards Act 1994.

Application of liability capping legislation on legal and other professions

5.2.2 Apart from the Solicitors Scheme, seven other professional standards schemes have been established in NSW over the years. They are the Professional Surveyors Scheme, Professional Engineers Scheme, National Institute of Accountants Scheme, Investigative and Remedial Engineers Professional Standards Scheme, Institute of Consulting Valuers Scheme, Accountants Professional Standards Scheme and the Barristers Professional Standards Scheme.

5.2.3 Under the Professional Standards Act 1994, the requirements for establishing a professional standards scheme apply to the legal profession and other professions alike. The legislation sets out a minimum level of liability applicable to all professions. Nevertheless, each of the occupational associations can always establish a higher threshold for its own profession. While the legislation lists the types of safeguards that all professional standards schemes must provide, each occupational association may determine the specifics of those measures, such as standards of insurance policies, to best suit the characteristics of the profession. In short, while the professional standards schemes share a common framework, the specific requirements vary.

Eligibility for professional standards scheme

5.2.4 Under the Professional Standards Act 1994, a professional standards scheme may apply to all persons or a specified class of persons within an occupational association. A person may apply to the occupational association for exemption from the professional standards scheme.

5.2.5 The Professional Standards Act 1994 requires professionals to have insurance and/or business assets¹²⁵ of value not less than the maximum amount of liability applicable under a professional standards scheme. An occupational association may require its members to hold insurance against occupational liability and impose such a requirement as a condition of membership. In that event, as a person must be a member of an occupational association before the respective professional standards scheme applies to him or her, the insurance provision is not just a membership condition but also an eligibility requirement for joining a professional standards scheme.

5.2.6 If a professional standards scheme applies to a person, it applies to each partner and employee of that person. In other words, if a person is covered by a professional standards scheme, the liability of his or her partners and employees will also be capped as a result. If a professional standards scheme applies to a body corporate, it also applies to each officer¹²⁶ of the body corporate as well.

¹²⁵ Business assets cannot be used as a reference to fulfil the requirement for limitation of liability unless the particular professional standards scheme has such specification.

¹²⁶ "Officer" of a corporation in general means a director or secretary of the corporation, or a person who is concerned or takes part in the management of that corporation.

Eligibility for Solicitors Professional Standards Scheme

5.2.7 The Solicitors Scheme is available to all members of the NSW Law Society who are holding a current practising certificate and have the benefit of an insurance policy. The insurance policy under which the amount payable in respect of occupational liability must not be less than the maximum amount of liability specified in the Solicitors Scheme¹²⁷. Members of the NSW Law Society can apply for exemption from the Solicitors Scheme.

5.2.8 For an incorporated legal practice, the practice itself is not covered by the Solicitors Scheme because a body corporate cannot be a member of the NSW Law Society, and therefore, not eligible for the Solicitors Scheme. As it is required by law¹²⁸ that there must be at least one solicitor director¹²⁹ in an incorporated legal practice, the solicitor director can be a member of the NSW Law Society and thus covered by the Solicitors Scheme.

5.3 Scope of liability limitation

Liability of law firm

5.3.1 If a law firm runs as a general partnership, its partners are fully and personally liable for all the liabilities of the firm. Nevertheless, under the Solicitors Scheme, the partners' liabilities are capped and hence, the law firm's liabilities are capped as a result.

5.3.2 The NSW Law Society currently only accepts individuals as members, and incorporated legal practices, as corporations, would not be eligible to be members, and hence, would not be covered by the Solicitors Scheme. In any event, as a corporation, the liability of an incorporated legal practice is limited.

Nature of liability for individual solicitors

5.3.3 The nature of the liability to be capped is governed by the Professional Standards Act 1994 for all professions alike. The capped occupational liability includes *"civil liability arising (in tort, contract or otherwise) directly or vicariously from anything done or omitted by a member of the occupational association acting in the performance of his or her occupation"*.¹³⁰

¹²⁷ The Solicitors Scheme does not limit liability using business assets.

¹²⁸ Section 47E of the Legal Profession Act 1987.

¹²⁹ A solicitor director means a director of an incorporated legal practice who holds an unrestricted practising certificate as a solicitor and barrister.

¹³⁰ Section 4 of the Professional Standards Act 1994.

5.3.4 The Professional Standards Act 1994 does not cap liability for damages arising from any one of the following¹³¹:

- (a) death or injury to a person;
- (b) breach of trust;
- (c) fraud or dishonesty; and
- (d) liability which may be the subject of proceedings under Part 13 or 14 of the Real Property Act¹³².

Maximum amount of liability

Statutory cap for all professions

5.3.5 The limitation of liability is made on a per claim basis. The maximum liability is a limitation of the amount of damages that may be awarded for a single claim, not for all claims arising out of a single event.¹³³

5.3.6 The Professional Standards Act 1994 prohibits the splitting of claimants or defendants, which may occur in an attempt to generate more claims so as to avoid the limit.¹³⁴ Two or more claims by the same person arising out of a single event against associated persons to whom a professional standards scheme applies are to be treated as a single claim. Persons are associated if they are partners, employees of the same employer or in the relationship of employer and employee, or officers of the same body corporate or in the relationship of body corporate and officer of the body corporate.¹³⁵

¹³¹ Section 5 of the Professional Standards Act 1994.

¹³² Under the Real Property Act, any person who suffers loss or damage in respect of any land arising from a number of reasons listed in Part 13 or 14 of the Real Property Act, is entitled to payment of compensation from the Torrens Assurance Fund administered by the Registrar-General.

¹³³ Section 29 of the Professional Standards Act 1994.

¹³⁴ Ibid.

¹³⁵ Ibid.

5.3.7 The Professional Standards Act 1994 provides that the maximum amount of liability must not be less than AUS\$500,000¹³⁶ (HK\$2,865,000) for a single claim, with the view that the great majority of claims are met in full¹³⁷. The policy behind the legislation is that *"it is preferable to provide some guarantee of payment for the vast majority of claimants than to have a system of unlimited liability with no certainty of any payment"*¹³⁸.

5.3.8 Professionals covered by a professional standards scheme are liable to damages not exceeding AUS\$500,000 (HK\$2,865,000), whilst their respective occupational association is given the discretionary authority to specify a higher maximum amount of liability. The statutory cap would not prevail over other regulatory schemes. For instance, if a statute requires a certain profession be covered with a higher compulsory insurance, the professionals concerned would be subject to that higher compulsory insurance requirement instead of the AUS\$500,000 (HK\$2,865,000) cap imposed by the Professional Standards Act 1994.

5.3.9 The Professional Standards Act 1994 provides for a number of different bases for specifying the limitation amount, including a set amount for all cases, different amounts for different classes of practitioners or different kinds of work, and a multiple of the fee charged for services provided. The occupational associations applying for a professional standards scheme may select one of these bases to best suit the characteristic of their professions.

Amount of liability capped under Solicitors Scheme

5.3.10 Under the Solicitors Scheme, an NSW Law Society member may have limited liability of between AUS\$1.5 million (HK\$8.60 million) and AUS\$50 million (HK\$286.5 million).

5.3.11 The Solicitors Scheme specifies different limitation amounts for different classes of persons. The persons specified include solicitors and their employees. For persons in a sole practitioner legal practice or in a legal practice having no more than three principals, the maximum amount of liability is AUS\$1.5 million (HK\$8.60 million). For solicitors who practise in a firm having more than three principals, it can be calculated by multiplying AUS\$500,000 (HK\$2,865,000) by the number of principals in the firm, up to AUS\$10 million (HK\$57.3 million), but a member can select a higher liability amount up to AUS\$50 million (HK\$286.5 million).

