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Christine M. Przybysz

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SHIELDED BEYOND STATE LIMITS: EXAMINING CONFLICT-OF-LAW ISSUES IN LIMITED LIABILITY PARTNERSHIPS

After Enron Corp.'s demise, accounting firm Arthur Andersen braced itself for potentially crushing liability stemming from its role in the energy corporation's collapse.¹ Since Enron's bankruptcy, Arthur Andersen has been convicted of criminal charges² and currently faces civil claims in an estimated amount of one billion dollars.³ The civil cases pending against Arthur Andersen worry many partners within the accounting firm, as they wonder how much liability, if any, they will have to shoulder personally.⁴ One bright spot for Arthur Andersen's partners is that the firm was formed as a limited liability partnership. The LLP business form limits the personal liability of partners.⁵ However, the LLP structure remains untested in a number of ways. One of the biggest questions facing Arthur Andersen is whether the LLP's liability protections will be recognized or whether the court will pierce the liability shield to assign personal liability to the partners.⁶

¹ Anthony Lin, *After Enron, Firms Rethink Partnership*, 227 N.Y. L.J. 1, 1 (2002). See generally Deborah L. Rhode & Paul D. Paton, *Lawyers, Ethics, and Enron*, 8 STAN. J.L. BUS. & FIN. 9 (2002), for factual background of the Enron scandal.

² See Kurt Eichenwald, *Arthur Andersen Guilty, Accounting Firm Announces It Is Going out of Business*, PITTSBURGH POST-GAZETTE, June 16, 2002, at A1; see also Ken Brown et al., *Andersen Fires Partner It Says Led Shredding of Documents*, WALL ST. J., Oct. 25, 2002, at A1 (describing some of the actions that led to criminal charges against Arthur Andersen for destruction of documents).

³ Susan Saab Fortney, *High Drama and Hindsight: The LLP Shield, Post-Andersen*, BUS. L. TODAY, Jan.-Feb. 2003, at 46, 47.

⁴ Mitchell Pacelle & Ianthe Jeanne Dugan, *Partners Forever? Within Andersen, Personal Liability May Bring Ruin*, WALL ST. J., Apr. 2, 2002, at C1.

⁵ In contrast to LLPs, partners in a general partnership are personally liable for all debts and obligations of the partnership. See generally UNIF. P'SHIP ACT § 15 (1914) (providing that a partner is jointly liable for all obligations of the partnership and severally liable for wrongful acts); cf. REVISED UNIF. P'SHIP ACT §§ 306, 307 (1997) (providing that partners are jointly and severally liable for all of the partnership's obligations, but the assets of the partnership must be inadequate or exhausted before relief can be sought from the partners).

⁶ Fortney, *supra* note 3, at 47.

This is just one of many questions raised by the Arthur Andersen case. A choice-of-law question exists as well. Arthur Andersen was organized under Illinois law, which limits personal liability of partners only for tort claims.⁷ The civil cases are pending in federal district court in Texas, which grants broad protection to partners in LLPs for all obligations whether arising from tort or contract claims.⁸ This poses the question as to which state's liability shield will be recognized. This Note focuses on this choice-of-law question as it relates to LLPs in general, and will seek to answer which jurisdiction's law should apply to regulate the liability of partners within an LLP.

Limited liability partnerships are recent creations in the realm of business associations. The first limited liability partnerships appeared around a decade ago, in the early 1990s. The newness of this business association is important; because LLPs have not been in existence for long, there has not been time or opportunity to develop much case law dealing with this business form.⁹ This means that there are many questions and uncertainties regarding the LLP form. Uncertainties also exist because of the inconsistent manner in which LLP statutes were adopted. Within ten years, all fifty states had adopted some form of an LLP provision.¹⁰ But the laws were not uniform in the extent of liability protection afforded to partners.¹¹ The early LLP statutes created narrow protections for partners in LLPs. These so-called "narrow-shield" statutes protected partners against vicarious liability only for malpractice or tort claims. As the LLP form spread in popularity, the liability shield expanded. Later statutes, known as "broad-shield" statutes, protected partners from contract liability in addition to tort liability. The trend has been for states to adopt a broad-shield type provision. However, almost one-third of the states still retain a narrow-shield provision.¹²

⁷ 805 ILL. COMP. STAT. ANN. 205/15 (West 1993). This provision has been amended to now provide liability protection from all debts and obligations, whether arising from tort or contract. See 805 ILL. COMP. STAT. ANN. 206/306 (West Supp. 2003) (effective Jan. 1, 2003). However, the amendment provision is not retroactive and does not cover partnerships organized before January 1, 2003. 805 ILL. COMP. STAT. ANN. 205/90 (West 1993 & Supp. 2003).

⁸ TEX. REV. CIV. STAT. ANN. art. 6132b, § 3.08 (Vernon Supp. 2003).

⁹ Alan R. Bromberg and Larry E. Ribstein cite the "novelty problem" surrounding LLPs. Because LLPs are novel business associations in comparison to corporations and partnerships, there is an absence of accepted customs and a paucity of case law to address uncertainties and questions that may arise. ALAN R. BROMBERG & LARRY E. RIBSTEIN, LIMITED LIABILITY PARTNERSHIPS AND THE REVISED UNIFORM PARTNERSHIP ACT § 1.07(a)(17) (2001).

¹⁰ See Elaine A. Welle, *When Are Limited Liability Partnership Interests Securities?*, 27 J. CORP. L. 63, 63 (2001) (noting that by 2001 every state permitted the formation of LLPs).

¹¹ See Carol J. Miller, *LLPs: How Limited Is Limited Liability?*, 53 J. MO. B. 154, 154 (1997) (listing five levels of varying degrees of liability protection).

¹² Currently, thirteen states still have narrow-shield liability provisions. These include

This difference in liability provisions may or may not be significant. The courts have not yet answered such questions as what would happen when an LLP formed in a broad-shield state is sued in a narrow-shield jurisdiction. Would the LLP's broad-shield protection be recognized, or would the partners' vicarious liability be judged under the more narrow statute? Similarly, would partners of an LLP formed in a narrow-shield jurisdiction be granted the protections of a broad-shield state if sued in that state?¹³ LLP statutes generally contain choice-of-law provisions, which answer these questions by applying the law of the state of organization.¹⁴ But these provisions have not yet been tested in court. Will these provisions be recognized? If not, what state's law should apply? Where should the court look for guidance if it should decide to look beyond a choice-of-law provision?

In attempting to answer these questions, this Note examines state LLP statutes and their liability and choice-of-law provisions. The choice-of-law question is also examined under a traditional conflict-of-law analysis. The end result shows that courts should recognize statutory choice-of-law provisions. The analysis also shows that if a court looks beyond a state's choice-of-law provision, the outcome would still be the same under conflict-of-law theories.¹⁵ Therefore, this Note demonstrates that the liability shield provided for by the state of formation governs the liability of partners in any jurisdiction.

Kentucky, Louisiana, Maine, Michigan, Nevada, New Hampshire, North Carolina, Ohio, Pennsylvania, South Carolina, Tennessee, Utah, and West Virginia. KY. REV. STAT. ANN. § 362.220 (Banks-Baldwin 2002); LA. REV. STAT. ANN. § 9:3431 (West 1997); ME. REV. STAT. ANN. tit. 31, § 295 (West Supp. 2002); MICH. COMP. LAWS ANN. § 449.46 (West 2002); NEV. REV. STAT. ANN. 87.150 (Michie 1999); N.H. REV. STAT. ANN. § 304-A:15 (Supp. 2002); N.C. GEN. STAT. § 59-45 (2001); OHIO REV. CODE ANN. § 1775.14 (Anderson 2002); 15 PA. CONS. STAT. ANN. § 8204 (West 1995 & Supp. 2003); S.C. CODE ANN. § 33-41-370 (Law Co-op. 1990 & Supp. 2002); TENN. CODE ANN. § 61-1-306 (2002); UTAH CODE ANN. § 48-1-12 (2002); W. VA. CODE ANN. § 47B-3-6 (Michie 1999 & Supp. 2003).

¹³ While the choice-of-law question applies to LLPs formed in broad-shield states and narrow-shield states alike, the potential consequences for each are different. Partners in an LLP formed in a broad-shield state face potentially damaging risks if the broad-shield is not recognized in every jurisdiction. In contrast, partners in narrow-shield LLPs would receive the benefit of additional liability protection if the narrow-shield was not recognized in broad-shield states.

¹⁴ See Stephen M. Brusini & Stephen D. Zubiago, *Crossing the Border: The Use of Limited Liability Partnerships in Interstate Commerce*, R.I. B.J., Apr. 1999, at 9, 42 (commenting that choice-of-law provisions in LLP statutes is an area of uniformity among the states).

¹⁵ Cf. *infra* Part I.D. (discussing choice-of-law provisions in LLP statutes and noting that most provisions provide that the law of the state of formation should apply in all cases).

I. LIMITED LIABILITY PARTNERSHIP STATUTES

A. *The Birth of Limited Liability Partnerships*

In order to better understand the dichotomy between broad-shield and narrow-shield LLP provisions, the limited liability partnership form itself must be put into context. The history of how the limited liability partnership first developed is helpful in comprehending the split between jurisdictions and why it exists.

