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Partnerships: Provide for Formation of Domestic Limited Liability Partnerships

The Act allows for formation of limited liability partnerships in Georgia. A partner in a limited liability partnership will not be derivatively liable for the acts or omissions of a partner or the acts or omissions of the limited liability partnership. The Act requires a partnership that desires limited liability status to file an election in every county in which it has an office. Additionally, the limited liability partnership is required to indicate its limited liability status through one of three options enumerated in the Act. The Act also affects foreign limited liability partnerships, domestic limited partnerships, foreign limited partnerships, limited liability companies, and foreign limited liability companies.

Effective Date: July 1, 1995

History

The Georgia General Assembly has been very active in recent years in the area of partnerships and corporations. For example,

1. In 1984, Georgia adopted the Uniform Partnership Act. ENCYCLOPEDIA OF GEORGIA LAW, Partnership § 2 (1990). Four years later, Georgia adopted a new limited partnership statute, the Georgia Revised Uniform Limited...
in 1994, the General Assembly regulated limited liability partnerships (LLPs) created under the laws of sister states. This legislation was enacted in response to the growing minority of states embracing LLPs. This growing trend is the result of derivative liability which flows from normal partnership arrangements.

The defining characteristic of a partnership is that a partner is liable jointly and severally for the wrongful acts of his or her partners that occur “in the ordinary course of business.” The result is that partners may be personally liable for an act they did not commit or of which they were unaware. Understandably,
this liability consequence has become an increasing concern to professionals who utilize partnerships.8

Due to these liability concerns, states, including Georgia, have enacted legislation authorizing the formation of limited liability companies (LLCs).9 In LLCs, the owners “are not personally liable for the liabilities and obligations of the entity.”10 Even though LLCs afford greater liability protection than partnerships, professionals in Georgia continue to utilize partnerships because they are reluctant to operate in an incorporated entity.11 There are two primary factors that explain this reluctance. First, partnerships are less “administratively burdensome” than LLCs.12 Second, professionals have continued to operate in the framework of partnerships because “professionals have long cherished the financial reward and status of ‘making partner.’”13 To allow professionals to operate in a partnership without the attendant liability problems, the Georgia General Assembly passed HB 563.14

HB 563

By passing the Act,15 Georgia has joined a growing minority

8. See McKnight, supra note 6, at 6.
13. Id.
14. Chambless Interview, supra note 11.
15. HB 563 had no substantive changes made in the House Judiciary Committee and was passed with limited changes made to the bill as introduced. Compare HB 563, as introduced, 1995 Ga. Gen. Assem. with HB
of states that allow for the formation of LLPs. In addition to creating LLPs, the Act modifies the laws relating to partnerships, foreign LLPs, limited partnerships (LPs), foreign LPs, and domestic and foreign LLCs.

**Limited Liability Partnerships**

The Act expressly includes LLPs in the definition of partnerships. As a result, LLPs are governed to the same extent as partnerships, except in the areas of liability and formation. Even though LLPs and partnerships vary in only a few areas, the differences are significant.

Unless an LLP agreement provides to the contrary, a partner in an LLP is not individually liable for the misdeeds of the partnership or a partner regardless of the cause of action the aggrieved party pursues. This blanket exemption from derivative liability makes the Act broader than other states' LLP statutes.

As a result of this broad exemption from derivative liability, most professionals who operate in an LLP need not worry about being liable for another partner's malpractice. However, lawyers may still be liable for the malpractice of their partners because of the Georgia Supreme Court's decision in *First Bank & Trust Co. v. Zagoria.* Consequently, lawyers may not be able to

17. O.C.G.A. § 14-8-6(a) (Supp. 1995).
20. Some states eliminate liability only when the other partner's liability is the result of "negligence, wrongful acts or misconduct, whether characterized as tort, contract or otherwise." BROMBERG & RIBSTEIN, *supra* note 3, at § 5.11 (citing DEL. CODE ANN. tit. 6, § 1515(b) (1994)). Georgia's statute is similar to the New York statute on LLPs because, like Georgia, New York "eliminates all liability, and not merely liability for co-partner negligence." BROMBERG & RIBSTEIN, *supra* note 3, at § 5.11.
22. 302 S.E.2d 674 (Ga. 1983). In Zagoria, the Georgia Supreme Court held that it is unconstitutional for the Georgia General Assembly to impose "regulations upon the practice of law" because the Georgia Supreme Court "has the authority and in fact the duty to regulate the law practice." *Id.* at 675. As a result, the court held that enactment of the professional corporation statute by the legislature could not affect legal liability which flows from "malpractice or obligations incurred because of a breach of a
fully enjoy the freedom from derivative liability encompassed in the Act.