¹³⁶ Sections 22-26 of the Professional Standards Act 1994.

¹³⁷ Speech of the Attorney General in the second reading of the Professional Standards Bill. NSW Legislative Council Hansard. 14 September 1994, pp.2933-2935.

¹³⁸ Ibid.

5.3.12 The maximum amount of liability of persons in a legal practice is specified in the Solicitors Scheme as follows:

Class	Description	Maximum amount of liability (for a single claim)
1	Persons in a sole practitioner legal practice or in a legal practice having no more than three principals ¹³⁹	AUS\$1.5 million (HK\$8.60 million)
2	4 principals	AUS\$2.0 million (HK\$11.46 million)
3	5 principals	AUS\$2.5 million (HK\$14.33 million)
4	6 principals	AUS\$3.0 million (HK\$17.19 million)
5	7 principals	AUS\$3.5 million (HK\$ 20.10 million)
6	8 principals	AUS\$4.0 million (HK\$ 22.92 million)
7	9 principals	AUS\$4.5 million (HK\$ 25.79million)
8	10 principals	AUS\$5.0 million (HK\$ 28.65 million)
9	11 principals	AUS\$5.5 million (HK\$ 31.52 million)
10	12 principals	AUS\$6.0 million (HK\$ 34.38 million)
11	13 principals	AUS\$6.5 million (HK\$ 37.25 million)
12	14 principals	AUS\$7.0 million (HK\$ 40.11 million)
13	15 principals	AUS\$7.5 million (HK\$ 42.98 million)
14	16 principals	AUS\$8.0 million (HK\$ 45.84 million)
15	17 principals	AUS\$8.5 million (HK\$ 48.71 million)
16	18 principals	AUS\$9.0 million (HK\$ 51.57 million)
17	19 principals	AUS\$9.5 million (HK\$ 54.44 million)
18	20 or more principals	AUS\$10.0 million (HK\$ 57.3 million)
19	Persons in a legal practice where the sole practitioner or principals in classes 1 -18, as the case may be, select and specify a maximum amount of liability greater than that specified for the class	The selected maximum amount of liability greater than that specified for the class but not exceeding a maximum amount of AUS \$50.0 million (HK\$ 286.5 million)

¹³⁹ Partners of the legal practice are regarded as principals of the practice.

5.4 Safeguards

5.4.1 The statutory cap on damages is tied to a number of safeguards. These measures are introduced not only to protect the interests of the parties concerned, but also to promote greater professional control through self-regulation.

Insurance

Statutory requirements

5.4.2 The Professional Standards Act 1994 in NSW requires the professions to insure in exchange for having their liability capped. The legislation provides that an occupational association may compel its members to hold insurance under a professional standards scheme and the insurance policy must comply with the standards determined by the respective occupational association.¹⁴⁰

5.4.3 Given that the benefit of insurance must not be less than the amount of the liability ceiling, the statutory requirement for minimum insurance is AUS\$500,000¹⁴¹ (HK\$2,865,000) for a single claim.

5.4.4 Although the Professional Standards Act 1994 does not require occupational associations to report annually to PSC the claims made against its members, PSC requires that they include claims information in their annual report on risk management strategies.

Solicitors Scheme requirements

5.4.5 A solicitor must have the benefit of insurance for an amount not less than his or her capped liability. The professional indemnity insurance policies cover both solicitors and their employees, although it is not usual to claim against employees.

5.4.6 The first AUS\$1.5 million (HK\$8.60 million) of insurance is to be covered by a master policy approved under the Legal Profession Act. The insurance policy concerned must cover all civil liability arising in connection with the solicitors' practice, have retrospective cover (covering claims notified in the year of cover that may arise from incidents that occurred before the commencement of the policy) and provide automatic reinstatement.¹⁴²

¹⁴⁰ Sections 21, 27 and 34 of the Professional Standards Act 1994.

¹⁴¹ Sections 22-26 of the Professional Standards Act 1994.

¹⁴² Where claims exhaust one's cover, the cover is automatically reinstated for covering another claim. For instance, where an insurance policy has a claim for AUS\$2 million (HK\$11.46 million) and uses up all the cover, the policy will cover another claim up to AUS\$2 million (HK\$11.46 million).

Disclosure of limited liability status

5.4.7 The Professional Standards Act 1994 requires a person with capped occupational liability to specify that fact on all documents given to a client or prospective client that promote or advertise the person or the person's occupation, including official correspondence ordinarily used by the person in the performance of his or her occupation.¹⁴³ Non-compliance of the disclosure requirement is an offence and the maximum penalty is a fine of AUS\$5,500 (HK\$31,515).¹⁴⁴

5.4.8 The Professional Standards Regulation 2004 prescribes a statement for solicitors and other professionals to adopt to fulfil the disclosure requirement. The statement is "*Liability limited by a scheme approved under Professional Standards Legislation.*"¹⁴⁵ The size of the disclosure statement is also specified in the Professional Standards Regulation 2004.¹⁴⁶ All in all, the disclosure should be adequate to reveal that the liability of the service provided is limited.

5.4.9 The policy statement on disclosure of limited liability issued by PSC states that, at a minimum, the disclosure should appear on the following documents:

- (a) letterhead, letters, etc. signed by the company or on its behalf;
- (b) fax cover sheets;
- (c) documents such as written advice, plans, drawings, specifications and other documents produced by the service provider for clients where those documents are not accompanied by a letter or other document on which appears a disclosure statement when given to a client;
- (d) newsletters and other publications;
- (e) memorandum of fees and invoices not accompanied by a letter or other document on which appears a disclosure statement when given to a client and where no previous documents on which appeared a disclosure statement was previously given to the client;
- (f) e-mail; and
- (g) websites via which services are delivered to clients¹⁴⁷.

¹⁴³ Section 33(1) of the Professional Standards Act 1994.

¹⁴⁴ Section 33(2) of the Professional Standards Act 1994.

¹⁴⁵ Until 29 October 2005, the old form of statement may be adopted as well: "*Liability limited by Solicitors Scheme, approved under the Professional Standards Act 1994 (NSW)*".

¹⁴⁶ It is required that the statement be printed in a size not less than the face measurement of Times New Roman typeface in 8 point.

¹⁴⁷ Where a website only contains promotional material, it is not necessary to include a disclosure statement.

Non-financial reporting

5.4.10 The NSW Law Society and other occupational associations have to provide an annual report to PSC as to the implementation and monitoring of their risk management strategies, the effect of these strategies and any changes made or proposed to be made under their respective professional standards scheme.¹⁴⁸ They are also required to monitor their members' compliance with the insurance requirements and the implementation of the complaints and disciplinary systems, to take appropriate actions and to report to PSC.

Financial reporting

5.4.11 The Professional Standards Act 1994 does not impose any reporting requirement on financial information of those covered by professional standards schemes. Those persons covered by the Solicitors Scheme are not required to report their financial position to the NSW Law Society or PSC either.

Complaints and disciplinary systems

Statutory requirements

5.4.12 The Professional Standards Act 1994 provides a Model Code to deal with complaints and disciplinary matters in Schedule 1 as default rules. Occupational associations may set up their own complaints and disciplinary systems.

5.4.13 The Model Code states that an occupational association must consider a complaint as soon as practicable. After an occupational association has conducted a hearing into a complaint against a person, it may discipline the person in various ways if it finds the complaint substantiated. However, an occupational association is not entitled to award any compensation. Within 30 days after a decision is made concerning a complaint, the complainant and the person against whom the complaint is made must be given a written statement of the decision with reasons for the decision.