The limited liability partnership first appeared in Texas in 1991.¹⁶ The arrival of the limited liability partnership was a direct result of the savings and loan crisis.¹⁷ The widespread failure of the savings and loan institutions in the late 1980s and early 1990s led to numerous lawsuits against shareholders, directors, and officers of the failed financial institutions. The amounts recovered from these suits were insufficient to cover the actual financial losses suffered.¹⁸ As a result, claims were filed against the lawyers and accountants who were closely involved with these institutions.

Claims against law and accounting firms were attractive because the firms generally had substantial malpractice insurance and many wealthy partners from whom money could be recovered.¹⁹ These lawsuits affected a large proportion of the law firms and accounting firms in Texas.²⁰ Many of these law firms and accounting firms were organized as general partnerships. As a result, the lawsuits put all of the partners at peril, even those who did not do any savings and loan work.²¹ "The[se] suits highlighted the vicarious liability of partners for each other's conduct, a liability that did not exist in other forms of professional organization."²²

The result of this experience was an amendment to Texas' Uniform Partnership Act that limited partners' joint and several

¹⁶ BROMBERG & RIBSTEIN, *supra* note 9, § 1.01(a).

¹⁷ See generally M. Mazen Anbari, *Banking on a Bailout: Directors' and Officers' Liability Insurance Policy Exclusions in the Context of the Savings and Loan Crisis*, 141 U. PA. L. REV. 547 (1992), for background on the savings and loan crisis, and B. Seth Bailey, *Chopping at the Roots: A Proposal to Change the Focus of Criminal Laws Dealing with Savings and Loan Fraud*, 24 AM. J. CRIM. L. 401, 405 (1997), for a discussion of the foundations leading to the savings and loan failures.

¹⁸ Robert W. Hamilton, *Registered Limited Liability Partnerships: Present at the Birth (Nearly)*, 66 U. COLO. L. REV. 1065, 1069-71 (1995) (discussing the birth of limited liability partnerships in Texas after the savings and loan crisis).

¹⁹ *Id.* at 1069; Patrick Cammarata, *Allowing Attorneys to Swing for the Fences: The Massachusetts Limited Liability Partnership Act*, 38 B.C. L. REV. 949, 954 (1997) (noting that the suits against the law firms involved in the savings and loan crisis allowed plaintiffs to recoup under multi-million dollar insurance policies and firm assets).

²⁰ Hamilton, *supra* note 18.

²¹ Brusini & Zubiago, *supra* note 14, at 9; see *supra* note 5.

²² BROMBERG & RIBSTEIN, *supra* note 9, § 1.01(a), at 3.

liability.²³ The amendment passed and was supported by professional firms that wanted limited liability but disliked incorporation for tax, professional tradition, or other reasons.²⁴ The new LLP law was popular; within two years of its passage, almost 600 Texas law firms had organized as limited liability partnerships.²⁵

B. Development of the Broad-Shield, Narrow-Shield Divide

The original Texas LLP statute was very narrow in its application and protections. First, the LLP form was only available for a short list of professional partnerships, such as doctors, accountants, and attorneys.²⁶ Second, it limited liability only for tort-based claims arising from errors, omissions, negligence, or malfeasance of other partners.²⁷ It did not extend to protect partners from vicarious liability for wrongful acts of partners that they supervised, nor for debts or obligations arising from other causes.²⁸

Other states soon followed in Texas' footsteps but passed broader limited liability statutes. A second generation of LLP statutes protected partners from liability for "debts and obligations" but continued to link the liability protection to claims arising from tort negligence and wrongful acts.²⁹ Finally, a third generation of statutes appeared, protecting partners from personal liability for all debts and obligations of the partnership whether they arose from a tort or from a contract.³⁰

The second-generation statutes represent narrow-shield LLP provisions, which are still in effect in one-third of the states.³¹

²³ Cammarata, *supra* note 19, at 954 (noting that this amendment was initiated by three Texas attorneys).

²⁴ BROMBERG & RIBSTEIN, *supra* note 9, § 1.01(a); *see also* Carol R. Goforth, *Limited Liability Partnerships: The Newest Game in Town*, 1997 ARK. L. NOTES 25 (noting that some of the same reasons for selecting the LLP form exist today).

²⁵ BROMBERG & RIBSTEIN, *supra* note 9, § 1.01(a), at 6 n.7.

²⁶ *Id.* § 1.01(a).

²⁷ Carol R. Goforth, *Limiting the Liability of General Partners in LLPs: An Analysis of Statutory Alternatives*, 75 OR. L. REV. 1139, 1147; *see* TEX. REV. CIV. STAT. ANN. art. 6132b, § 3.08 (LEXIS through 1994 Supp.), *amended by* TEX. REV. CIV. STAT. ANN. art. 6132b, § 3.08 (Vernon Supp. 2003).

²⁸ Miller, *supra* note 11, at 154-55 (discussing Texas' first limited liability partnership statute).

²⁹ *Id.* at 155 (describing the "second generation" as statutes passed after 1993). An example of a second generation statute is Louisiana's LLP provision, which allowed partners protection from malpractice and tort claims, including willful and intentional misconduct. *See* LA. REV. STAT. ANN. § 9:3431 (LEXIS through 1994 Supp.), *amended by* LA. REV. STAT. ANN. § 9:3431 (West 1997).

³⁰ Miller, *supra* note 11, at 155. New York and Minnesota were the first states to enact LLP provisions protecting partners from tort liability and contract liability. However, *see* BROMBERG & RIBSTEIN, *supra* note 9, § 1.01(c), for an interesting discussion about differences between the New York and Minnesota statutes showing how Minnesota's provision was even broader than New York's.

³¹ *See supra* note 12 and accompanying text (listing states with such provisions).

These statutes protect partners only from tort liability, leaving partners unprotected from liability for contract claims.³² An example of a narrow-shield provision is Ohio's LLP statute, which provides that a partner in an LLP is "not liable, directly or indirectly . . . for debts, obligations, or other liabilities of any kind . . . arising from negligence or from wrongful acts, errors, omissions, or misconduct, whether or not intentional or characterized as tort, contract, or otherwise."³³ Despite any apparent ambiguity in the language that may lead one to believe that this statute protects partners from contract liability, the statute does not reach that far. The statute's language is only meant to cover the type of misconduct or negligence that could also breach a contract, so that tort claims are protected no matter how they may be characterized in court.³⁴

In contrast, broad-shield provisions protect partners from contract liability as well as tort liability. Missouri's broad-shield provision states that a partner is not "directly or indirectly [liable] for any debts, obligations and liabilities of, or chargeable to, the partnership or each other, whether in tort, contract or otherwise."³⁵ In spite of this broad protection from vicarious liability, partners are still liable for debts and obligations arising from their own negligence, as they are in narrow-shield states.³⁶

The differences among liability shields do not end with the broad-shield and narrow-shield classification. Even within these two categories, there are varying degrees of liability protection.³⁷ However, it is this split between broad-shield and narrow-shield jurisdictions that gives rise to the choice-of-law question at hand. The question is whether an LLP's liability shield as provided by its

³² See Brusini & Zubiago, *supra* note 14, at 10 (discussing Rhode Island's LLP provision and the fact that it protects partners from only one type of liability). The result of such a statute is that partners may remain jointly liable for partnership obligations arising from contracts. *Id.* This is similar to the liability partners in a general partnership face. See sources cited *supra* note 5.

³³ OHIO REV. CODE ANN. § 1775.14(B) (Anderson 2002); see also Brusini & Zubiago, *supra* note 14, at 10 (analyzing Rhode Island's statute, which is similar to Ohio's, and characterizing it as a narrow-shield provision).

³⁴ BROMBERG & RIBSTEIN, *supra* note 9, § 1.01(b), at 11 n.18 (commenting on the 1994 version of Delaware's LLP provision, which contained language similar to Ohio's current statute).

³⁵ MO. ANN. STAT. § 358-150 (West 2000 & Supp. 2003); see Brusini & Zubiago, *supra* note 14, at 9, 10 (discussing the characteristics and language of broad-shield statutes).

³⁶ Miller, *supra* note 11, at 155-56. Some states also provide that partners are still liable for wrongdoing by other partners under their direct supervision and control. Only a few states have eliminated partner liability for supervisory-based vicarious liability. *Id.* at 156; see also MO. ANN. STAT. § 358-150 (West 2000 & Supp. 2003) (maintaining partner liability for a partner's own acts or for misconduct of any person under the partner's direct supervision and control).

³⁷ Miller, *supra* note 11, at 154.

state of organization would be recognized in a jurisdiction with a contrasting liability shield. Most LLP statutes contain a choice-of-law provision.³⁸ But LLP statutes, including their choice-of-law provisions, have not been challenged in court. The outcome of the choice-of-law question remains to be seen.

C. Limited Liability Theories in LLPs

The trend among states is to provide for a broad-shield.³⁹ But the split among broad-shield and narrow-shield jurisdictions may remain for some time. Not all states may adopt a broad-shield as the choice regarding how much liability protection to provide partners in an LLP is guided by a number of theoretical underpinnings.⁴⁰

One such theoretical consideration supports the danger tort liability poses to a partnership's existence. The reason both narrow-shield and broad-shield statutes provide limited liability protection for tort obligations is that tort claims can create potentially disastrous liability.⁴¹ Partners in a general partnership may face overwhelming liability for uncontrollable events.⁴² This liability may leave the partnership and all the individual partners facing huge punitive damages because of the tortious conduct of one partner.⁴³ Furthermore, it may be hard for partners to control the negligent or tortious conduct of other partners. Often, there is little a partner can do to prevent another partner from creating liabilities. As such, imposing vicarious personal liability does not act to encourage partners to act in the best interests of creditors or clients.⁴⁴ Moreover, imposing vicarious liability for torts can impose costs

³⁸ See *supra* note 14 and accompanying text.

