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WHAT KIND OF PARTNER ARE YOU?

Liability of Texas Partners Depends Upon the Form of Partnership

In Texas, there are several different types of entities that physician's groups, healthcare providers, medical suppliers, physician investors, urgent care centers and other types of medical providers may choose from when structuring their business. Many of them decide on the partnership form. The choice of partnership entity that is made in the initial planning phases of a venture can have enormous implications on an individual partner's responsibility to answer for certain debts and obligations of the venture. This article will describe the three main forms of partnerships common in Texas and an individual partner's liability to third parties with respect to the chosen form of partnership.

Common Partnerships Recognized in Texas

The three main types of partnerships in Texas are: 1) the General Partnership; 2) the Limited Liability Partnership; and 3) the Limited Partnership. Other considerations aside, the liability that an individual partner may face can be a stark and significant factor in determining how best to structure one's business.

The General Partnership ("GP")

One of the simplest forms of business entities is the general partnership. Two or more persons are necessary to form a general partnership and the partnership may be easily established by either written or oral agreement between the partners. Of course, while written partnership agreements are always a prudent and recommended solution to govern a general partnership, Texas law makes it clear that they are not necessary to create a general partnership. Partners are not required to make any filings with any governmental entity to make their general partnership effective.

The Limited Liability Partnership ("LLP")

The limited liability partnership is a creation of state law and requires a filing or registration to be made with the Texas Secretary of State to establish its existence. As such, a limited liability partnership is either a (i) general partnership that has registered with the Texas Secretary of State to become a limited liability partnership or (ii) a limited partnership that has registered with the Texas Secretary of State as a limited liability partnership (known as a limited liability partnership and a limited partnership). In addition to an initial application to register the partnership as a limited liability partnership, which is effective for a one year period, the entity must, in order to maintain its LLP status, renew its registration

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with the Texas Secretary of State on an annual basis *and* maintain at least \$100,000 of liability insurance or provide \$100,000 of its own funds (cash, CD, letter of credit or bond) in a designated and segregated account as “self insurance” for potential claims for error, omission, negligence, incompetence or malfeasance.¹ Each initial and renewal applications for the LLP registration must be accompanied with a \$200 per partner filing fee. The payment of this annual fee and the timely registration of the partnership are important steps to maintain for the continued protection that an LLP affords its partners.

Limited Partnership (“LP”)

The limited partnership, like the limited liability partnership, is also a creation of state law and requires a filing or registration to be made with the Texas Secretary of State to establish its existence, and the payment of a one-time filing fee of \$750. The limited partnership, unlike the LLP, has two classifications of partners: general partners and limited partners. General partners are involved in the management and operation of the partnership, while limited partners are not.

Liability of Partners

Under Texas law, partners in a general partnership are jointly and severally liable for all debts and obligations of the GP.² Since partners in a general partnership have the ability to act on behalf of and bind the partnership, all partners can be held liable for all acts and obligations of all other partners in the GP. For individual partners, this joint and several liability has the effect of exposing such individual’s personal assets to creditors of the partnership regardless of fault or knowledge of such partner. Because of these unlimited liability characteristics, general partnerships are not an attractive option and are not favored by businesses.

An alternative to a general partnership is to form a limited liability partnership by establishing and maintaining an effective registration with the Texas Secretary of State. A partner in a limited liability partnership will not be personally liable for a debt or obligation of the partnership *unless* such a partner (i) was supervising or directing a partner or representative of the LLP when an error, omission, negligence, incompetence, or malfeasance was committed by the supervised partner or representative of the LLP; (ii) was directly involved in the specific activity in which the error, omission, negligence, incompetence or malfeasance was committed by the other partner or representative of the LLP; or (iii) had notice or knowledge of the error, omission, negligence,

¹ Tex. Bus. Orgs. Code §§152.802 (e) & 152.804 (2006)

² Tex. Bus. Orgs. Code §152.304 (2006)

incompetence or malfeasance and failed to take reasonable action to cure it.³ In other words, a partner in an LLP who is not responsible for an action or inaction that gives rise to a claim *and* has no knowledge of such action or inaction will not be personally liable for such claim. An LLP gives its partners incrementally more liability protection than partners in a general partnership enjoy and can be well worth the time and energy that it takes to register and maintain the LLP status.

Lastly, at the pinnacle of liability limiting protection for partners is the limited partnership. In a word, the key to the favorable status that is afforded to limited partners is “passive.” Limited partners normally are not liable to third parties for obligations of the limited partnership. However, this general rule has exceptions. A limited partner who is also a general partner of the limited partnership or exercises control over the partnership other than its rights as a limited partner, can become liable for the debts and obligations of the limited partnership.⁴ Therefore, it is very important that limited partners only participate in the business of the limited partnership to the extent set forth in the LP’s agreement of limited partnership. Additionally, limited partners should consult with their legal counsel and consider the breadth and scope of participation that is required of limited partners by an LP’s constituent documents so as not to run afoul of the “passive” nature that is intended for limited partnership interests, and the corresponding freedom from liability of partnership debts and obligations.

The form of partnership as well as the extent of involvement of an individual partner will determine his or her personal liability for the debts and obligations of the partnership. Owners or operators should give careful consideration to these liability and other issues before embarking on a venture. There are many advantages to the partnership form, and utilizing the right strategies and techniques can allow partners to manage many of the downside risks. Potential partners are encouraged to know and understand their relative rights, responsibilities and options before becoming a partner in any business, as differing situations offer unique perspectives and considerations. Do you know what kind of partner you are?

³ Tex. Bus. Orgs. Code §152.801(2006)

⁴ Tex. Bus. Orgs. Code §153.102 (2006)