Solicitors Scheme requirements

5.4.14 Members of the NSW Law Society to whom the Solicitors Scheme applies are subject to the complaints and disciplinary system operating under Part 10 of the Legal Professions Act. This complaints and disciplinary system is applicable to all legal practitioners in general.

¹⁴⁸ Section 37(2) of the Professional Standards Act 1994.

5.4.15 Under Part 10 of the Legal Profession Act, complaints may be made in writing to the Legal Services Commissioner¹⁴⁹ or to the NSW Law Society Council against the professional misconduct and unsatisfactory professional conduct of a legal practitioner. A complainant may also make a complaint in connection with a consumer dispute.

5.4.16 After the Legal Services Commissioner or the NSW Law Society has completed the investigation of the complaint, proceedings must be instituted in the independent Administrative Decisions Tribunal¹⁵⁰ with respect to the complaint, if it is satisfied that there is a reasonable likelihood that the legal practitioner will be found guilty of professional misconduct or unsatisfactory professional conduct.¹⁵¹

Risks management strategies

Statutory requirements

5.4.17 When an occupational association seeks the approval of PSC for its professional standards scheme, it must furnish PSC with a detailed list of the risk management strategies intended to be implemented in respect of its members and the means by which those strategies are to be implemented.¹⁵² The means of implementation may be imposed as a condition of membership or otherwise.¹⁵³

Solicitors Scheme requirements

5.4.18 The centerpiece of the NSW Law Society's risk management strategies is the Risk Management Education Program. The programme is designed to assist practitioners in devising appropriate risk management and practice management systems delivered through a course programme covering communication skills, quality assurance, risk management and the like. The NSW Law Society also requires members to undertake practice management courses before they move from employed practitioners to sole practitioners or partners. Other risk management strategies adopted by the NSW Law Society include professional conduct and practice rules; guidelines to good practice; client care guidelines; surveys of practices and office procedures of firms.

¹⁴⁹ The Office of the Legal Services Commissioner oversees and participates in a co-regulatory disciplinary system with the NSW Law Society, the NSW Bar Association and the Department of Fair Trading (licensed conveyancers' professional body). It is a statutory body independent from the legal profession.

¹⁵⁰ The Tribunal is established under the Administrative Decisions Tribunal Act 1997 for the purposes of making decisions at first instance in relation to matters over which it is given jurisdiction by an enactment and reviewing decisions made by administrators.

¹⁵¹ Compensation (limited to AUS\$10,000 (HK\$57,300)) is only available from the Administrative Decisions Tribunal in cases where the solicitor has been found guilty of unsatisfactory professional conduct or professional misconduct and where the complainant has suffered a loss and cannot receive compensation from another source, for instance from the Professional Indemnity Insurance.

¹⁵² Section 36(1) of the Professional Standards Act 1994.

¹⁵³ Section 36(2) of the Professional Standards Act 1994.

5.5 Impact

Clients and other parties concerned

5.5.1 A recent report¹⁵⁴ discloses that the average size of professional indemnity claims settled across professions in 2003 was AUS\$21,713 (HK\$124,415), which was well below the AUS\$500,000 (HK\$2,865,000) statutory threshold. According to PSC, this survey shows that most claimants are fully compensated for damages and only corporate clients would experience limits on their claims against professions, but they have the capacity to self-insure and to manage risk. PSC is not aware of any large claim across professions that is above the limitation amount since the professional standards schemes commenced.¹⁵⁵

Solicitors

5.5.2 PSC is of the view that as the legal profession has a well-developed system of regulation before the commencement of the Solicitors Scheme, it is difficult to identify the direct impact of the Solicitors Scheme on legal practitioners and the legal profession of NSW as a whole.

5.5.3 Under State regulation, a NSW solicitor only needs AUS\$1.5 million (HK\$8.6 million) insurance cover, irrespective of the size of the law firm or the risk of the work. Therefore, under the Solicitors Scheme, some law firms have to take out more insurance to fit within the limited liability for the classes specified in the Solicitors Scheme. Nevertheless, PSC believes that, in capping the maximum civil liability of solicitors, the amount of insurance they have to pay is also indirectly capped. However, PSC has not collected data on whether the legal practices' insurance costs are reduced as a result of the Solicitors Scheme. PSC believes that there are many factors affecting claims, including economic conditions.

5.5.4 According to the annual report of PSC¹⁵⁶, the NSW Law Society reported that while claim notifications increased slightly in 2003-2004, they remained considerably below the 2000-2001 figures. During the reporting period, premiums for solicitors increased by 5% over the previous year.

¹⁵⁴ Australian Competition and Consumer Commission. (2004).

¹⁵⁵ Reply from the Professional Standards Council.

¹⁵⁶ Professional Standards Council. (2004).

Other professions

5.5.5 According to PSC, the impact of the professional standards schemes has been more dramatic for other occupations. For instance, insurance and continuing education which were not compulsory for some occupations are established after their respective professional standards scheme has been set up. PSC states that one of the impacts of the Professional Standards Act 1994 is that self-regulating occupations with professional standards schemes are more accountable to the community because they report to the community through their reports to PSC.

Chapter 6 - Analysis

6.1 Introduction

6.1.1 The concept of limited liability is widely recognized in the world of commerce. However, it has always been a subject of debate whether limited liability should be extended to professional practices in that the principle of joint and several liability has been regarded as one way to make professionals more accountable to clients. Nevertheless, more and more places have adopted or are considering the enactment of statutes enabling the formation of limited liability partnership (LLP).

6.1.2 The Standing Committee on Company Law Reform (SCCLR) of Hong Kong recommended in its twentieth annual report 2003-2004 that a consultation exercise should be conducted to seek the public's views on LLPs after further consultation and examination of the implications of the various issues arising from LLPs. Members of SCCLR considered that LLPs may not necessarily solve the problems relating to joint and several liability; however, it was a global trend that should be duly regarded. The Law Society of Hong Kong also floated the proposal of introducing LLPs to the legal profession in late 2004.

6.1.3 This analysis will first explore the nature of LLPs in England and Wales (UK) and the State of New York (NY). Secondly, this chapter will study various aspects of the operation of LLPs applicable to both the practice of law and other business, and the special rules, if any, for solicitors' LLPs. The LLP structure will then be compared to a different approach adopted by New South Wales (NSW) in addressing the concern of partners' liability in a general partnership. (See appendix I)

6.2 Nature of limited liability partnership

6.2.1 An LLP is a business structure combining the limited liability feature of a limited company and the flexibility of internal organization of a general partnership. The essence of LLPs in both the UK and NY is to render the privilege of limited liability to the innocent members/partners (members for LLPs in the UK and partners for LLPs in NY), so as to insulate members/partners' personal assets from claims incurred by the faults of others, without imposing all the stringent requirements of companies on LLPs.

6.2.2 LLPs in both the UK and NY have some other common features, including the requirement of at least two members/partners to form an LLP, the use of private agreement to govern the mutual rights and duties between members/partners, and being taxed as partnerships.

6.2.3 Nevertheless, the UK LLPs differ in various other ways from their NY counterparts. The UK LLPs have more in common with limited companies, and partnership law does not apply to them. A large number of provisions of the company and insolvency law apply to the UK LLPs protecting those parties who have dealings with them, with disclosure and winding up safeguards being at least up to the level required for limited companies.

6.2.4 The NY LLPs have more in common with general partnerships. There is no separate LLP legislation and the Partnership Law applies to the NY LLPs except for provisions stated to be otherwise.

6.2.5 In theory, members/partners of an LLP possess the advantage of limited liability. However, limited liability can be negated by bankers or clients requiring members/partners of an LLP to provide personal guarantees for bank loans or other transactions. In that event, any debts or liabilities may still be reclaimed from the personal assets of the members/partners of the LLP.