Code section 14-8-15(b), however, only relates to derivative liability; the Act makes clear that partners in LLPs continue to be personally liable for their own acts or omissions.\(^{23}\) Furthermore, because the LLP is regulated as a partnership, the partnership is liable for the omissions and acts of the partner even though other partners are not individually liable.\(^{24}\)

The elimination of derivative liability appears in other sections of the Act. The Act states that a partner in an LLP does not have to pay partner or partnership losses governed by Code section 14-8-15(b).\(^{25}\) Additionally, the Act expressly exempts a partner in an LLP from liability for obligations that arise when a co-partner continues acting for the partnership after the LLP has been dissolved.\(^{26}\) Furthermore, the Act prevents the estate of a
duty to a client.” \textit{Id.} After establishing that the Georgia Supreme Court was the only branch of government that could limit or modify lawyer liability, the court held that “when a lawyer holds himself out as a member of a law firm the lawyer will be liable not only for his own professional misdeeds but also for those of the other members of his firm.” \textit{Id.} at 676. This holding should prevent lawyers operating in an LLP from enjoying blanket immunity from derivative liability because the court stated that this holding is applicable to partnerships as well as professional corporations. \textit{Id.}

Not surprisingly, the Act was drafted with the assumption that the Georgia Supreme Court regulates lawyers and legal liability and that the passage of the Act would not free lawyers from derivative malpractice liability. Telephone Interview with Robert P. Bryant, Chair, Partnership Subcommittee of the Corporate and Banking Section of the State Bar of Georgia (May 23, 1995) [hereinafter Bryant Interview]. The Partnership Subcommittee of the Corporate and Banking Section of the State Bar of Georgia drafted HB 563. \textit{Id.} As a result of the Act not relieving lawyers from derivative malpractice liability, the State Bar of Georgia has proposed to the Georgia Supreme Court an ethical rule relieving lawyers from derivative malpractice liability. \textit{Id.} The prospects for the acceptance of this proposal may be minimal if the sentiments of the Georgia Supreme Court have not changed since \textit{Zagoria:} a “client has the right to expect the fidelity of other members of the firm. It is inappropriate for the lawyer to be able to play hide-and-seek in the shadows and folds of the corporate veil and thus escape the responsibilities of professionalism.” \textit{Zagoria}, 302 S.E.2d at 675.

24. Chambless Interview, supra note 11.
deceased partner in an LLP from being derivatively liable for the debts of the partnership, which are exempt under Code section 14-8-15.27

**Formation of LLPs**

Under the Act, an LLP must record its LLP election in the superior court clerk's office of every county in which the partnership has an office.28 The LLP election must state the name of the partnership, the business in which the partnership is planning to engage, a statement that the partnership intends to be an LLP, and a statement that the election to be an LLP has been "duly authorized."29 The Act specifies that the partnership becomes an LLP at the time the election is recorded or at the date or time specified in the election.30 Even though the information required in the election statement may subsequently change, the status of the LLP will not be affected.31

The LLP election has to be executed by a majority of the partners or by "one or more partners authorized to execute an election," unless the partnership agrees otherwise.32 The partnership continues to be an LLP until a cancellation notice is recorded in the superior court clerk's office in every county in which the partnership has an office.33 The Act specifies that the cancellation must be executed in the same manner as the election.34

Interestingly, a partnership can become an LLP through a process other than election. The Act allows a partnership to become an LLP by succeeding to the status of another LLP.35 Under Code section 14-8-62, if an LLP dissolves but its business is continued by a new partnership, the new partnership acquires

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27. Bryant Interview, supra note 22 (citing O.C.G.A. § 14-8-36 (Supp. 1995)).
29. Id. § 14-8-62(a)(1)-(4). The Act also allows an LLP to include any other matters the partners choose to include in the election. Id. § 14-8-62(a)(5).
30. Id. § 14-8-62(c).
31. Id. § 14-8-62(d).
32. Id. § 14-8-62(b).
33. Id. § 14-8-62(c).
34. Id. § 14-8-62(c)(1)-(2).
35. Id. § 14-8-62(f).
the dissolved partnership's LLP status, provided that the old partnership's business affairs were not liquidated. The new partnership retains this LLP status until it is cancelled.

The Act requires a partnership operating as an LLP to signal that it is an LLP. The LLP can accomplish this by using one of the following three options after the firm's name: the words "limited liability partnership," the abbreviation "L.L.P.,” or the designation "LLP."

