Lawyers practicing together will eventually reach a stage where the focus must change from the goals of individuals to the preservation of the group as an institution. More than half of the firms in the Los Angeles area do not have a partnership agreement and if they do, most partnership agreements do not adequately address matters that are critical to the existence of a firm as an entity separate from the individual members of the firm. Both large and small firms contemplating long-term growth may benefit from addressing the issues raised in this article.

In the context of firm growth, it is important to distinguish between the goals of the group and the goals of the individual. The emphasis in a well-organized law firm must be on the protection of the entity (and therefore the combined goals of the firm’s principals). This may mean that individual goals are, of necessity, sublimated to the needs, goals, and objectives of the organization.

A law firm’s partners must determine whether they will practice together in effect as “roommates,” with no obligations beyond the need to pay their share of the “rent” on a monthly basis, or whether they will institutionalize the firm by in effect entering into a “spousal” relationship, with all of its attendant long-term benefits and obligations.

No business organization can survive as an institution unless it has developed the following characteristics:

- A solid and adaptable financial and personal infrastructure;
- Workable methods of governance, with a strong, centralized, and responsive management structure devoted to protecting and enhancing the institution without doing unnecessary harm to its individual members;
- An adequate capitalization method to meet its current and future needs; and
- A process for selecting and disciplining its principals as well as for assisting the individual members of its constituency at their various life cycles.

**WHAT’S THE SECRET TO A GOOD RELATIONSHIP? GET IT IN WRITING**

Lawyers who spend a lifetime telling their clients to “get it in writing” are the same people who die without a will, or end up in litigation because they did not have a written agreement with their partners. They simply do not give
proper attention to their own business affairs and are blind to potential problems.

Every law firm with two or more owners needs a partnership agreement. The fact that a firm has operated successfully for years without one is not a valid reason to continue. Do not ignore the need for a partnership agreement just because you are practicing law with friends and colleagues in a harmonious relationship at the moment. The agreement proves its true value when a problem arises, which may not occur until 20 years or longer after the firm is founded. Once a problem surfaces, it will be too late. Firms break apart, often in litigation, for lack of an adequate agreement to guide the partners through difficult times.

Having said that it is essential that every well-organized law firm must have a written partnership agreement, what are the basics that should be covered, for even in idyllic relationships, unforeseen problems can cause strains and splits. A comprehensive partnership agreement should at least address these critical questions:

**THE PARTNERS:**

- How and under what conditions will new partners be admitted?
- To what extent does the partnership limit the partners’ outside activities?
- What are the voting rights of each partner?
- How do the partners manage the firm?

**CAPITAL CONTRIBUTIONS:**

- How is the capital contribution of a new partner set?
- Is a new partner required to buy into unbilled time and uncollected fees?
- Are the founding partners to be compensated for their sweat equity?
- Is there any provision for a “capital call”?

**ALLOCATION OF PROFITS:**

- How are income-sharing determinations to be made?

**RETIREEMENT:**

- Is the issue addressed at all- if only in the negative?
- Does the firm have a mandatory retirement age?
- How is the capital account returned to the retiring partner?
- Does the firm have retirement benefits, funded or unfounded?

**WITHDRAWAL:**

- How are clients notified?
- How are files handled?
- How does the firm allocate monies received after a partner’s departure?

**EXPULSION:**
- What actions or conditions can be the basis for expulsion?
- What is the process for expulsion?
- How are clients notified, and how are files handled?
- How does the firm handle monies received after a partner’s departure?

**DISABILITY:**
- Is the issue addressed at all – if only negatively?
- How is a disability determination made?
- How long will the partnership continue to pay a disabled partner?

**DEATH:**
- When does a deceased partner’s interest in the firm terminate?
- When is the deceased partner’s capital account paid back?
- How are undistributed profits handled?

**PAYMENT OBLIGATIONS:**
- Is the financial health of the partnership given priority?
- Are there lower payments and longer terms in case of multiple departures?

**PROFESSIONAL LIABILITY:**
- Assuming that the firm carries professional liability and employee practices insurance, are there provisions for the responsibility for the payment of the deductible(s)?
- What provisions are there regarding departed partners?

**DISSOLUTION:**
- Is there an orderly process for dissolution?
- Are the duties of the partners during dissolution, particularly with regard to completing existing matters, spelled out?

**DISPUTE RESOLUTION:**
- Have the partners agreed to a method for the resolution of any disputes through mediation/arbitration or reference?

The list of critical questions raises tough and difficult issues. Expulsion, disability, death and liquidation are not happy thoughts. Lawyers coming
together with friends and colleagues are anticipating good times and financial success. They ignore the possibility of failure. However, they should realize it is better to decide how to resolve a future problem in the abstract than wait for a real problem and real people with all the egos and emotions that will be attached.

Without a guiding agreement, the issues can be difficult. Does a partner get to keep money earned from teaching an evening class at the local law school? What can the firm do if a partner will not admit being impaired? What will happen if the active partners cannot support the unfounded retirement benefits of retired partners? What protection does the firm have if a partner withdraws to set up a practice across the street? How is the firm’s receivable protected after a client elects to go with a withdrawing partner?

None of these questions should be problematic, given an adequate partnership agreement.

**THERE IS NO SUBSTITUTE**

Law firms no longer can support unproductive partners, whether they are impaired, disabled or just plain lazy. Unfunded retirement benefits can raise havoc with a firm’s budget. The potential for disruptive controversies has never been greater.

Lawyers today are mobile. Spending a career with one firm will become the exception, not the rule. Some lawyers will leave firms to accept better offers; others will leave as a result of downsizing. Positions in existing firms may be in short supply. Because of these trends, an increasing number of lawyers will start their own firms.

In this environment, every firm must have a comprehensive partnership agreement. It is not too late for lawyers who are practicing together based only on a handshake to document their relationship. Firms with inadequate agreements need to evaluate their situations and make improvements.

Lawyers establishing a new firm must get it right from the start. There is no substitute for a comprehensive partnership agreement that protects the firm and each of its lawyers.

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