6.2.6 Instead of introducing LLPs, NSW has enacted a liability capping legislation, which enables the formation of professional standards schemes, requiring professionals to insure and implement risk management strategies in exchange for having their liability capped. Under these schemes, while professionals are still liable for each other's faults, their liability is capped at a specified level.

6.3 Eligibility

Types of business

Access to limited liability partnership and liability cap

6.3.1 The LLP option is open to all types of business in the UK. The UK government originally planned to restrict the LLP option to professionals only, but abandoned the restricted approach which was inconsistent with the law relating to companies where no such restriction was in place. In addition, the government considered it unfair for businesses excluded from LLP status to compete with those which enjoyed a commercial benefit brought by the LLP structure.

6.3.2 NY is one of the two states in the US which limit access to the LLP structure. Members of around 40 licensed professions may practise through LLPs in NY. Similarly, the liability capping option in NSW is limited to members of the occupational associations which have set up their own professional standards schemes.

Use of limited liability partnership and liability cap by solicitors

6.3.3 The Law Society of England and Wales allows its members to operate as LLPs. The Limited Liability Partnerships Act (LLPs Act) of the UK came into force in April 2001, and there were 215 law firms operating through LLPs in early 2005. In NY, lawyers are one of the licensed professionals authorized by the NY Partnership Law to form LLPs. An empirical study conducted in mid-2002 showed that 21% (or 1 113 firms) of NY's 5 202 law firms operated as LLPs.

6.3.4 The Law Society of New South Wales (NSW Law Society) is the first occupational association in NSW that has set up its own professional standards scheme – the Solicitors Professional Standards Scheme (Solicitors Scheme), which caps the liability of its members. There are 8 618 members of the NSW Law Society participating in the Solicitors Scheme.

Use of limited liability partnership and liability cap by other professions

6.3.5 The LLPs Act of the UK provides that "any two persons or more who carry on a lawful business with a view to profit" may form an LLP. Although the LLP option is open to all businesses, the requirement of "a lawful business" in the legislation leaves room for individual professions to determine whether their fellow professionals should be allowed to operate through LLPs.

6.3.6 There were 5 279 effective LLPs in the UK as at 31 March 2004, and the majority of them are operated by professions and businesses other than law firms. Professionals such as accountants, architects and doctors are allowed to operate through LLPs, whilst barristers are prohibited to do so.

6.3.7 In NY, apart from lawyers, around 40 occupations in the areas of health, architecture, engineering and the like are allowed to practise through LLPs. In NSW, apart from solicitors, seven other professional standards schemes for surveyors, engineers, accountants, barristers and valuers have been established since 1996.

Statutory requirements for establishing limited liability partnership or professional standards scheme

6.3.8 Both the UK and NY require two or more persons to form an LLP. A sole practitioner cannot have the privilege of limited liability through LLPs. In the UK, a member of an LLP can be an individual, an LLP or a company, whilst the NY law also allows a general partnership to be a partner of an LLP as far as each partner of the general partnership is either a licensed professional or a licensed professional firm. In NY, only partnerships but not individual professionals are eligible to register as an LLP. Both the UK and NY require registration for businesses intending to form an LLP.

6.3.9 The Professional Standards Act 1994 of NSW provides that only occupational associations may submit a professional standards scheme to the Professional Standards Council (PSC) for approval. The legislation requires PSC to publish a notice in a daily newspaper inviting comments on the proposed scheme.

6.3.10 A professional must be a member of an occupational association in order to be eligible for the relevant professional standards scheme. The occupational association may determine whether its professional standards scheme applies to all members or a specified class of persons.

Disqualification of members

6.3.11 The court in the UK has the power to disqualify a member of an LLP, whilst the court in NY does not have such power. Members of LLPs in the UK are subject to the same disqualifications and penalties that currently apply to company directors. In particular, the person acts in contravention of a disqualification order will be personally liable for all the relevant debts of the LLP concerned in the UK. In NY, the court may dissolve an LLP for reasons specified in the Partnership Law, e.g. if a partner has been declared incompetent in any judicial proceedings, or if any partner turns bankrupt.

6.3.12 In NSW, a person who is or is reasonably likely to be affected by the scheme published may apply to the Supreme Court for an order that the scheme is void. Either House of Parliament of NSW may also disapprove a proposed scheme. In addition, a professional standards scheme may be amended or revoked as a result of the review conducted on PSC's own initiative or by direction of the government. As to whether a particular person is disqualified from being covered by a professional standards scheme is a matter of his or her occupational association.

Legal professional body's requirements for practising through limited liability partnership

6.3.13 In both the UK and NY, a law firm in the form of an LLP must be owned and run by lawyers. In the UK, it is further required that a legal practice must also obtain recognition from the Law Society of England and Wales as a recognized body prior to its operating through an LLP. In addition, the Law Society of England and Wales requires that an LLP must also have at least one member who is "*qualified to supervise*".

6.3.14 The NSW Law Society provides that solicitors must hold a current practising certificate and have the benefit of an insurance policy not less than the required maximum amount of liability, so as to be eligible for the Solicitors Scheme.

6.4 Scope of liability limitation

Liability of limited liability partnership

6.4.1 In both the UK and NY, an LLP is liable for the wrongful acts and omission of its members/partners to the same extent as the members/partners so acting in the ordinary course of the business of the LLP. However, an LLP is not bound where a member/partner acts beyond his or her authority and the person with whom he or she is dealing knows that he or she does not have such authority.

6.4.2 Under the Solicitors Scheme of NSW, the liability of partners is capped at the level specified and they are fully liable for the firm's liability. Therefore, the liability of the partnership is indirectly capped as well.

Liability of individual members/partners

Liability for one's own wrongdoings

6.4.3 In all three places, solicitors are liable for the liabilities incurred by their own acts. Whilst the liability of solicitors arising from their own faults are unlimited in an LLP of UK and NY, solicitors of NSW under the Solicitors Scheme have their liability capped at the specified level.

Liability for other members/partners' wrongdoings

6.4.4 The LLP statutes in both the UK and NY aim at protecting members/partners of an LLP from being liable for each other's acts or omissions solely by virtue of being a member/partner of the LLP.

6.4.5 In NY, the Partnership Law expressly provides that a partner of an LLP is not liable directly or indirectly for all liabilities, whether arising in tort, contract or otherwise, solely by reason of being a partner of that LLP. It is described as a full shield against liability, in contrast with the partial shield adopted by some other states in the US, which do not protect partners from contract liabilities.

6.4.6 Instead of expressly conferring limited liability upon members of LLPs, the UK LLPs Act provides that an LLP is a separate legal person from its members, and hence separates the liability of the LLP from that of its members. The LLPs Act also states that members are agents of the LLP but not of each other. Therefore, individual members are not liable for each other's acts simply by virtue of being a member of the LLP, and liability is confined to the negligent member and the LLP.

6.4.7 In NSW, both tort and contract liabilities of a partner is capped at a level specified by the respective professional standards scheme. However, liability for damages arising from the death or injury to a person, a breach of trust, fraud and dishonesty are not capped¹⁵⁷. The liability capping legislation provides a blanket cover to all professionals under their respective professional standards schemes, no matter whether they have personal involvement in the wrongful act or not. Partners are still liable for each other's acts, but their liability and the wrongdoers' liability are both capped at a level specified in the professional standards scheme. Individual occupational associations may set the liability cap at a higher level than the statutory cap.

