

# COPRAC Symposium

## April 20, 2013

Law Firm Dissolution/Partner Withdrawal

**Breaking up is hard to do**



### Panelists

Merri A. Baldwin  
Rogers Joseph O'Donnell PC

Matthew Heyn  
Klee, Tuchin, Bogdanoff & Stern LLP

Scott B. Garner  
Morgan Lewis & Bockius LLP

Pamela Phillips  
Arnold & Porter LLP

## Law Firm Partner Withdrawal

### HYPOTHETICAL NO. 1:

Lorna is a partner in a firm that seems to be in trouble. The profits are shrinking, lawyers have left, and morale is low.

Lorna decides she wants to move to another firm. She wants to make sure she brings as many clients with her as possible to whatever firm she goes.



Lorna wants to reach out and start letting clients know she plans to leave, and to start planting the seed of asking them to come with her to the new firm. She also wants to let her favorite two associates know, so that they can participate in the interviewing at other firms if they want.



- What actions can Lorna ethically take with respect to notifying current clients of the possibility she will leave?
- What are Lorna's options concerning notifying associates of her plans to leave and asking them to consider joining her?

## Client Comes First



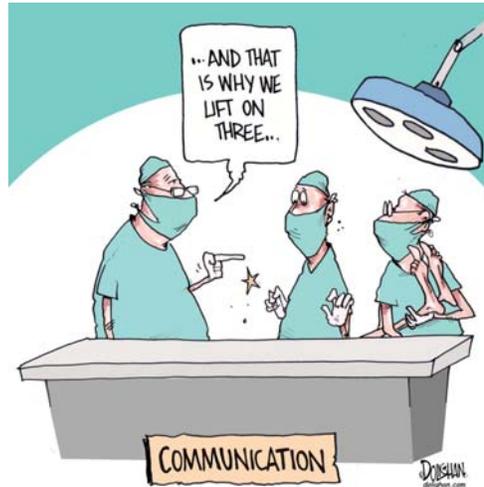
## Client Comes First

- “[T]he interests of the clients must prevail over all competing considerations if the practitioner’s withdrawal from the firm or the firm’s dissolution is to be accomplished in a manner consistent with professional responsibility.” Cal. State Bar Formal Opinion No. 1985-86.
- “Clients are not merchandise.” ABA Formal Opinion 300 (1961).

## Client Comes First

- Rule 3-700(A)(2): “A member shall not withdraw from employment until the member has taken reasonable steps to avoid reasonably foreseeable prejudice to the rights of the client, including giving due notice to the client, allowing time for employment of other counsel, complying with rule 3-700(D), and complying with applicable laws and rules.”

# Communication



# Communication

- Rule 3-500: "A member shall keep a client reasonably informed about significant developments relating to the employment or representation. . . ."
- Lawyer must keep client informed about changes in lawyer's employment status. State Bar Formal Opinion No. 1985-86; *see also* ABA Formal Opinion 99-414.

## Solicitation of Clients

- Contacting clients for purposes of convincing them to move with lawyer to new firm constitutes a “solicitation” under Rule 1-400.
  - A “solicitation” is any communication
    1. “Concerning the availability for professional employment of a member or a law firm in which a significant motive is pecuniary gain; and
    2. Which is (a) delivered in person or by telephone, or (b) directed by any means to a person known to the sender to be represented by counsel in a matter which is a subject of the communication.”

Rule 1-400(B).



## Solicitation of Clients

- Lawyers may solicit present or former clients consistent with Rule 1-400(C). *See also* Model Rule 7.3(a)(2); ABA Formal Opinion 99-414.
  - But may not solicit law firm clients with whom lawyer had no personal interaction. San Diego Bar Ass’n Formal Opinion 1975-11.
  - And may not solicit clients using any improper means. *See Reeves v. Hanlon*, 33 Cal. 4<sup>th</sup> 1140, 1147 (2004) (discussing application of tort of intentional interference with prospective economic advantage).

## Solicitation of Clients

- Must weigh rights and obligations to notify clients of departure with fiduciary obligations owed to the law firm. See *Fox v. Abrams*, 163 Cal. App. 3d 610, 616-17 (1985) (lawyers owe other lawyers in firm fiduciary duty, regardless of corporate form of law firm); see also *Graubard v. Moskowitz*, 653 N.E. 2d 1179 (1995) (discussing sliding scale of duties owed to other lawyers in law firm).

## Solicitation of Clients

- 2013 Harry B. Sondheim Professional Responsibility Award Recipient Paul Vapnek recommends a joint letter to the extent feasible, which includes the following:
  - The field or fields in which the withdrawing attorney will be practicing law;
  - The date of departure;
  - Whether the firm will continue to handle similar matters;



## Solicitation of Clients

[Continued]

- Who will be responsible for ongoing legal work during the transition period;
- That the client has the right to decide who will complete or continue his legal matters; and
- That the client may have all files, papers, and property.

Weil & Brown, CAL. PRAC. GUIDE: PROF. RESPONSIBILITY § 10:233 (The Rutter Group 2013); *see also* Cal. State Bar Formal Opinion 1985-86.

## Solicitation of Clients

- Notifications to clients may not be misleading or coercive. Rule 1-400(D).
- May not malign former law firm or withdrawing partners. ABA Formal Opinion 99-414.