³⁹ BROMBERG & RIBSTEIN, *supra* note 9, § 1.01(c) (stating that two-thirds of the states have enacted broad-shield provisions).

⁴⁰ The discussion in this Note is limited to theories underlying limited liability in LLPs. For a brief overview of theories underlying the general concept of limited liability, see Rebecca J. Huss, *Revamping Veil Piercing for All Limited Liability Entities: Forcing the Common Law Doctrine into the Statutory Age*, 70 U. CIN. L. REV. 95, 103-09 (2001).

⁴¹ BROMBERG & RIBSTEIN, *supra* note 9, § 3.02.

⁴² See UNIF. P'SHIP ACT § 15 (1914) (providing that a partner is jointly liable for all obligations of the partnership and severally liable for wrongful acts); *cf.* REVISED UNIF. P'SHIP ACT §§ 306, 307 (1997) (providing that partners are jointly and severally liable for all of the partnership's obligations, but the assets of the partnership must be inadequate or exhausted before relief can be sought from the partners).

⁴³ See *supra* notes 19-22 and accompanying text (discussing the liability general partners faced in the aftermath of the savings and loan scandal); see also Fortney, *supra* note 3, at 47 ("The situation the Andersen partners . . . face is the very type of catastrophe that the LLP structure was intended to address – the risk of personal liability when the firm's assets and insurance are wholly inadequate to satisfy claims.").

⁴⁴ BROMBERG & RIBSTEIN, *supra* note 9, § 3.02 (stating that partners can often control contract liability, but that there is little partners could do to prevent tort liabilities).

on partnerships that exceed any social benefit derived from vicarious liability.⁴⁵ For these reasons, extending limited liability protection for tort claims to partners in an LLP makes sense.

Some additional theoretical considerations argue against extending liability protection for contract claims. The first such theoretical consideration centers on the effect that limiting contractual liability would have on a partner's behavior within an LLP. An LLP presents special risks to creditors due to its structure.⁴⁶ Partners are, by definition, co-owners of the partnership.⁴⁷ They have the right, as co-owners, to participate directly in managing the business. Partners directly participating in management can cause the business to engage in activities that injure creditors. While it is good for businesses to take risks, limited liability may encourage partners in an LLP to take risks that have high potential payoffs for themselves but impose costly risks on the LLP's creditors.⁴⁸ Other risks presented by limiting liability in LLPs are also unique to this business form. The fact that co-owners directly manage the business differentiates LLPs from other business associations like limited partnerships and corporations, where the owners may not be the ones managing the business.⁴⁹ Additionally, unlike all other business forms, LLP statutes do not restrict distributions or compromises of contribution obligations, which can increase the risk to creditors who rely on firm assets when making business decisions.⁵⁰ The way to mitigate these risks in an LLP is to provide a restricted form of limited liability,⁵¹ i.e., enact a narrow-shield LLP statute.

A second consideration focuses on further potential effects of limiting liability for contractual breaches. By not limiting liability

⁴⁵ *Id.* § 3.01(c) (providing a detailed analysis of the social benefits derived from vicarious liability, or lack thereof, and the tenuous effect vicarious liability has on businesses and partnerships); see also *supra* text accompanying notes 19-22 (noting the huge vicarious liabilities of partners in connection with the savings and loan crisis).

⁴⁶ See BROMBERG & RIBSTEIN, *supra* note 9, § 1.03(b) (comparing LLPs to corporations and other unincorporated business forms).

⁴⁷ UNIF. P'SHIP ACT § 6 (1914); REVISED UNIF. P'SHIP ACT § 101 (1997).

⁴⁸ BROMBERG & RIBSTEIN, *supra* note 9, § 1.03(a).

⁴⁹ *Id.* § 1.03(b). In this respect, LLPs do not differ from limited liability companies and close corporations, where business owners directly manage the business and have limited liability. However, as noted above, other characteristics of the LLP differentiate it from even these business forms. *Id.*

⁵⁰ *Id.*

⁵¹ *Id.* However, there are ways in which such risks may be mitigated without requiring a narrow-shield. First, states can (and some do) require LLPs to have a certain amount of insurance. Second, not limiting liability for a partner's own wrongdoings or supervisory liability may be a sufficient enough restriction on limiting liability. *Id.* Liability for a partner's own acts or supervisory liability may not be limited even in broad-shield jurisdictions. See *supra* note 36 and accompanying text.

for contract obligations, the “basic vicarious liability nature of partnership” is preserved.⁵² Under the uniform partnership acts, partners retain joint liability for contract obligations and joint and several liability for tort obligations.⁵³ Partnerships remain the only business formations that permit vicarious liability against partners.⁵⁴ Therefore, it may be necessary for LLPs to retain some vicarious liability in order to remain true to the partnership form and to maintain partnership status under regulatory statutes.⁵⁵ Not limiting contractual liability also places the onus on partners to act in the interests of creditors and clients. This is based on a theory that any injury resulting from a breach may be foreseeable and, therefore, the partners could act to prevent the injury and avoid liability. Partners can contract and negotiate for liability protection from contractual breaches.⁵⁶ It is common for partners in partnerships to enter into enforceable “nonrecourse” contracts with creditors. These nonrecourse contracts state that creditors will not seek compensation from the partners’ individual assets.⁵⁷ One could argue that partners need no further protection.

For these reasons, some states may continue to favor a narrow-shield. It is important to note, however, that there are many arguments against narrow-shields and in favor of broad-shield protection.⁵⁸ Because of the various theoretical considerations, there may never be uniformity among limited liability partnership provisions when it comes to the level of protection afforded to partners, as some states will continue to favor a narrow-shield and others the broad-shield.

⁵² BROMBERG & RIBSTEIN, *supra* note 9, § 3.03(b).

⁵³ UNIF. P'SHIP ACT § 15 (1914); REVISED UNIF. P'SHIP ACT § 306 (1997).

⁵⁴ General partnership and limited partnership statutes hold some or all partners vicariously liable for partnership obligations. See UNIF. P'SHIP ACT § 15 (1914); REVISED UNIF. P'SHIP ACT § 306 (1997); UNIF. LTD. P'SHIP ACT § 303 (1985). LLCs and corporations protect owners from vicarious liability. See UNIF. LTD. LIAB. CO. ACT § 303 (1996); MODEL BUS. CORP. ACT § 6.22 (1984).

⁵⁵ BROMBERG & RIBSTEIN, *supra* note 9, § 3.03(b).

⁵⁶ *Id.* § 1.03(b).

⁵⁷ *Id.* § 3.01(b). Interestingly, some argue that partners in an LLP should automatically have limited liability against contract claimants because the LLP status of a business provides notice to creditors and clients. This notice sufficiently warns creditors of the limited liability nature of the partnership and should encourage creditors to seek ways to protect themselves in their dealings with such businesses. See *id.*

⁵⁸ See *id.* § 3.03(b) (providing several arguments against unlimited contractual liability and lending support to a broad-shield formation). Furthermore, support for broad-shield protection is demonstrated from the fact that two-thirds of the states now provide this type of protection for LLPs. See *supra* note 12 and accompanying text (listing statutes with narrow-shield provisions). For further discussion on theories underlying broad-shield and narrow-shield formulations, see Goforth, *supra* note 27, at 1170-96, favoring ultimately a narrow-shield approach.

The limited liability afforded to partners in a limited liability partnership is the most significant feature of the business form.⁵⁹ It is also the feature that may create the most uncertainty for partners. The strength of the limited liability protection offered by the LLP has yet to be tested. The question remains whether an entity formed in a broad-shield jurisdiction will have its protections recognized when sued in a narrow-shield jurisdiction or vice versa. The analysis below will show that based on statutory language and conflict-of-law theories, the shield provided by the state of organization will likely be recognized by courts in other jurisdictions.

D. LLPs and Choice-of-Law Provisions

As noted above, two-thirds of the states have enacted an LLP statute granting a broad-shield type protection to partners, while one-third of the states maintain a narrow-shield provision.⁶⁰ This split among states' liability provisions may lead to some uncertainty when limited liability partnerships with one type of shield are sued in a jurisdiction that provides for a different liability shield. This uncertainty has generally been ameliorated by the fact that LLP statutes today contain a choice-of-law provision.⁶¹ Indeed, one could say that choice of law is one area of uniformity in LLP provisions.⁶² These choice-of-law provisions are similar to Ohio's statute, which states that "the organization and internal affairs of a foreign [LLP] and the liability of the partners for the debts, obligations, or other liabilities . . . shall be governed by the laws of the state under which the foreign [LLP] is organized."⁶³

⁵⁹ BROMBERG & RIBSTEIN, *supra* note 9, § 1.02(b) (explaining that the level of liability protection afforded affects not only the partners' liability, but internal rules governing LLPs, the treatment of LLPs under regulatory provisions like the bankruptcy and tax codes, and a business's choice to form a limited liability partnership).