6.4.8 Broadly speaking, both LLPs and liability capping legislation intend to limit liability of members of a professional business. However, they have different focuses. Both the UK and NY employ LLPs in the hope of protecting the personal assets of innocent partners from being called on when the liability exceeds the assets of a partnership and the coverage of insurance policy for others' wrongdoings. On the other hand, the liability capping legislation aims at providing "*some guarantee of payment for the vast majority of claimants than to have a system of unlimited liability with no certainty of any payment*", and "*a fairer balance between professional risk and reward, one where professionals can obtain adequate insurance at reasonable cost*"¹⁵⁸. Therefore, it does not matter whether a partner is personally involved in the wrongful act or not.

Indirect liability by contribution

6.4.9 The LLPs Act of the UK has no provision on whether innocent members of an LLP may be compelled to contribute to make good losses of working capital after the LLP has satisfied a claim out of its capital. These payments are technically "*contributions*", but they are in fact indirect payments to satisfy a claim. In the UK, this issue of contribution is to be determined by the agreement reached among the members of the LLP. The NY Partnership Law, however, expressly provides that LLP partners are protected from indirect liability by way of contribution and indemnification. The Professional Standards Act 1994 of NSW has no provision on this issue.

¹⁵⁷ Liability that may be the subject of proceedings under Part 13 or 14 of the Real Property Act, which is related to a compensation scheme for losses in respect of land, is not capped as well.

¹⁵⁸ A letter from the President of the NSW Council of Professionals, quoted by Helen Sham-Ho, Member of the Legislative Council of NSW on 21 September 1994.

Liability for supervision

6.4.10 The Partnership Law of NY provides that each partner of an LLP is personally and fully liable for any negligent or wrongful act or misconduct committed by any person under his or her "*direct supervision and control*". In the UK, there is no statutory provision imposing such liability to the members of an LLP. Nonetheless, the Law Society of England and Wales warns that it is dangerous to assume that the LLP status protects solicitors from the consequences of "*negligent supervision of staff*". The Professional Standards Act 1994 of NSW has no provision on this issue.

Liability in the winding up of limited liability partnership

6.4.11 Unlike a general partnership, the members/partners of an LLP in both the UK and NY are not obliged to contribute anything upon its winding up when the liquidator seeks contribution to enforce third party claims.

6.4.12 However, there are two exceptions in the UK. Firstly, in the event of the winding up of an LLP, past and present members contribute to the assets of the LLP only to the extent that they have agreed and they are not obliged to agree to contribute anything. Secondly, on the application of the liquidator, withdrawals of the LLP's properties made by a member during the two years prior to the commencement of winding up may be subject to clawback, if it is proved that at the time of the withdrawal, the member knew or had reasonable grounds for believing that the LLP was, or would be unable to pay its debts. The Professional Standards Act 1994 of NSW has no provision on this issue.

6.5 Safeguards

6.5.1 Among the three places studied, the LLP legislation in the UK offers more measures to safeguard the interests of clients and the public. These measures are provided in the Companies Act and the Insolvency Act and apply to LLPs with appropriate modifications, with the view of maintaining equal treatment between directors of companies and members of LLPs. These statutory safeguards have two main objectives:

- (a) preserving the LLP assets which can be claimed by third parties; and
- (b) requiring the LLP to disclose sufficient information so that third parties are fully informed as to the limited liability and the financial viability of the business with which they are dealing.

6.5.2 The safeguards imposed by the NY legislation emphasize the disclosure of non-financial information, but have no measure to preserve the LLP assets. The NSW liability capping legislation promotes greater self-regulation, through the complaints system and risk management, to improve the standard of professional services and protect the interests of the public.

6.5.3 Apart from the statutory safeguards which are applicable to all LLPs and all professional standards schemes, the Law Society of England and Wales and the NSW Law Society also impose their own insurance and disclosure requirements on their members respectively.

Insurance

6.5.4 In both the UK and NY, there is no compulsory insurance requirement in their respective LLP statutes. In contrast, the Professional Standards Act 1994 in NSW requires professionals to insure in exchange for having their liability capped. The legislation provides that an occupational association may compel its members to hold insurance under a professional standards scheme.

6.5.5 The Law Society of England and Wales has its own rules on insurance. Before solicitors (or registered European lawyers) can practise through an LLP in the UK, the LLP must obtain recognition from the Law Society of England and Wales as a "*recognized body*", by taking out a minimum qualifying insurance for the LLP and a compulsory top-up insurance in that clients or third parties may have limited assets against which to claim.

6.5.6 The NY State Bar Association does not have any insurance requirement on LLPs or its partners. The Solicitors Scheme of NSW requires that a solicitor must have the benefit of insurance for an amount not less than his or her limited liability.

Disclosure of limited liability status

6.5.7 Both the UK and NY statutes require that the name of an LLP must contain the words "*limited liability partnership*" or various forms of its abbreviation. The NY law further requires that within 120 days after the effective date of the registration of an LLP, a copy of the items in the application for registration or a copy of a notice containing those items has to be published in newspapers. The UK law does not require a publication of notice, but it specifies the types of documents and correspondence to carry the LLP's full corporate name and its particulars.

6.5.8 Similarly, the Professional Standards Act 1994 of NSW requires a person whose occupational liability is capped to notify that fact on all documents given to a client or prospective client by carrying the statement "*Liability limited by a scheme approved under Professional Standards Legislation.*"

6.5.9 For solicitors' LLPs in the UK, the Law Society of England and Wales has its own disclosure rules. An LLP's notepaper must include the words "*regulated by the Law Society*" and a list of the members or a statement that the list is open to inspection at the office. It is also required that where a partnership converts to an LLP, the law firm has to notify its clients, either before the change or soon afterwards. In NY, there is no duty for a law firm to inform its clients about the change in its liability status, although it is customary to do so.

Disclosure of non-financial information

6.5.10 Both the UK and NY statutes require LLPs to submit regular reports of non-financial information. In the UK, an LLP has to deliver to the Registrar of Companies successive annual returns containing the address of the registered office of the LLP, the names and usual addresses of the members of the LLP and other particulars. Failure of filing will result in a fine. In NY, LLPs are required to submit a non-financial statement every five years. If the statement is not timely filed, the Department of State may revoke the registration of the LLP.

6.5.11 In NSW, the NSW Law Society and other occupational associations have to provide an annual report to PSC as to the implementation and monitoring of its risk management strategies, the effect of these strategies and any changes made or proposed to be made. PSC also requires insurance information to be included in the annual report.

6.5.12 Apart from regular reports, the Law Society of England and Wales requires a law firm operating as an LLP to notify the Society about the registered office and practising addresses of the LLP, the names and professional qualifications of all members of the LLP, and all subsequent changes. The NY State Bar Association does not have such requirements.

Disclosure of financial information

6.5.13 The UK is the only place studied that applies the accounting and auditing requirements for companies to LLPs, including solicitors' LLPs. An LLP is required to keep proper accounting records for three years, and send the annual accounts with the auditors' report to every member of the LLP and file with the Registrar of Companies. LLPs qualified as small and medium-sized LLPs may prepare and deliver abbreviated accounts to the Registrar of Companies. The auditing requirement is also exempted if both the turnover and balance sheet total are less than the specified amounts. Both NY and NSW do not impose any financial disclosure requirement.

Preservation of assets in the course of winding up

6.5.14 The LLPs Act of the UK provides that on the application of the liquidator, withdrawals made by an LLP member during the two years prior to the commencement of winding up may be subject to clawback if it is proved that at the time of the withdrawal, the member knew or had reasonable grounds for believing that the LLP was, or would be unable to pay its debts. There is no similar provision in the NY and NSW statutes.