The Act clarifies the General Assembly's intent that domestic LLPs be recognized outside of Georgia. Additionally, the Act emphasizes that it is Georgia's policy that "internal affairs," including liability, be governed by Georgia law.

**Partnerships**

The Act changes the liability language in Code section 14-8-15. Under prior law, a partner in a general partnership was jointly and severally liable for all debts and obligations of the partnership. Under the new law, the partner is jointly and severally liable for liabilities as well as debts and obligations. However, this change does not broaden the liability of a partner.

36. Id.
37. Id.
38. Id. § 14-8-63.
39. Id.
40. Id. § 14-8-64(a).
41. Id. § 14-8-64(b).
42. Compare id. § 14-8-15(a) with 1984 Ga. Laws 1439 (formerly found at O.C.G.A. § 14-8-15 (1994)).
44. O.C.G.A. § 14-8-15(a) (Supp. 1995).
45. Chambless Interview, supra note 11. The "liabilities" language was included as a synonym for debts and obligations and does not constitute a separate category of partner responsibility. Bryant Interview, supra note 22. The "liabilities" language was added in order to bring the language of O.C.G.A. § 14-8-15(a) in conformity with the language of O.C.G.A. § 14-8-15(b). Bryant Interview, supra note 22. "[A] partner in a limited liability partnership is not individually liable . . . for any debts, obligations, or liabilities . . . ." O.C.G.A. § 14-8-15(b) (Supp. 1995).
Foreign LLPs

Under the Act, a foreign LLP no longer has to certify that it has capital accounts or liability insurance in the amount of one million dollars to register to do business in Georgia.46 Similarly, the Act no longer conditions applicability of foreign law to foreign LLPs on the basis of the foreign LLP having the requisite one million dollars in capital accounts or liability insurance.47

As is the case with domestic LLPs, the Act gives foreign LLPs the option of utilizing the designation “LLP” as the means by which to signal that the partnership is an LLP.48 Prior to the Act, a foreign LLP had to use either the words “limited liability partnership” or the abbreviation “L.L.P.”49

Limited Partnerships

The Act affects the liabilities and duties of a partner in an LP.50 The Act provides that partners in an LP will not be liable to the LP or the partners in the LP if they rely in good faith on a provision in the partnership agreement.51 The Act also allows

47. Compare O.C.G.A. § 14-8-45(a) (Supp. 1995) with 1994 Ga. Laws 1674 (formerly found at O.C.G.A. § 14-8-45(a)(9) (1994)). The liability insurance requirement was eliminated because the Subcommittee decided that the operation of domestic LLPs in Georgia should not be conditioned on acquiring liability insurance. Bryant Interview, supra note 22. As a result, the Subcommittee decided that foreign LLPs should not be required to acquire liability insurance. Bryant Interview, supra note 22. The Subcommittee decided against requiring domestic LLPs to carry liability insurance because no other business entity in Georgia is required to do so. Bryant Interview, supra note 22.
50. See 1952 Ga. Laws 375 (codified at O.C.G.A. § 14-9A-2 (1994)). A LP should not be confused with an LLP. To be an LP in Georgia, the partnership must have at least one general partner and one limited partner. Id. There is no such requirement for LLPs. See O.C.G.A. § 14-8-62(a)-(f) (Supp. 1995). Although limited partners in LLPs “are not personally liable for the liabilities and obligations of the entity,” Chambless Interview, supra note 11, the general partner in an LP has the same liabilities as a partner in a regular partnership. 1952 Ga. Laws 375 (codified at O.C.G.A. § 14-9A-70 (Supp. 1994)).
the duties and liabilities of a partner in an LP that exist in law or in equity to be modified by the partnership agreement.\footnote{52} However, the Act provides that the partnership agreement cannot limit or eliminate a partner's liability if it arises out of one of the following transactions: intentional misconduct, a knowing violation of the law, or a breach of any provision of the partnership agreement that results in the breaching partner securing a personal benefit.\footnote{53} These are the same transactions for which the LP cannot indemnify a partner.\footnote{54}

The Act also adds to the merger laws related to LPs. Under Code section 14-9-206.1(g), a foreign corporation or a foreign LLC that is authorized to transact business in Georgia does not need to obtain a certificate of withdrawal from the state if it merges with and into a domestic LP, provided that the foreign corporation or the foreign LLC does not survive the merger.\footnote{55}

