

BY ARTHUR D. BURGER

Accountable for Others

Recent decision underscores ethical responsibilities of lawyers in supervisory positions.

Ethics

A recent decision by the Delaware Supreme Court may be causing some discomfort for managing partners of law firms around the country, who may suddenly be concerned that they will be personally subject to bar discipline for failing to properly supervise firm employees.

In *In the Matter of James F. Bailey Jr.*, No. 334, 2002 (May 2, 2003 DE), the court suspended the managing partner of a small firm from the practice of law for six months and one day as a result of a series of financial and accounting mishaps at the firm, including its delays in paying its payroll and unemployment taxes.

One unusual component of the *Bailey* decision was the explicit link that it made between a firm's obligation to comply with tax laws and the personal ethical mandate of a managing lawyer.

Deciding what it said was a question of first impression in Delaware, the court held that "the managing partner of a law firm has enhanced duties, vis-à-vis other lawyers and employees of the firm, to ensure the law firm's compliance with its record-keeping and tax obligations."

The respondent, James Bailey, was the managing partner of a firm with two partners, several associates, and about a dozen employees, the court noted. The firm employed various bookkeepers and an outside CPA.

Audits of the firm by the bar showed, however, that the firm had failed to perform reconciliations of its trust account, had frequent overdraft balances in its operating account, and had failed

to make payroll and unemployment tax payments on time. Also of particular concern were transfers of funds from the trust account to the operating account that were used to pay a personal debt of Bailey's.

There was a dispute as to whether the wrongful transfer of funds was done at Bailey's direction or with his implicit permission. The court upheld the finding that he knew or should have known about it—and thus affirmed a finding of "knowing misconduct" against him. This was a key finding in upholding a six-month suspension in a case in which there was no suggestion of theft or criminal conduct.

Of wider significance was the court's broader holding with respect to the ethical responsibility of managing partners.

The court stated, "As managing partner, Bailey is responsible for maintenance of the Firm's books and records and is responsible for the filing and payment of all employee payroll taxes and corporate taxes associated with the operation of the Firm." This responsibility stems largely from Rule 5.3(b) of the Delaware Rules of Professional Conduct (identical to the D.C. rule and the American Bar Association model rule), which requires that a supervising lawyer "shall make reasonable efforts to ensure that the [nonlawyer employees'] conduct is compatible with the professional obligations of the lawyer."

The court also found that the failure to pay taxes on a timely basis was a violation of a lawyer's obligation under Rule 1.15(b) to promptly deliver to a third party any funds or property to which the other party is entitled.

In my opinion, the holding in *Bailey* does not necessarily place all ethical responsibilities on the individual with the title "managing partner." The determination of which lawyer or lawyers have supervisory authority with respect to a particular activity will depend on the facts of each case.

For one thing, a managing partner (or firm president in a professional corporation) may assign certain supervisory functions to another lawyer or lawyers in the firm who have knowledge and experience in that area. Decision making and oversight may

also be shared with a management committee. Also, every lawyer who handles a client matter, whether or not a member of firm management, is responsible for ensuring proper handling of funds and property that comes into his or her control. A lawyer is also responsible for exercising diligence in overseeing any nonlawyer employees whom the lawyer supervises or is assigned to supervise.

The central point is that in nearly all jurisdictions (New York and New Jersey are rare exceptions), a firm as an entity cannot be the subject of discipline. (*See my column "The Finger Points at You, Not Your Firm," Legal Times, April 17, 2000.*) (A firm as an entity, however, can be liable for sanctions under the current version of Fed. R. Civ. P. 11 and D.C. Superior Court Civil Rule 11.) Bar counsel, of course, also have no authority over non-lawyer employees. Thus a lawyer who is in a supervisory position is accountable for the diligence with which that supervision is carried out.

A lawyer is, of course, not ethically responsible for any and all acts of employees under all circumstances. (Tort liability is another matter.) Yet a lawyer can be found to have violated ethical obligations if he or she was not diligent in supervising an

employee, even if the lawyer did not participate directly in the conduct at issue.

Under Comment 1 to D.C. Rule 5.3, "The measures employed in supervising non-lawyers should take account of the fact that they do not have legal training and are not subject to professional discipline." This standard may call for training sessions, day-to-day guidance, monitoring and audits, and other steps. The precise nature of the supervision will depend on the complexity of the matter in which the employees are engaged. Hiring persons of competence and integrity is also a fundamental component of the obligation.

Bailey serves as a warning to managing partners and other lawyers with management authority that effective supervision is not just a matter of risk avoidance for the firm, but also a matter of personal ethical responsibility.

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