⁶⁰ See *supra* note 12 and accompanying text (listing statutes with narrow-shield provisions).

⁶¹ See BROMBERG & RIBSTEIN, *supra* note 9, tbl. 6-2 (showing that all states but Louisiana have adopted an LLP statute containing a choice-of-law provision). In 1993, the District of Columbia was the first jurisdiction to include a choice-of-law provision in its LLP statute. The D.C. law provided that foreign limited liability partnerships could qualify and register locally and be governed by the liability limitations of the state in which they were formed. D.C. CODE ANN. § 41-147 (1994 Supp.) (repealed 1998).

⁶² Brusini & Zubiago, *supra* note 14, at 42.

⁶³ OHIO REV. CODE ANN. § 1775.05(C) (Anderson 2002). Note that a foreign limited liability partnership means any partnership organized and registered as an LLP under the laws of another state. *Id.* § 1775.05(D). However, not all states provide that the law of the state of formation will govern the liability of partners. Pennsylvania's statute provides that the liability of partners shall be governed by the laws of the jurisdiction under which the LLP was organized, except that the partners shall not be entitled greater protection from liability than is available to partners in a domestic LLP. 15 PA. CONS. STAT. ANN. § 8211 (West 1995 & Supp. 2003). Pennsylvania is a narrow-shield state and therefore, its provision seems to reject recognition of the broad-shield protections that a majority of other jurisdictions provide to partners.

These provisions seem to answer clearly the choice-of-law question, as they provide that the law of the state where the LLP was organized will govern the LLP in other jurisdictions. This would mean that the liability protection provided to partners of an LLP formed in a broad-shield state would extend to protect them when sued in a narrow-shield state. But this may not be the case. The way in which some state LLP statutes define what qualifies as a foreign LLP creates some uncertainty as to how the LLPs will be governed and whether the state of formation's law will actually apply. For example, some state statutes define foreign limited liability partnerships as those firms that are not only denominated as such under the law of the state of organization, but that also meet some sort of "similarity" test, though this test may not be defined.⁶⁴ One such state provision is Colorado's LLP statute. The statute defines a foreign LLP as an entity that is formed under the laws of a jurisdiction other than the State of Colorado and is functionally equivalent to a domestic LLP.⁶⁵ Yet, the statute fails to define the term "functionally equivalent." Since Colorado is a broad-shield state,⁶⁶ does that mean that an LLP formed in a narrow-shield state would not be functionally equivalent? Alabama's state statute provides that a foreign limited liability partnership is a partnership formed under the laws of another state as either a partnership or limited liability partnership in which no partner is personally liable for debts or obligations under the law of such state.⁶⁷ Under this statute, an LLP formed in a narrow-shield jurisdiction would not fall within this definition because partners are still personally liable for contract liability. In such instances, would the law of the state of formation be applied or ignored?⁶⁸ Courts have not yet provided the answer to such questions and LLP provisions remain largely unchallenged. In order to answer the choice-of-law questions presented by LLP statutes, it may be necessary to look to conflict-of-law theories.⁶⁹

⁶⁴ BROMBERG & RIBSTEIN, *supra* note 9, § 6.02(a).

⁶⁵ COLO. REV. STAT. § 7-90-102 (2002).

⁶⁶ COLO. REV. STAT. § 7-60-115(2)(a) (2002).

⁶⁷ ALA. CODE § 10-8A-101(4) (1999 & Supp. 2002).

⁶⁸ There may be other statutory provisions involved in the choice-of-law provision. For example, if a state's LLP provision states that a foreign limited liability partnership is governed by the law of the state of formation, that may not be the end of the analysis. The law of the state of formation may provide that the LLP is governed by the state where its chief executive office is located. The LLP provision may also allow partners to elect which jurisdiction will govern its partnership agreement. However, some states do not allow partners to waive the state of formation's law regarding partner liability by a contractual choice-of-law provision. See BROMBERG & RIBSTEIN, *supra* note 9, § 6.03; REVISED UNIF. P'SHIP ACT § 106 (1997).

⁶⁹ However, there may be other ways around the choice-of-law conflict. See BROMBERG & RIBSTEIN, *supra* note 9, § 6.02, which discusses the effects of LLP statute registration re-

II. LIMITED LIABILITY PARTNERSHIPS AND CONFLICT-OF-LAW THEORIES

As discussed above, limited liability statutes contain a choice-of-law provision stating that a state must recognize and apply the law of the state under which the LLP was formed. However, as also noted, there are ambiguities in LLP laws that may create a loophole in choice-of-law provisions. When courts are confronted with such choice-of-law conflicts, they turn to general conflict-of-law theories.⁷⁰

The study of conflict of laws focuses on events that have legal implications involving more than one sovereign.⁷¹ Conflict of laws involves the basic question of whether courts should emphasize the law of the state where parties reside, or the law of the state in which significant events occurred.⁷² This question is complex due to the disagreement between courts and scholars as to the preferred approach to resolving conflict-of-law problems.⁷³ The area of conflict of laws is described as “a dismal swamp, filled with quacking quagmires, and inhabited by learned but eccentric professors who theorize about mysterious matters in a strange and incomprehensible jargon.”⁷⁴ Despite this, conflict of laws continues to be a pervasive and developing area of law.

A. Major Approaches to the Choice-of-Law Question

Over time, various approaches to conflict-of-law questions have been developed. Four major conflict-of-law approaches include the First Restatement’s vested-rights approach, the Second Restatement approach, Brainerd Currie’s interest-analysis approach, and the better-law approach.⁷⁵ At present, a majority of

quirements that may also alleviate the problem of how to treat a foreign LLP.

⁷⁰ The Restatement (Second) of the Conflict of Laws provides that states must recognize and follow statutory choice-of-law provisions. Should a jurisdiction determine that the choice-of-law provision would not apply to a foreign LLP, conflict-of-law principles would apply. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6(1) (1971).

⁷¹ WILLIAM M. RICHMAN & WILLIAM L. REYNOLDS, UNDERSTANDING CONFLICT OF LAWS § 1 (1984).

⁷² ROBERT A. LEFLAR ET AL., AMERICAN CONFLICTS LAW § 2 (4th ed. 1986).

⁷³ See RICHMAN & REYNOLDS, *supra* note 71, § 44 (discussing the history of and various approaches to conflict of laws).

⁷⁴ EDWIN SCOTT FRUEHWALD, CHOICE OF LAW FOR AMERICAN COURTS: A MULTILATERALIST METHOD I (2001) (referring to a statement made by William L. Prosser in *Interstate Publication*, 51 MICH. L. REV. 959 (1953)). The field of conflict of laws has further been attacked by Professor Perry Dane, who referred to conflict of laws as “the law’s psychiatric ward.” *Id.*; see also ROBERT A. SEDLER, ACROSS STATE LINES: APPLYING THE CONFLICT OF LAWS TO YOUR PRACTICE I (1989).

⁷⁵ These will be discussed in detail below. This Note has limited its analysis to these four common approaches, but other conflict-of-law theories exist, such as Lea Brilmayer’s negative rights approach, Edwin Scott Fruehwald’s multilateralist method, and Albert Ehrenzweig’s true

courts follow the Second Restatement.⁷⁶ Yet, the question as to which approach to use is by no means settled.

1. Underlying Factors in Picking a Choice-of-Law Approach

With various approaches to choose from, how do courts choose? One way may be to look at the social and legal goals underlying each approach. There are various ways of classifying these approaches, and how an approach is classified may lend insight into its underlying social and legal goals. For example, one method of classification divides the approaches between “jurisdiction selecting systems” and “content selecting systems.”⁷⁷ A jurisdiction-selecting system is one that chooses a state’s law regardless of the substance of the case or the legal policy. A jurisdiction-selecting system is an approach that would apply a bright-line rule. An example would be a choice-of-law rule providing that the law of the state where a car accident occurred always applies in car accident cases.⁷⁸ In contrast, a content-selecting system chooses and applies a particular state law based on the motivating policy of the laws. A content-selecting system would be one in which the court would examine the public policy behind the competing state laws. Then the impact of the choice-of-law decision on that policy would be considered.⁷⁹

Another method of classification is that of unilateralist or multilateralist approaches. A unilateralist approach favors the forum state’s law and asks whether lawmakers intended the law to apply to the particular facts at hand and whether or not there is a state interest in the issue. If it is determined that the law’s scope encompasses the controversy, a court will apply the forum law even if another state has a greater interest.⁸⁰ One could imagine that a unilateralist approach might involve a bright-line rule applying the forum state’s laws in most occasions. On the other hand, a multilateralist approach tries to connect the controversy with the most appropriate legal system. Restrictions on multilateralist approaches are that (1) it may not reflect any unjustified preference,

rules approach. See LEA BRILMAYER, *CONFLICT OF LAW: FOUNDATIONS AND FUTURE DIRECTIONS* 25-27 (1995); FRUEHWALD, *supra* note 74, at 103-22; RICHMAN & REYNOLDS, *supra* note 71, § 67 (discussing Ehrenzweig’s true rules approach).

⁷⁶ SEDLER, *supra* note 74, at 28.

⁷⁷ RICHMAN & REYNOLDS, *supra* note 71, § 44 (describing these “systems” of identifying conflict-of-law theories).