Complaints and disciplinary systems

6.5.15 Both the UK and NY statutes do not require LLPs to adopt any particular complaints and disciplinary system. Both the Law Society of England and Wales and the NY State Bar Association do not have a separate set of complaints and disciplinary rules for lawyers practising through LLPs either. In contrast, the Professional Standards Act 1994 of NSW provides a Model Code of complaints and discipline as default rules. Occupational associations may establish their own complaints and disciplinary systems. For instance, the NSW Law Society has its own complaints and disciplinary system.

Risk management strategies

6.5.16 In NSW, an occupational association must include a detailed list of risk management strategies and the means by which these strategies are to be implemented in its proposal to establish a professional standards scheme. Under the Solicitors Scheme, the NSW Law Society operates a Risk Management Education Program. The UK and NY statutes do not require LLPs, including solicitors' LLPs, to have particular risk management strategies.

6.6 Impact

Impact on clients and third parties concerned

6.6.1 Both the Law Society of England and Wales and the NY State Bar Association opine that lawyers practising through LLPs do not have any impact on the number of claims, in the sense that the limited liability status of a law firm does not affect its liability or the availability of the firm's assets to pay a debt. Therefore, it makes no difference to clients and third parties in respect of making claims against law firms, whether they operate as LLPs or not. However, the Law Society of England and Wales also states that the ability of the claimant to get his or her claim fully paid may be affected by limitation of liability. For instance, if a claim exceeds the firm's insurance cover and the LLP's assets are exhausted, the claimant cannot claim against the personal assets of individual lawyers of that LLP.

6.6.2 In NSW, PSC is of the view that the ability of the claimant to get his or her claim fully paid is largely unaffected. It quotes a recent survey across professions that most claimants are fully compensated for damages and only corporate clients might experience limits on their claims against professions, but they have the capacity to self-insure and manage risk. PSC is not aware of any large claim across professions that is above the limitation amount since the professional standards scheme commenced.

Impact on legal practices

6.6.3 For legal practices in the UK and NY, the limited liability status through LLPs does not change the need for insurance to protect their own assets since they remain liable for their own faults. The Law Society of England and Wales believes that the premium for LLPs is likely to be higher than that for general partnerships because it is more difficult to enforce payment of the final premium when an LLP fails. In addition, solicitors' LLPs in the UK have to take out a higher insurance cover than sole practitioners and general partnerships. In practice, the difference in the amount of insurance cover may not exist, as large law firms, regardless of their business structures, all have vast top-up cover on a purely voluntary basis.

6.6.4 Similarly, some law firms in NSW whose partners are under the liability capping scheme have to take out more insurance to fit within the Solicitors Scheme.

6.6.5 Among the three places studied, the LLP legislation in the UK imposes the most stringent financial reporting requirement. The Law Society of England and Wales is of the view that this public filing of financial information will accelerate the breaking down of the culture of secrecy about law firms' financial affairs.

6.6.6 In NSW, as the legal profession had had a well-developed system of regulation before the commencement of the Solicitors Scheme, PSC finds it difficult to identify the direct impact of the Solicitors Scheme on legal practitioners and the legal profession of NSW as a whole. PSC believes that the impact of the professional standards schemes has been more dramatic for other occupations. For instance, insurance and continuing education, which were not compulsory for some occupations, are established after their respective professional standards schemes have been set up.