\textit{Foreign LPs}

Prior to the Act, a foreign LP had to register with the Secretary of State if it transacted business in Georgia.\footnote{56} The Act does not affect this requirement;\footnote{57} however, it changes and adds to the illustrative list of activities that do not constitute transacting business.\footnote{58} The Act adds that mere ownership of property does not constitute transacting business.\footnote{59} Additionally, the Act expands and combines two of the prior exceptions.\footnote{60} Consequently, the ownership or control of an entity\footnote{61} organized in Georgia or transacting business in Georgia does not constitute

\footnote{52} Id. § 14-9-108(b)(1).
\footnote{53} Id.
\footnote{54} Id. § 14-9-108(a)(1)-(2). This provision retains the language of the prior law. \textit{Compare id. with} 1988 Ga. Laws 1016 (formerly found at O.C.G.A. § 14-9-108(1)-(2) (1994)).
\footnote{55} O.C.G.A. § 14-9-206.1(g) (Supp. 1995).
\footnote{56} 1988 Ga. Laws 1016 (formerly found at O.C.G.A. § 14-9-902 (1994)).
\footnote{58} See id.
\footnote{59} Id. § 14-9-902(b)(9).
\footnote{60} \textit{Compare id.} § 14-9-902(b)(13) with 1988 Ga. Laws 1016 (formerly found at O.C.G.A. § 14-9-902(b)(10)-(11) (1994)).
\footnote{61} The Code uses the term "person," which is defined as including "a natural person, partnership, limited liability partnership, limited partnership (domestic or foreign), trust, estate, association, or corporation." 1994 Ga. Laws 1674 (codified at O.C.G.A. § 14-8-2(7) (1994)).
transacting business, regardless of whether the control or ownership is direct or indirect.62

Limited Liability Companies

Under prior law, members of an LLC managed by two or more members had no duties to the LLC merely by acting in their official capacities, provided that the members were not also managers.63 Under the Act, a member in the aforementioned situation may have duties to the LLC if the duties are set forth in the LLC operating agreement or the articles of organization.64

Prior to the Act, a member or manager was allowed to rely on financial data or similar data detailed in Code section 14-11-305, if the data was prepared or presented by persons believed to be reliable and competent.65 The Act, however, provides that the member or manager cannot rely on this information if the member or manager has knowledge that makes reliance unwarranted.66

The Act also affects distributions in LLCs. Under the Act and prior law, members who become dissociated with LLCs are entitled to receive fair value for their interests, provided that the members' dissociations did not cause the LLCs to dissolve and certain exceptions are not present.67 The Act changes the exceptions.68 Consequently, the member is not entitled to compensation if the member's dissociation is voluntary, the member assigns the entire interest in the LLC, or the LLC purchases or redeems the member's interest in the LLC.69

The Act makes voluntary dissociation an exception in another context.70 Under the old law, an LLC dissolved when a member

63. 1993 Ga. Laws 123, § 1 (formerly found at O.C.G.A. § 14-11-305(1) (1994)).
64. O.C.G.A. § 14-11-305(1) (Supp. 1995).
70. Voluntary dissociation was changed in both contexts for estate and gift tax purposes. Bryant Interview, supra note 22.
voluntarily dissociated himself from the company unless the partners in the LLC elected, within ninety days of the dissociation, to continue operations.71 Under the Act, a voluntary dissociation will not trigger dissolution.72

The Act also changes the merger laws involving LLCs.73 Under the Act, an LLC may now merge with or into a corporation.74

**Foreign LLCs**

The changes the Act makes in the area of foreign LLCs mirror changes made in the area of foreign LPs. As is the case with foreign LPs, the Act adds to the illustrative list of activities in which a foreign LLC may engage without having to register with the Secretary of State.75 The Act states that owning property, by itself, is not considered transacting business in Georgia.76 Additionally, the Act expands an activity enumerated in the old law.77 As a result, a foreign LLC does not transact business in Georgia by merely owning or controlling a "person"78 transacting business in Georgia or organized under Georgia laws, regardless of whether the control or ownership is direct or indirect.79

Furthermore, the foreign LLC merger law in Code section 14-11-905(d) is similar to the law governing foreign LP mergers.80 The Act provides that a foreign business, authorized to do business in Georgia, does not need to withdraw when the foreign business merges with an LLC, provided that the foreign business is not the surviving entity.81

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73. Compare id. § 14-11-901(a) with 1993 Ga. Laws 123 (formerly found at O.C.G.A. § 14-11-901(a) (1994)).
78. See supra note 61 for the statutory definition of “person.”
80. Compare id. § 14-9-206.1(g) with id. § 14-11-905(d).
81. Id. § 14-11-905(d).