⁷⁸ See *id.* This example is similar to the First Restatement. See *infra* Part II.A.2.

⁷⁹ See RICHMAN & REYNOLDS, *supra* note 71, § 44. Another example of a content selecting system is the interest-analysis approach discussed below. See *infra* Part II.A.4.

⁸⁰ FRUEHWALD, *supra* note 74, at 2 (noting further that often a unilateralist approach results in the application of forum law).

and (2) the choice-of-law outcome must be foreseeable by the parties involved in the dispute. In this respect, a multilateralist approach could be similar to a jurisdiction-selecting system in that it would apply the laws of the territory where the last act in a chain of events occurred.⁸¹ Such an approach would be both impartial and foreseeable.

One final classification distinguishes between consequentialist approaches and deontological approaches.⁸² Consequentialist approaches focus on policy and social goals by considering which state's law produces the better result for society at large. Such an approach would apply the state's law that is more likely to result in justice and promote public policy. Deontological approaches appeal to conformity with certain rules of duty and emphasize principles and personal rights,⁸³ as they are more concerned with the impact of the decisions on individual parties than societal interests. For these reasons, a deontological approach might be one that applies the state law that would most protect the parties' expectations.

These different classifications can apply simultaneously.⁸⁴ For example, the First Restatement approach is deontological, multilateralist, and a jurisdiction-selecting system. The interest-analysis approach and the better-law approach could be described as consequentialist, unilateralist, and content-selecting. While these classifications may add more confusion and complexity to the conflict of law discussion, they explain the legal and social goals underlying each conflict-of-law approach. Furthermore, they may give insight into a court's decision to apply a certain approach. The classifications also add some context to an analysis of the different approaches described below.

2. *The First Restatement Approach*

The first conflict-of-law approach that developed was the First Restatement. The First Restatement was a rejection of the principle of comity, which guided conflicts of law at that time.⁸⁵ Comity guided states to respect the laws of other sovereigns. The First Restatement rejected this principle because it gave courts too much discretion to enforce or not to enforce the local law in favor

⁸¹ *Id.*

⁸² *Id.* at 3 (comparing consequentialist approaches to deontological approaches).

⁸³ *Id.* (arguing that choice-of-law theories should be deontological because choice-of-law approaches should be content- and forum-neutral).

⁸⁴ *See id.*

⁸⁵ RICHMAN & REYNOLDS, *supra* note 71, § 51.

of another state's law.⁸⁶ Instead, the First Restatement proffered the vested-rights approach. The vested-rights theory is a geographical approach to the conflicts problem, in which rights of parties are considered vested in the place in which they were created.⁸⁷ Put simply, this theory states that when an event occurs, the law where the event occurred would govern.⁸⁸

The goal of the vested-rights approach is to promote uniformity and ease of administration.⁸⁹ This approach consists of a two-step process. First, the character of the issue involved is determined, meaning the court determines whether the case involves tort, contract, property, or some other specific area of law. Second, the court applies the choice-of-law rule applicable to that area of law. Each area of law has a particular choice-of-law rule that defines where a right vests and therefore, which state's law would govern.⁹⁰

What does this mean in practice? In a tort case, the law of the "place of the wrong" determines which law governs under this theory.⁹¹ The place of the wrong is the state where the last event necessary to make an actor liable for an alleged tort takes place. Usually, for torts the last act is the harm to the plaintiff and, therefore, the place of the wrong is usually the place where the injury occurred.⁹² There are exceptions to this idea of the place of the wrong. One such exception deals with vicarious liability. When vicarious liability is at issue, the place of the wrong applies only if the defendant authorized the tortfeasor to act for him in that state.⁹³ Other exceptions to the place of the wrong include when the defendant justifiably relies upon the law of the state where he acted, but injury occurs in a different state that has a higher standard of

⁸⁶ See JOSEPH H. BEALE, SELECTIONS FROM A TREATISE ON THE CONFLICT OF LAWS § 16 (1935) (suggesting that conflict-of-law questions be resolved by the "law of the land"). Some theorists also saw comity as a violation of the notion that no law could have an effect outside of its jurisdiction. The First Restatement and the vested-rights theory restrained comity because it limited judges' discretion to a territorial based conflict-of-law theory. RICHMAN & REYNOLDS, *supra* note 71, § 51(b).

⁸⁷ BEALE, *supra* note 86, § 15.

⁸⁸ See *id.* § 41.

⁸⁹ SEDLER, *supra* note 74, at 29.

⁹⁰ RICHMAN & REYNOLDS, *supra* note 71, §§ 51-53; see also Jennifer J. Johnson, *Risky Business: Choice-of-Law and the Unincorporated Entity*, 1 J. SMALL & EMERGING BUS. L. 249, 260 (1997) (providing a brief overview of conflict-of-law theories).

⁹¹ RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 377 (1934).

⁹² *Id.* §§ 377, 384; see also BEALE, *supra* note 86, §§ 377.2, 378.2, 384.1.

⁹³ RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 387 (1934); see also RICHMAN & REYNOLDS, *supra* note 71, § 53 (explaining that if a defendant did not authorize his agent to enter that state, then he has not submitted himself to that state's law). However, it is not clear which state's law would apply when the agent has not been authorized to act, but one might assume that under the vested-rights theory, a tort analysis would apply.

care.⁹⁴ The vested-rights approach provides that the defendant's "reasonable expectations about the results of his conduct should not be frustrated because of the fortuity of an out-of-state injury."⁹⁵

In a contract case, the law of the "place of making" of the contract applies.⁹⁶ The place of the making refers to the place where the principal event necessary to make a contract occurs.⁹⁷ An exception to this rule is when the issue deals with performance or breach. In those instances, the place of performance determines which law governs.⁹⁸

How would the First Restatement answer the choice-of-law question posed by broad-shield and narrow-shield LLPs? To answer the question, the court must determine which state's law would govern the liability of partners for contractual liability. This question also involves some elements of vicarious liability, for it seeks to determine if the partners will be liable for contractual obligations of the partnership and other partners. Under the vested-rights approach of the First Restatement, the law of the state of formation may govern.

First, the LLP choice-of-law question presented would involve contractual liability, presumably for a breach of contractual duties. In a contract situation, the First Restatement calls for the law of the state where performance was to occur to govern the question of liability.⁹⁹ However, this question is fact specific. The answer would depend on the particular contract itself. But if the contract called for an LLP to provide services within the state where the LLP was formed, then the law of the formation state would apply and the shield provided partners by the laws under which they organized would remain intact.

In regards to the vicarious liability aspect of the problem, the First Restatement provides that a partner would be liable under another state's laws if he had authorized another partner to act as

⁹⁴ RESTATEMENT (FIRST) OF CONFLICT OF LAWS §§ 380(2), 382 (1934); RICHMAN & REYNOLDS, *supra* note 71, § 53. As mentioned above, it is usually the law of the state where the injury occurs that applies. Where the injury occurs is not necessarily the same location as where the defendant may have acted.

⁹⁵ RICHMAN & REYNOLDS, *supra* note 71, § 53.

⁹⁶ RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 332 (1934); BEALE, *supra* note 86, § 332.4.

⁹⁷ BEALE, *supra* note 86, § 311.1. There are differences for formal contracts and informal contracts. In a formal contract setting, the place of delivery is the deciding location. In an informal contract case, it is the location of the offeree's promise that matters. Other exceptions include questions dealing with details of contract performance. In such a case, the law of the place of performance governs. *See id.* §§ 312.1, 312.2.

⁹⁸ *Id.* §§ 355.1, 370.1; RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 358 (1934).

⁹⁹ RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 358 (1934); BEALE, *supra* note 86, § 370.1.

an agent in another state.¹⁰⁰ In an LLP, all partners are agents of the partnership.¹⁰¹ But the vested-rights approach makes exceptions for the reasonable reliance and expectations of the defendant. A partner in a limited liability partnership formed in a broad-shield state relies on that protection. As a result, a partner may not take the same precautions to monitor or control the actions of his or her partners as he or she might have taken in a narrow-shield LLP. A partner in a narrow-shield jurisdiction, in contrast, knows about the potential risks of contractual liability and can take some measures to protect him or herself. Taking the parties' expectations into consideration, a court will likely recognize the liability shield of the state of formation.

The vested-rights approach was criticized as favoring predictability over equality and as being too rigid.¹⁰² The vested-rights approach was also criticized because rather than being concerned with what law is better, it concentrates on labeling the legal issue involved and locating the jurisdiction where the event happened.¹⁰³ Other criticisms are that the theory is too simplistic, that it tries to separate between issues of torts and contracts that often should be linked, and that it often results in the choice of the law of a place that has no interest in the case.¹⁰⁴

3. *The Second Restatement Approach*

The Second Restatement resulted from these criticisms. The Second Restatement adopted a more "policy-centered" approach and chose the applicable law on a case-by-case basis after considering policy and fairness to parties.¹⁰⁵ This analysis applies a balancing test to determine which state's law governs. However, the first step under the Second Restatement is to determine if there is an applicable statutory choice-of-law rule. The Second Restatement provides that if a statutory choice-of-law rule exists, the court must follow it.¹⁰⁶ When a state statute expresses a choice-of-law rule, the role of the courts becomes interpretive as to the meaning and objective of the choice-of-law rule.¹⁰⁷ When a state's choice-of-law rule is ambiguous, the courts examine the state's

¹⁰⁰ See *supra* note 93 and accompanying text.