Appendix I

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Eligibility			
Is the limited liability partnership (LLP) structure/liability capping legislation available to all types of business?	<ul style="list-style-type: none"> • Yes, but individual profession can determine if their members can operate through LLPs or not. 	<ul style="list-style-type: none"> • No, it is limited to around 40 licensed professionals, including lawyers, accountants and licensed physicians. 	No, liability capping is limited to members of the occupational associations which have set up their own professional standards schemes and got approved by the Professional Standards Council (PSC).
Statutory requirements for establishing an LLP or a professional liability scheme	<ul style="list-style-type: none"> • There must be two or more persons. • The business has to be a lawful business. • An LLP must become incorporated by registration with the Registrar of Companies. One of the proposed members must sign a statement of compliance that the persons named in the form are associated for carrying on a lawful business with a view to profit. 	<ul style="list-style-type: none"> • There must be two or more persons. • The licensed professionals have to form a general partnership before applying for registration. • The partnership has to file with the Division of Corporations of the Department of State a registration which sets forth the name of the LLP and other particulars. A certified copy of the registration has to be filed with the licensing authority within 30 days. 	<ul style="list-style-type: none"> • Only an occupational association may set up a professional standards scheme. Before approval, PSC must publish a notice in a daily newspaper explaining the nature of the scheme, and inviting comments. • The Attorney General, the court or either House of Parliament may disapprove the scheme.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Eligibility (cont'd)			
Legal professional body's requirements for allowing a law firm to operate through an LLP	<ul style="list-style-type: none"> The law firm must obtain recognition from the Law Society of England and Wales as a recognized body, which must comply with the requirements of professional conduct and the Solicitors' Incorporated Practice Rules 2004 and ensure its members to do so. The Law Society of England and Wales may, by discretion, refuse an application if: <ul style="list-style-type: none"> (a) it is not satisfied that a member of the law firm is a suitable person to be engaged in the direction or ownership of an LLP; or (b) it considers that it is proper in the public interest not to recognize the body. 	The ownership of the LLP is restricted to those individuals and entities authorized to practise law in the State of New York (NY).	Not applicable.
Statutory requirements for being a member/partner of an LLP or for participating in the Professional Standards Scheme	A member can be an individual, an LLP, or a company.	<ul style="list-style-type: none"> A partner can be an individual, a general partnership or LLP, or a company. Each partner must be a licensed professional or a licensed professional firm. 	<ul style="list-style-type: none"> A professional must be a member of an occupational association. A professional standards scheme may provide that it applies to all persons or to a specified class of persons within an occupational association, except for those apply to be exempted. Each member must have the benefit of an insurance policy against occupational liability and/or business assets of value not less than the maximum amount of liability specified in a professional standards scheme.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Eligibility (cont'd)			
Legal professional body's requirements for being a member/partner of an LLP or for a member to be covered by the Solicitors Professional Standards Scheme (Solicitors Scheme)	<ul style="list-style-type: none"> The only persons who may be members of a law firm operating as an LLP are: <ol style="list-style-type: none"> individual solicitors with a practising certificate or an European/foreign lawyer permitted under the Law Society of England and Wales' rules; a company/an LLP which is a recognized body and has at least one director/member who is a solicitor or a registered European lawyer (REL); and A European corporate practice. An LLP must have at least one member who is "qualified to supervise". 	Partners must be individuals or entities authorized to practise law in NY.	<ul style="list-style-type: none"> The Solicitors Scheme is applicable to all members of the Law Society of New South Wales who are: <ol style="list-style-type: none"> holding a current practising certificate; and having the benefit of an insurance policy under which the amount payable is not less than the required maximum amount of liability specified in the Solicitors Scheme. Member may apply for exemption from the Solicitors Scheme.
Does the court have any authority to disqualify a member/partner of an LLP, or revoke a professional standards scheme?	<ul style="list-style-type: none"> Yes, members of LLPs are subject to the same disqualification rules and penalties that apply to company directors. Undischarged bankrupts are automatically disqualified. There are a number of grounds where the court is authorized to issue a disqualification order for a specified period of time. If a person acts in contravention of a disqualification order, he or she is not only guilty of a criminal offence, but also personally liable for all the relevant debts of the LLP. 	No, the court does not have any power to disqualify a partner of an LLP, but it may order the dissolution of an LLP.	<ul style="list-style-type: none"> Yes, a person who is or is reasonably likely to be affected by a professional standards scheme may apply to the Supreme Court for an order that the scheme is void. PSC may review the operation of a professional standards scheme. The concerned professional standards scheme may be amended or revoked as a result of the review.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Scope of liability limitation			
Is an LLP a separate legal entity?	Yes.	It is not expressly stated in the legislation. The NY State Bar Association is of the view that an LLP has a separate legal personality from its partners.	Not applicable.
Liability of an LLP/a law firm under the Solicitors Scheme in general	<ul style="list-style-type: none"> An LLP is liable to the same extent as a member who has incurred liabilities as a result of his or her wrongful act or omission in the course of the business of the LLP or with its authority. An LLP is not bound where a member acts beyond his or her authority and the third party knows that he or she has no authority to act, or the third party does not know or believe him or her to be a member of the LLP. 	<ul style="list-style-type: none"> An LLP is liable to the same extent as a partner who has caused loss or injury of a third party, or incurred penalty by his or her wrongful act or omission in the ordinary course of the business of the LLP, or with the authority of his or her co-partners. An LLP is not bound if a partner so acting has no authority to act for the partnership in the particular matter, and the person with whom he or she is dealing has knowledge of the fact that he or she has no such authority. 	<ul style="list-style-type: none"> A law firm which runs as a general partnership has its liability capped because its partners' liability is capped under the Solicitors Scheme.
Are members/partners of an LLP, or those under a professional standards scheme liable for their own wrongful acts or omissions?	Yes.	Yes.	Yes, but their liabilities are capped at the level specified in the professional standards scheme.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Scope of liability limitation(cont'd)			
Are the members/partners of an LLP, or the participants of the Solicitors Scheme liable for the acts or omissions of each other solely by virtue of being a member/partner of the firm?	<ul style="list-style-type: none"> • No. • The Limited Liability Partnerships Act 2000 (LLPs Act) does not expressly confer limited liability upon members of LLPs. As an LLP is a separate legal person from its members, liability is confined to the LLP itself and the liability of individual members is separated from that of the LLP. • As members are agents of the LLP and not of each other, individual members will not be liable for each other's acts simply by virtue of being a member of the LLP. 	<ul style="list-style-type: none"> • No, a partner of an LLP is not liable directly or indirectly (by way of indemnification or contribution) for liabilities arising in tort, contract or otherwise, solely by reason of being a partner of that LLP. • Under the NY statute, if a majority of partners in an LLP agree, all or specified partners may be liable in their capacity as partners for all or specified debts, obligations or liabilities of the LLP. 	<ul style="list-style-type: none"> • Yes. • Statutory requirements are: <ul style="list-style-type: none"> (a) The partners of a general partnership are liable for the acts and omissions of each other even if the professional standards scheme is applicable to them, albeit the level of their liability is capped. (b) The professional standards schemes cap civil liability arising in tort, contract or otherwise, directly or vicariously from anything done or omitted by a member of the occupational association in the performance of his or her occupation. (c) The capping of liability does not apply to liability for damages arising from death or personal injury to a person, a breach of trust, fraud or dishonesty, and liability which may be the subject of proceedings under Part 13 or 14 of the Real Property Act 1900. • Solicitors Scheme requirements are: <ul style="list-style-type: none"> (a) The level of the capped liability is determined by the number of principals in the firm.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Scope of liability limitation (cont'd)			
Do members/partners of an LLP bear liability indirectly by way of contribution or indemnification?	<ul style="list-style-type: none"> The LLP legislation has no provision on this point. It is determined by the members' agreement. 	No, the legislation expressly provides that LLP partners are protected from indirect liability <i>"by way of indemnification, contribution or otherwise"</i> for claims.	Not applicable.
Are members/partners required to contribute to the assets of an LLP to satisfy third party claims in the winding up of the LLP?	<ul style="list-style-type: none"> Members only have to contribute to the extent that they have agreed in the event of an LLP being wound up and they are not obliged to agree to contribute anything. If it is proved that a member of an LLP has withdrawn properties of the LLP during the two years prior to the commencement of the winding up of the LLP, knowing or had reasonable grounds for believing that the LLP was, or would be unable to pay its debts, the member may have to pay back those withdrawals as the court thinks proper. 	No, the Partnership Law exempts partners of LLPs from contributing the amount necessary to satisfy the liabilities in the event of the winding up of an LLP.	Not applicable.
Is a member/partner of an LLP liable for the acts or omissions of persons under his or her direct supervision?	<ul style="list-style-type: none"> There is no statutory provision that directly imposes such liability to the members of an LLP. The Law Society of England and Wales' guideline states that it is dangerous to assume that the LLP status will protect solicitors from the consequences of <i>"negligent supervision of staff"</i>. The Law Society of England and Wales explains that a member of an LLP would not automatically be responsible in law for that happening. It depends on the circumstances and whether a duty of care and actual negligence could be demonstrated. 	Yes, each partner is personally and fully liable for <i>"any negligent or wrongful act or misconduct"</i> committed by any person <i>"under his or her direct supervision and control"</i> while rendering professional services on behalf of the LLP.	Not applicable.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Safeguards			
Is there any statutory requirement for compulsory insurance?	No, there is no compulsory insurance requirement in the LLPs Act.	No, there is no statutory insurance requirement for LLPs.	<ul style="list-style-type: none"> Yes, each professional standards scheme requires professionals to hold insurance against occupational liability and the insurance policy must comply with the standards determined by the occupational association.
Does the legal professional body impose any requirement for compulsory insurance cover?	<ul style="list-style-type: none"> Yes, before one applies to the Law Society of England and Wales for recognition as an LLP, one must arrange to have a minimum qualifying insurance for the LLP, which is the same amount required for sole practitioners and general partnerships. In addition, an LLP must have top-up insurance, which is compulsory for LLPs only. 	No, there is no compulsory insurance requirement on LLPs or its partners.	<ul style="list-style-type: none"> Yes, under the Solicitors Scheme, a solicitor must have the benefit of insurance for an amount not less than his or her limited liability. The insurance policy must cover all civil liability arising in connection with the solicitors' practice.
Is it a statutory requirement that the name of the law firm must disclose its limited liability partnership status?	Yes, the name of an LLP must end with the expression " <i>limited liability partnership</i> ", or the abbreviation " <i>llp</i> " or " <i>LLP</i> ".	Yes, the name of each registered LLP must contain the words " <i>Registered Limited Liability Partnership</i> " or " <i>Limited Liability Partnership</i> " or the abbreviations " <i>R.L.L.P.</i> ", " <i>RLLP</i> ", " <i>L.L.P.</i> " or " <i>LLP</i> ".	Not applicable.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Safeguards (cont'd)			
Statutory disclosure requirements regarding the limited liability status/liability capped status	<ul style="list-style-type: none"> An LLP is required to paint or affix its name on the outside of every office or place in which its business is carried on, in a conspicuous position and in letters reasonably legible. An LLP must put its full corporate name on its business correspondence. An LLP must also put its registered number, place of registration, address of its registered office and the fact that it is an LLP (if its name is not spelled out in full) on its business letters and order forms. If an LLP uses a trading name, it must put its full corporate name, principal place of business and a list of the LLP's members (or, where there are more than 20 members, a statement that the list is open to inspection) on its business letters and other documents. 	<p>Within 120 days after the effective date of the registration of an LLP, a copy of the items in the application of registration or a copy of a notice containing those items has to be published in two newspapers once in each week for six successive weeks. The newspapers must be published in the county in NY in which the principal office of the registered LLP is located.</p>	<ul style="list-style-type: none"> The Professional Standards Act 1994 requires a person whose occupational liability is limited to notify that fact on all documents given to a client or prospective client by carrying the statement "<i>Liability limited by a scheme approved under Professional Standards Legislation.</i>" The size of the disclosure statement is also specified in the regulations. PSC has further issued a policy statement guiding participants of the professional standards schemes on the kinds of documents where the disclosure statement should appear.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Safeguards (cont'd)			
Legal professional body's disclosure requirements regarding the limited liability status/liability capped status	<ul style="list-style-type: none"> Under section 2 of the Solicitors' Publicity Code 2001, the LLP's notepaper must include: <ol style="list-style-type: none"> the words "<i>regulated by the Law Society</i>"; and either a list of the members or a statement that the list is open to inspection. "<i>The Guidance to the Professional Conduct of Solicitors (1999)</i>" requires that where a partnership converts to an LLP, the law firm has to notify its clients, either before the change or soon afterwards. 	The NY State Bar Association does not impose any duty on a law firm to inform its clients individually that it has converted from a general partnership into an LLP, although it is customary to do so.	Same as the statutory disclosure requirements.
Non-financial reporting	<ul style="list-style-type: none"> An LLP has to deliver to the Registrar of Companies successive annual returns four weeks before the anniversary of the incorporation of the LLP. The annual return has to contain, inter alia, the followings: <ol style="list-style-type: none"> the address of the registered office of the LLP; and the names and usual residential addresses of the members of the LLP, and the names of those members who are designated members. If an LLP fails to deliver an annual return in time, the LLP and its designated members are guilty of an offence and liable on summary conviction to a fine. The registered office and practising addresses of the LLP, the names and professional qualifications of all members of the LLP, and all subsequent changes have to be notified to the Law Society of England and Wales. 	<ul style="list-style-type: none"> Each LLP has to, within 60 days prior to the fifth anniversary of the effective date of its registration and every five years thereafter, furnish a statement to the Department of State setting forth, inter alia, the followings: <ol style="list-style-type: none"> the name of the LLP; the address of the principal office of the LLP; and a statement that it is eligible to register as an LLP. If the statement is not timely filed, the Department of State may proclaim that the registration to be revoked 60 days after mailing to the LLP a notice of the failure to file the statement. The NY State Bar Association does not require law firms operating through LLPs to file any annual report or update the changes in names of partners or other particulars with the Association. 	The NSW Law Society and other occupational associations subject to a professional standards scheme have to provide an annual report to PSC as to the implementation and monitoring of its risk management strategies, the effect of these strategies and any changes made or proposed to be made.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Safeguards (cont'd)			
Statutory requirements on financial reporting	<ul style="list-style-type: none"> • LLPs are subject to accounting and auditing requirements similar to those for companies. • It is a statutory requirement that an LLP has a duty to keep proper accounting records for three years. The annual accounts and the auditor's report must be sent to every member of the LLP and filed with the Registrar of Companies. • LLPs qualified as small and medium-sized LLPs may prepare and deliver abbreviated accounts to the Registrar of Companies. The auditing requirement may also be exempted if the turnover and balance sheet total are less than the specified amounts. 	<ul style="list-style-type: none"> • The NY Partnership Law does not impose any financial disclosure requirement on LLPs. 	Neither the Professional Standards Act 1994 nor the Solicitors Scheme imposes any financial disclosure requirement upon the professionals who participate in the Solicitors Scheme or other professional standards schemes.
Preservation of the legal practices' assets in the course of winding up	On the application of the liquidator, a member of an LLP may have to pay back withdrawals made during the two years prior to the commencement of the winding up if it is proved that at the time of the withdrawal, the member knew or had reasonable grounds for believing that the LLP was, or would be unable to pay its debts.	There is no statutory provision to claw back the capital withdrawn by partners of an LLP while the business is or is about to become insolvent.	Not applicable.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Safeguards (cont'd)			
Is there any statutory requirement for LLPs or participants of professional standards schemes to establish a particular complaints and disciplinary system?	No.	<ul style="list-style-type: none"> The NY Partnership Law provides that businesses operating through LLPs, other than those authorized to practise law, must be under the supervision of the Regents of the University of the State of New York. These LLPs are subject to disciplinary proceedings and penalties in the same manner and to the same extent as are provided with respect to individuals and their licences relating to the applicable profession. The Appellate Division of the New York State Supreme Court regulates and disciplines lawyers in NY, whether they practise through LLPs or not. 	Yes, the Professional Standards Act 1994 provides a Model Code of complaints and disciplinary matters in Schedule 1 as default rules. Occupational associations may set up their own complaints and disciplinary systems as well. The NSW Law Society has its own complaints and disciplinary system under Part 10 of the Legal Professions Act.
Does LLP legislation or liability capping legislation require any risk management strategies to be adopted by LLPs or participants of professional standards schemes?	No.	No.	<ul style="list-style-type: none"> Yes. Statutory requirement is: An occupational association must have a detailed list of the risk management strategies and the means by which those strategies are to be implemented. Solicitors Scheme requirement is: The NSW Law Society operates a Risk Management Education Program, which is designed to assist practitioners in devising appropriate risk management and practice management systems.