¹⁰¹ UNIF. P'SHIP ACT § 9 (1914); REVISED UNIF. P'SHIP ACT § 301 (1997).

¹⁰² See RICHMAN & REYNOLDS, *supra* note 71, § 44 (explaining that the vested-rights approach was considered too inflexible and that this criticism eventually led to the Second Restatement).

¹⁰³ *Id.* § 52.

¹⁰⁴ *Id.* § 56.

¹⁰⁵ SEDLER, *supra* note 74, at 28.

¹⁰⁶ RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6(1) (1971).

¹⁰⁷ LEFLAR ET AL., *supra* note 72, § 93, at 273.

policies and interests in determining whether the statute is adequate to answer the choice-of-law question.¹⁰⁸

If there is not an applicable statutory choice-of-law rule, the court then looks for the state with the "most significant relationship."¹⁰⁹ The state with the most significant relationship to the case is the state whose law applies.¹¹⁰ To make this determination, the Second Restatement sets forth a balancing test of several factors, including: (1) the needs of the interstate system; (2) the relevant policies of the forum and other states involved and the interest of these states in resolving the issue; (3) the basic policies of the particular area of law involved; (4) the protection of justified expectations; (5) certainty, predictability, and uniformity of result; and (6) ease of administration.¹¹¹ The Second Restatement does not call for special weight to be given to any factor, but rather provides that the judge can balance the factors appropriately.¹¹²

In practice, the Second Restatement has separate analyses for tort and contract cases. For tort cases, the choice-of-law analysis includes the place where the injury occurred, the place where conduct causing the injury occurred, the domicile or the place of business of the parties, and the place where the relationship between the parties centered.¹¹³ In a contract case, the Second Restatement provides that courts should first look to see if the parties specified a governing law in the contract.¹¹⁴ However, the contractual choice-of-law provision is not automatically applied. The Second Restatement provides that a contractual choice of law should be respected with two exceptions. First, if the chosen state has no substantial relationship to either party or the contract and there is no reasonable basis for the specified choice, then the contractual choice of law will not be followed. Second, courts can reject the contractual choice of law if the chosen state's law is contrary to a fundamental policy of another state that has a material interest in the case.¹¹⁵ Often, however, the parties' choice of law is upheld.¹¹⁶ In instances where there is no contractual choice of law, then such factors as the place of contracting, the place of negotiation, the

¹⁰⁸ *Id.* § 93, at 274 (explaining that courts typically want to find that a state has answered the choice-of-law problem).

¹⁰⁹ RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6 (1971).

¹¹⁰ *See id.* §§ 6, 145, 188.

¹¹¹ *Id.* § 6(2); *see also* RICHMAN & REYNOLDS, *supra* note 71, § 59(c); SEDLER, *supra* note 74, at 34.

¹¹² RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6(2) cmt. c (1971).

¹¹³ *Id.* § 145.

¹¹⁴ *Id.* § 187 (explaining when the law of the state chosen by the parties should be applied).

¹¹⁵ *Id.* §§ 186-87.

¹¹⁶ Johnson, *supra* note 90, at 264 (referring to application of the Second Restatement in modern courts).

place of performance, the location of the contract's subject matter, and the domicile of the parties should be examined.¹¹⁷ The Second Restatement also includes provisions dealing with contractual liability for partners in general partnerships. These provisions state that the law of the state with the most significant relationship will determine whether a partner is liable for obligations of the partnership.¹¹⁸

Under this conflict-of-law approach, the outcome to the LLP choice-of-law question would be the same as under the First Restatement, though the analysis would be different. The court would first look to see if there was an applicable statutory choice-of-law provision. Most states provide a choice-of-law provision for LLPs in their statutes.¹¹⁹ Therefore, the analysis would end here unless there was some ambiguity in the provision. If there was an ambiguity, the court would try to resolve it by examining the objectives and policies underlying the statute. It may be that a court would determine an LLP choice-of-law statute is unambiguous and adequate to answer a choice-of-law question. But if it does not, then the court would look for the state with the most significant relationship.

In the LLP choice-of-law scenario, it seems that most of the balancing test factors used to determine the state with the most significant relationship would favor applying the law of the state of organization. Applying the law of the state of organization would protect justified expectations, and aid predictability and uniformity. As discussed above, the partners may not have contemplated that their liability shield would not extend into other states, especially since most states have a choice-of-law rule. Therefore, partners in a broad-shield state would not have taken extra precautions based on their reliance on state law. Applying the law of the state of formation would also promote uniformity. This is true regardless of whether the case involved an LLP formed under a broad-shield or narrow-shield jurisdiction. When the law of the state of formation is chosen, the outcome for partners in LLPs throughout the formation state will be uniform. Without such a result, the outcome for partners would then rest on where they were sued and make liability for contractual obligations an unpredictable matter. Finally, such an outcome would protect the relevant policies of partnership law. Indeed, a state has an interest in

¹¹⁷ RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 188(2)(a)-(e) (1971). These factors are in addition to the balancing test factors set forth in § 6 of the Second Restatement.

¹¹⁸ *Id.* § 295 (explaining liability of partnerships and partners in accordance with §§ 292 and 294 of the Restatement (Second)).

¹¹⁹ See *supra* Part I.D. (discussing statutory choice-of-law provisions).

seeing that its laws are respected and recognized as they apply to businesses formed within its borders.¹²⁰ Furthermore, respecting partners' expectations of liability and providing a uniform result for partners within a state can act to promote entrepreneurship.¹²¹

4. *The Interest-Analysis Approach*

Since the Second Restatement, other conflict-of-law approaches have developed. These include Brainerd Currie's interest-analysis approach. Under this approach, the default rule is to apply the forum state's law.¹²² When confronted with a choice-of-law question, interest analysis instructs that the social, economic, and administrative goals of the forum law should be analyzed, as well as the policies behind the foreign jurisdiction's law. After such analysis, if it is determined that the forum state has a governmental interest in the case at bar, then the forum state's law applies. If the forum state does not have an interest, but another state does, only then does the other state's law govern.¹²³ However, Currie did not clarify what factors go into the determination of state interest. He wrote that it is not clear "whether it implies a judgment as to the relative merits of the conflicting policies, or a comparative appraisal of the number, character, and significance of the relations of the state to the case."¹²⁴

William Baxter modified the interest-analysis approach by including external objectives in the choice-of-law consideration. Baxter initiated a "comparative impairment" analysis. This involved recognition of the fact that each state needs to have its policies respected by other states.¹²⁵ As a result, courts should compare the extent to which each state's policy would be impaired if its laws were not applied, and then apply the law of the state that would suffer the most impairment.¹²⁶ Other proposals under this

¹²⁰ Not only do state LLP provisions include a choice-of-law provision regulating that the state of formation's laws will be recognized for foreign LLPs, but most include a provision that LLPs formed under its own laws shall have its internal affairs, including the liability of partners, governed by that state's laws wherever it may be doing business. BROMBERG & RIBSTEIN, *supra* note 9, § 6.02(d).

¹²¹ See Note, *The Internal Affairs Doctrine: Theoretical Justifications and Tentative Explanations for Its Continued Primacy*, 115 HARV. L. REV. 1480, 1486-87 (2002) (making the same argument in justifying the internal affairs doctrine, which is a choice-of-law rule that applies to corporations and provides that the law of the state of incorporation governs questions of shareholder and director liability).

¹²² BRAINERD CURRIE, *The Constitution and the Choice of Law: Governmental Interests and the Judicial Function*, in SELECTED ESSAYS ON THE CONFLICT OF LAWS 188, 188 (1963).

¹²³ *Id.* at 189.

¹²⁴ *Id.* at 272.

¹²⁵ RICHMAN & REYNOLDS, *supra* note 71, § 64(b) (explaining Baxter's comparative impairment analysis).

¹²⁶ *Id.*

approach include applying the law that favors recovery. However, the law favoring recovery should not be applied if it is aberrational or against the national trend.¹²⁷

Under this approach, the result to the LLP choice-of-law question seems most uncertain. Under Currie's interest-analysis approach, the outcome may be that the law of the forum state applies since the default rule favors the law of the forum. But does the forum state really have an interest in such a case? It may if it has sufficient contacts with one of the parties or with the contractual relationship involved. However, a comparative-impairment analysis would change the outcome, as it seems that the law of the state of organization would suffer greater impairment if it were not applied. If the forum law were applied in this scenario, the law of the state where the LLP was organized would be undermined and would no longer provide for a uniform or predictable result. Partners would no longer know the extent of their liability, despite the efforts of the state of organization to set some limits to partner liability. In a final twist to this analysis, if recovery were to be considered as part of the analysis, the outcome would favor the law of a narrow-shield jurisdiction whether it was the forum state or the state of formation. This is because a narrow-shield provision allows creditors to recover from partners for contractual liability. But one can argue that the narrow-shield construction is "aberrational" as it does not coincide with the national trend relating to partner liability.¹²⁸

5. *The Better-Law Approach*

One final major conflict-of-law approach that developed is Robert Lefflar's better-law approach. Lefflar perceived five considerations as influencing the choice of law: (1) predictability of result; (2) maintenance of interstate and international order; (3) simplification of the judicial task; (4) advancement of the forum's governmental interests; and (5) application of the better law.¹²⁹

The "better law" means that a law is superior to others when it achieves societal goals and a just result.¹³⁰ While some critics of the better-law approach argue that it is one way for courts to cloak their analysis and to consistently apply forum law, that is not and

¹²⁷ *Id.* § 64(c) (describing Professor Weintraub's "functional" approach to the interest analysis, which favors the law that allows recovery unless it conflicts with the national trend).