Appendix I (cont'd)

Comparison of the various attributes of the limited liability partnership and liability capping legislation in selected places

	The United Kingdom	The State of New York	The State of New South Wales
Impact			
Impact of the use of LLPs/ Solicitors Scheme by the legal practices on clients and third parties concerned	<p>The Law Society of England and Wales' views:</p> <ul style="list-style-type: none"> • Since the liability of LLPs is backed by compulsory insurance and the Solicitors' Compensation Fund as for general partnerships, it makes no difference to clients and third parties in respect of making claims against a law firm, whether it operates through an LLP or not. • However, the ability of the claimant to get fully paid may be affected because, if a claim exceeds the firm's insurance cover and the LLP's assets are exhausted, the claimant cannot claim against the personal assets of individual lawyers of that LLP. 	<p>The NY State Bar Association's views:</p> <ul style="list-style-type: none"> • The limited liability status of a law firm does not affect its liability or the availability of its assets to pay a debt. It has no such information on the impact of law firms practising as LLPs on their clients. 	<p>PSC's views:</p> <ul style="list-style-type: none"> • It is not aware of any large claim across professions that is above the limitation amount since the introduction of professional standards schemes. • A recent survey shows that most claimants are fully compensated for damages and only corporate clients might experience limits on their claims against professions, but they have the capacity to self-insure and manage risk.
Impact of the use of LLPs/ Solicitors Scheme by the legal practices on solicitors and law firms	<p>The Law Society of England and Wales' views:</p> <ul style="list-style-type: none"> • The insurance premium for an LLP is not lower than that for a general partnership because the risk to the LLP itself (and hence to the insurer) is no less. Instead, it believes that the premium is likely to be higher because an insurer would be more difficult to enforce payment of the final premium when the LLP fails. • The statutory requirement to file financial information will accelerate the breaking down of the culture of secrecy about law firms' financial affairs. 	<p>The NY State Bar Association's views:</p> <ul style="list-style-type: none"> • It has no such information on the impact of law firms practising as LLPs on the firms and the solicitors themselves. The limited liability status of a law firm does not change its need for insurance to protect its own assets. In the case of a partner of an LLP, he or she still needs to protect himself or herself for those claims to which the limited liability status is not applicable. 	<p>PSC's views:</p> <ul style="list-style-type: none"> • As the legal profession has a well-developed system of regulation before the commencement of the Solicitors Scheme, it is difficult to identify the direct impact of the Solicitors Scheme on legal practitioners and the legal profession of NSW as a whole. • Some law firms have to take out more insurance to fit within the Solicitors Scheme. • PSC has not collected data on whether the insurance costs are reduced as a result of the Solicitors Scheme.

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