¹²⁸ See *supra* note 12 and accompanying text (noting that the trend among states is to adopt a broad-shield liability provision).

¹²⁹ LEFLAR ET AL., *supra* note 72, § 95.

¹³⁰ See *id.* § 107 (discussing some foundations of better-law determinations).

should not always be the case.¹³¹ The better-law approach involves some questioning of forum law to see if it is archaic in comparison to other states' laws. If it is, and if other state laws are influenced by other policy considerations, then forum law should not apply.¹³²

Under this approach, the LLP choice-of-law question may be resolved in favor of the state of organization. First, one of the factors considered under this approach is the need for predictability. Applying the law of the state of organization would ensure a predictable result for partners and would prohibit forum-shopping by parties.¹³³ Second, applying the law of the state of organization would maintain interstate order, as it would encourage freedom in commercial intercourse and unrestricted transactions of goods and people from state to state.¹³⁴ However, the better-law consideration of this approach may determine in some cases that the law of the state of formation does not apply. If an LLP formed in a narrow-shield jurisdiction was being sued in a broad-shield jurisdiction, the better-law analysis would include an analysis of which law was outmoded. While LLP statutes are not archaic in any sense of the word, narrow-shield statutes may be considered as outmoded as they are not part of the national trend. But this is only part of the better-law analysis. The court under this approach could still find that applying the law of the state of organization, whether it be a narrow-shield or a broad-shield jurisdiction, would achieve such societal goals as ensuring predictability, encouraging business, and respecting expectations of parties.

The above discussion shows that there are many options available to courts when deciding choice-of-law issues. With the development of these alternative theories, the state of conflicts of law today remains confusing and uncertain. At present, most courts follow the Second Restatement.¹³⁵ Yet, some courts do not use the Second Restatement or any of its superseding approaches because of their complexity and uncertainty.¹³⁶ In the sphere of tort cases, conflict of laws is especially unsettled.¹³⁷ Some courts retain the First Restatement's vested-rights approach. Some juris-

¹³¹ See RICHMAN & REYNOLDS, *supra* note 71, § 66(b) (discussing concerns with the better-law approach).

¹³² See LEFLAR ET AL., *supra* note 72, § 107 (examining courts' approaches when the law of their state is inferior).

¹³³ See generally *id.* § 103.

¹³⁴ *Id.* § 104 (explaining that such freedoms "are necessary to the success of our federal system").

¹³⁵ SEDLER, *supra* note 74, at 28.

¹³⁶ FRUEHWALD, *supra* note 74, at 95-96 (criticizing the Second Restatement).

¹³⁷ See LEFLAR ET AL., *supra* note 72, § 131 (discussing a variety of choice-of-law approaches in tort cases).

dictions reject vested rights, but have not settled on a specific approach to take its place. Some follow the better-law approach. Some scholars suggest that there is a trend for tort cases, which is that choice-of-law decisions favor plaintiffs and forum residents.¹³⁸ In contract cases, however, the choice-of-law question is settled. First and foremost, courts recognize the choice-of-law selection made by the parties in a contract. When a choice of law is not stipulated, then the courts will either apply the vested-rights approach or look for the most significant relationship. However, whichever approach is chosen, most courts act to protect the expectations of the parties.¹³⁹

6. *Constitutional Considerations and the Choice of Law*

No matter what approach a court may use, any conflict-of-law theory is limited by the Constitution. Constitutional limits on conflict-of-law theories include due process, full faith and credit, the commerce clause, privileges and immunities, and equal protection.¹⁴⁰ However, the Supreme Court has rarely applied the commerce clause, privileges and immunities clause, or equal protection clause in choice-of-law cases.¹⁴¹ The most influential constitutional considerations in choice-of-law questions are due process and full faith and credit. Due process is concerned with the effects of the choice of law on parties and seeks to eliminate unfair surprise and to ensure foreseeability of result.¹⁴² Due process is also concerned with guaranteeing that there is a sufficient interest between the jurisdiction whose law is applied and the controversy.¹⁴³ The constitutional due process requirement acts to limit the reach of a forum's legitimate authority.¹⁴⁴ Meanwhile, full faith and credit mandates respect for legal decisions of other states.¹⁴⁵ It applies to rules of law as well as to judicial judgments and calls for nondiscrimination towards legal rules of other states.¹⁴⁶ However, this standard generally has been interpreted to mean that a forum "need only open its doors to the same extent that it would for a

¹³⁸ RICHMAN & REYNOLDS, *supra* note 71, § 72(b).

¹³⁹ *See id.* § 73 (noting that protecting the expectations of parties is one of the primary goals of contract laws).

¹⁴⁰ BRILMAYER, *supra* note 75, at 112 (stating that federalism is "[t]he key constitutional concept in interstate relations" as it is federalism that makes constitutional limits on state authority necessary).

¹⁴¹ *See* RICHMAN & REYNOLDS, *supra* note 71, § 84(b)-(d).

¹⁴² *Id.* § 84(a).

¹⁴³ *See* BRILMAYER, *supra* note 75, at 117 (explaining the Supreme Court's historical efforts to determine the required connection).

¹⁴⁴ *Id.* at 115.

¹⁴⁵ *Id.* at 129.

¹⁴⁶ *Id.* (explaining the nondiscrimination approach to the full faith and credit clause).

domestic cause of action.”¹⁴⁷ This does not mean that the forum must subordinate its own laws unless it determines another jurisdiction has a significant interest in the controversy.¹⁴⁸

When combined with the conflict-of-law theories described above, it seems these constitutional limits would favor the application of the law of the state of organization in the choice-of-law question facing LLPs. Due process is concerned with foreseeability and unfair surprise to parties. This seems to call for a choice-of-law ruling that would protect the expectation of parties and lead to a predictable result for future cases. This is accomplished when the law of the state of organization is applied. Applying the laws of a state other than that of formation would require partners to conduct their business differently in different jurisdictions, increasing the cost of doing business.¹⁴⁹ Furthermore, the full faith and credit clause requires respect to be given to another jurisdiction’s laws when it has an interest in having its law applied. The state of organization does have an interest in seeing that its law is applied, as it would be a recognition of the state’s ability to govern entities formed within its borders.

In summary, conflict-of-law theories and the constitutional constraints guiding these theories seem to suggest that the law of the state of formation should apply to the choice-of-law questions raised by broad-shield and narrow-shield LLP provisions. This conclusion is further supported with an examination of choice-of-law principles that generally apply to corporations and other types of business associations.

B. Business Entities and the Choice of Law

In regards to corporations, two choice-of-law rules are generally recognized. First, when the question involves the internal affairs of the corporation, the law of the place of incorporation controls.¹⁵⁰ This is known as the internal affairs doctrine. The second rule states that when the case involves corporate responsibility to others, general conflict-of-law rules govern.¹⁵¹

The internal affairs doctrine is a judge-made choice-of-law doctrine that encourages courts to apply the law of the incorporat-

¹⁴⁷ *Id.*

¹⁴⁸ *See id.* at 129-31 (discussing situations when another state’s laws are treated differently).

¹⁴⁹ Furthermore, easing the costs of business is a benefit to society. *See generally* BROMBERG & RIBSTEIN, *supra* note 9, § 3.02 (discussing policy behind limited tort liability); *see also supra* note 45 and accompanying text.

¹⁵⁰ RICHMAN & REYNOLDS, *supra* note 71, § 76.

¹⁵¹ RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 301 (1971).

ing state in cases involving corporations.¹⁵² The origin of the internal affairs doctrine revolves around the fact that corporations were created by individual states.¹⁵³ When a state agreed, it would issue a charter to a corporation. The internal affairs rule dictated that only the chartering state could regulate the entity. The original concept was based on the principle that courts did not have jurisdiction over foreign corporations.¹⁵⁴

As conflict-of-law theories developed, the internal affairs doctrine remained intact. Both the First and Second Restatements supported the doctrine.¹⁵⁵ The doctrine has also garnered statutory support. The Model Business Corporation Act ("MBCA") contains a provision supporting the enforcement of the internal affairs rule.¹⁵⁶ Such support exists for the doctrine because the rule allows for uniform treatment in cases where it is needed.¹⁵⁷ The doctrine also offers the advantages of convenience, certainty, predictability, and ease of application.¹⁵⁸ The rule has also traditionally applied to cases dealing with imposing liability on shareholders of the corporation.¹⁵⁹ From this historical analysis of the doctrine's application, it seems one could easily argue that there would be some benefit if the doctrine were applied to limited liability partnerships as well.¹⁶⁰

However, there are limitations to the application of the internal affairs rule. While the Second Restatement supported the use of the internal affairs doctrine, it did so in a qualified way. The Second Restatement provided that in the event a state other than the state of incorporation has a more significant relationship with

¹⁵² Note, *supra* note 121, at 1480 (explaining the internal affairs doctrine).

¹⁵³ Johnson, *supra* note 90, at 269 (explaining the development of the internal affairs rule as state charters created corporations).

¹⁵⁴ See BEALE, *supra* note 86, §§ 166.1, 166.2 (noting that a corporation only "exists" inside the state of incorporation).

¹⁵⁵ See RESTATEMENT (FIRST) OF CONFLICT OF LAWS §§ 182-87 (1934) (providing that the law of the state of incorporation shall apply in certain situations involving corporations); RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 306-07 (1971) (proscribing when the law of the state of incorporation will determine shareholder liability).

¹⁵⁶ MODEL BUS. CORP. ACT § 15.05(c) (1984) (providing that a state is not authorized to apply its laws "to regulate the organization or the internal affairs of a foreign corporation authorized to transact business" within the state).

¹⁵⁷ See PHILLIP I. BLUMBERG, *THE LAW OF CORPORATE GROUPS: TORT, CONTRACT, AND OTHER COMMON LAW PROBLEMS IN THE SUBSTANTIVE LAW OF PARENT AND SUBSIDIARY CORPORATIONS* § 26.02 (1987) (listing as examples of cases needing uniformity those involving the election of directors, legality of dividends, and legality of stock issuance).

¹⁵⁸ *Id.*

¹⁵⁹ One such example was *Chandler v. Peketz*, 297 U.S. 609 (1936), in which the law of the state of incorporation provided for double liability of shareholders. Double liability was enforced even though the law of the forum state and other states did not allow for such liability. See BLUMBERG, *supra* note 157, § 26.02 n.20.

¹⁶⁰ See Johnson, *supra* note 90, at 282-94 (proposing that the internal affairs doctrine be extended to limited liability partnerships and all other unincorporated business forms).

the transaction or parties, the law of that state should be applied.¹⁶¹ Instances in which another state other than the state of incorporation has a more significant relationship include: (1) when the corporation has little contact with the state of incorporation except for incorporating there; (2) the corporation has a significant relationship to the other state; (3) the rule of the other state embodies an important policy; (4) the legal issue involved does not affect the corporate structure or internal administration or other aspect of corporate affairs for which a uniform rule is essential; and (5) the subject matter permits the application of multiple regulatory schemes.¹⁶² But it seems this exception to the internal affairs doctrine is often ignored.¹⁶³

There are also arguments against automatic application of the doctrine. Phillip Blumberg argues that “[i]n an economy increasingly conducted on a multistate and multinational basis, a choice-of-law rule involving excessive reliance on the law of the state of incorporation becomes increasingly unsatisfactory.”¹⁶⁴ This is because today, most corporations are incorporated in locales far from where they may be doing business and in locales chosen for reasons unrelated to the business.¹⁶⁵ Also, some states have rejected the MBCA because of its support for the doctrine.¹⁶⁶ The MBCA’s language creates the presumption that judicial interference with the application of the doctrine is prohibited.¹⁶⁷ Finally, some states such as California and New York choose not to apply the doctrine in some cases involving foreign corporations.¹⁶⁸ However, these views are in the minority, as the internal affairs doctrine remains the mainstream approach.¹⁶⁹

The choice-of-law principle guiding corporations is similar to choice-of-law principles governing other business organizations, such as general partnerships and limited partnerships. General

¹⁶¹ RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 302(2), 306 (1971).

¹⁶² BLUMBERG, *supra* note 157, § 26.02; *see* RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 302(2) cmt. e-g (explaining application of the significant relationship test).

¹⁶³ Johnson, *supra* note 90, at 271.

¹⁶⁴ BLUMBERG, *supra* note 157, § 26.02.

¹⁶⁵ *See id.* (explaining further that almost one-half of the largest corporations in the U.S. have incorporated in Delaware even though Delaware is unrelated to any location of business, employees, factories, etc.).

¹⁶⁶ Note, *supra* note 121, at 1480-81 (noting that Louisiana and New Jersey have declined to adopt the language of the 1984 revision of the MBCA and, by doing so, allow their courts to disregard the internal affairs doctrine).

¹⁶⁷ *See* MODEL BUS. CORP. ACT § 15.05 (1984).

¹⁶⁸ Note, *supra* note 121, at 1480 (explaining that these states do not apply the internal affairs doctrine “in cases involving foreign corporations not traded on a national securities exchange with a specified level of contact with the forum state”).

¹⁶⁹ LEFLAR ET AL., *supra* note 72, § 255 (identifying challenges to the internal affairs doctrine while recognizing that it remains the mainstream approach).

partnerships are created when partners contract to join together in order to transact business.¹⁷⁰ Limited partnerships are general partnerships in which some partners have limited liability and others have general liability.¹⁷¹ As a result, partnerships are commonly treated as contracts for choice-of-law purposes.¹⁷² Therefore, under the First Restatement, general partnerships are to be governed by the law of the state in which the partnership agreement was made or to be performed.¹⁷³ A state may also choose to follow the Second Restatement conflict-of-law principles applicable to contracts.¹⁷⁴ Therefore, if the partnership agreement specified the law to be applied, the court would respect this selection. If no governing law were chosen, the law of the state with the most significant relationship would apply.¹⁷⁵ Finally, there have been statutory developments regarding the choice-of-law question relating to general partnerships and limited partnerships. The Revised Uniform Partnership Act provides as a default rule that the law of the state “in which a partnership has its chief executive office governs relations among . . . and between the partners.”¹⁷⁶ The Proposed Revision of the Revised Uniform Limited Partnership Act proposes that “[t]he laws of the State or other jurisdiction under which the foreign limited partnership is organized govern its internal affairs and the liability of its partners.”¹⁷⁷

Such statutory provisions exist for limited liability companies as well. The limited liability company is a business formation that provides liability protection to all owners and members and is treated for tax purposes like a partnership.¹⁷⁸ Similar to corporations, partnerships, and limited partnerships, foreign limited liability companies are governed by the law of the state of organiza-

¹⁷⁰ UNIF. P'SHIP ACT § 6 (1914) (defining a partnership as “an association of two or more persons to carry on as co-owners a business for profit”); REVISED UNIF. P'SHIP ACT § 202 (1997) (defining a partnership as “an association of two or more persons to carry on as co-owners a business for profit”).

¹⁷¹ REVISED UNIF. LTD. P'SHIP ACT §§ 303, 403 (1985) (defining certain characteristics of both general and limited partners in limited partnerships).

¹⁷² See Johnson, *supra* note 90, at 275, 277 (indicating, however, that the Revised Uniform Limited Partnership Act provides that the state of organization governs internal affairs of a limited partnership).

¹⁷³ RICHMAN & REYNOLDS, *supra* note 71, § 54(a).

¹⁷⁴ See *supra* text accompanying notes 114-16.

¹⁷⁵ See *supra* text accompanying notes 114-16.

¹⁷⁶ REVISED UNIF. P'SHIP ACT § 106 (1997). The comments note that this is only a default rule and that the partners may select another jurisdiction's laws to govern by including such a provision in the partnership agreement. Also, while the place of a partnership's chief executive offices may be different from the state of formation, it is important to note that the uniform rule does not apply, or provide for, the application of the law of the forum state.

¹⁷⁷ REVISED UNIF. LTD. P'SHIP ACT § 901(a) (March 2000 Draft).

¹⁷⁸ See BROMBERG & RIBSTEIN, *supra* note 9, §§ 1.04(c), 301(f) (comparing LLPs to LLCs).

tion.¹⁷⁹ This general consensus as to the choice-of-law rule governing business associations lends much support to the argument that the law of the state of organization should apply in LLPs as well.

CONCLUSION

A division exists among state LLP statutes. Some states have chosen to provide partners a broad liability shield, protecting them from personal liability for tort and contractual obligations. Other states extend partners a narrow-shield, protecting them only from tort liability. This split raises a question: What would happen when an LLP with one type of liability shield is sued in a state providing for more or less liability protection?

One source that is available to answer this question is state choice-of-law provisions for LLPs, as these statutes are uniform throughout the states. LLP statutes apply the law of the state of formation to questions dealing with the internal affairs and liability of the partners. However, due to the haphazard way in which LLP statutes were adopted, there may be ambiguities in the statutes that create a loophole to the choice-of-law rule. When that happens, states may look to conflict-of-law theories to help them decide which state's law should apply.

Based on the factors considered under each of the major conflict-of-law approaches and the constitutional restraints on choice of law, it seems courts should apply the law of the state of formation. Applying the law of the formation state will protect the expectations and justifiable reliance of partners, allow for ease of administration, allow for predictability, and support the policy goals of the formation state. Furthermore, the generally applied conflict-of-law approach for all other business formations results in the law of the state of organization governing questions of liability. Based on this analysis, a strong argument exists that the law of the state of formation should govern the liability of partners, wherever they may be sued.

CHRISTINE M. PRZYBYSZ[†]

¹⁷⁹ UNIF. LTD. LIAB. CO. ACT § 1001(a) (1996) (providing that the laws of the state under which a foreign LLC is organized govern its organization, internal affairs, and the liability of its managers and members).

[†] J.D. Candidate, 2004, Case Western Reserve School of Law. I would like to thank Professors Jonathan Entin and David Sokolow for their guidance in the development of this Note.