## Solicitation of Associates

- Solicitation of at-will employees (*e.g.*, associates) ordinarily is not actionable.
- May become actionable as an interference with prospective economic advantage if the interference is accompanied by “an act ‘proscribed by some constitutional, statutory, regulatory, common law, or other determinable legal standard.’” *Reeves v. Hanlon*, 33 Cal. 4<sup>th</sup> 1140, 1152-53 (2004) (quoting *Korea Supply Co. v. Lockheed Martin Corp.*, 29 Cal. 4<sup>th</sup> 1134, 1159 (2003)).

## HYPOTHETICAL NO. 2:

After Lorna interviews with a firm she really likes, the interviewing partner asks Lorna for a list of her current clients and matters, past and expected billings and revenues for those clients and matters, and a list of all her clients and matters she has handled over the last ten years.

One of Lorna's clients is a small technology company in the middle of very confidential merger discussions. The client would not want the matter disclosed.

- Can Lorna provide that information? Are there constraints on her ability to provide that information?
- What information can Lorna request from the new firm concerning the firm's matters and clients, if any?

# Confidentiality

- It is an attorney's duty "[t]o maintain inviolate the confidence, and at every peril to himself or herself to preserve the secrets, of his or her client." Cal. Bus. & Prof. Code § 6068(e)(1).
- Rule 3-100(A): "A member shall not reveal information protected from disclosure by Business and Professions Code section 6068, subdivision (e)(1) without the informed consent of the client. . . ."



"Actually, I've found 90% of success isn't showing up, it's shutting up."

## Confidentiality

- Model Rule 1.6(b)(7): “A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary: . . . (7) to detect and resolve conflicts of interest arising from the lawyer’s change of employment or from changes in the composition or ownership of a firm, but only if the revealed information would not compromise the attorney-client privilege or otherwise prejudice the client.”

## Confidentiality

- Comment 13 to Model Rule 1.6: May disclose confidential information “once substantive discussions regarding the new relationship have occurred.”
- “Any such disclosure should ordinarily include no more than the identity of the persons and entities involved in a matter, a brief summary of the general issues involved, and information about whether the matter has terminated. Even this limited information, however, should be disclosed only to the extent reasonably necessary to detect and resolve conflicts of interest that might arise from the possible new relationship.”

## Confidentiality

- Examples where disclosure not allowed per Comment 13:
  - The fact that a corporate client is seeking advice on a corporate takeover that has not been publicly announced;
  - The fact that a person has consulted a lawyer about the possibility of divorce before the person's intentions are known to the person's spouse;
  - The fact that a person has consulted a lawyer about a criminal investigation that has not led to a public charge.

### HYPOTHETICAL No. 3

Lorna decides to join the new firm. Before she gives notice to her old firm, she downloads all her personal files from the firm's server onto a portable hard drive, as well as all the electronic files for matters in which she was involved while she was at the firm.



She updates her contact list on her iPhone with the contact information for her current and former clients, as well as colleagues at other firms. She notifies all her clients that she is leaving, tells them that they are free to select whatever counsel they wish to represent them, and offers to remain their counsel.

Several of the clients respond right away by email saying that they would jump ship and go with her.



Lorna then tells the managing partner she is leaving, and forwards the emails from those clients who want to come with her.

Within 15 minutes, the managing partner tells her she needs to leave that day and asks for her to be escorted from the building.

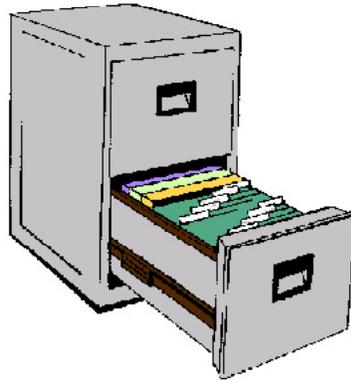


Later that day, the managing partner contacts all of Lorna's clients, tells them that Lorna has no trial experience, and offers to continue to represent the clients at a discount.



- Has Lorna behaved ethically?
- Has the managing partner behaved ethically?

## Client Files



## Client Files

- Rule 3-700(D): Terminated or withdrawing lawyer shall “promptly release to the client, at the request of the client, all the client papers and property.”
- Comment: “Paragraph (D) is not intended to prohibit a member from making, at the member’s own expense, and retaining copies of papers released to the client. . . .”

## Client Files

- ABA Formal Opinion 99-414 at 8: “To the extent that these documents were prepared by the lawyer and are considered the lawyer’s property or are in the public domain, she may take copies with her. Otherwise, the lawyer may have to obtain the firm’s consent to do so.”
- ABA Formal Opinion 99-414 at 8: “[A]bsent special circumstances, the lawyer does not violate any Model Rule by taking with her copies of documents that she herself has created for general use in her practice.”

## Client List

- Uniform Trade Secrets Act (Cal. Civ. Code §§ 3426 *et seq.*)
  - “Under the USTA, a client list qualifies as a ‘[t]rade secret’ if it [d]erives independent economic value, actual or potential, from not being generally known to the public or to other persons who can obtain economic value from its disclosure or use’ and ‘[i]s the subject of efforts that are reasonable under the circumstances to maintain its secrecy.” *Reeves v. Hanlon*, 33 Cal. 4<sup>th</sup> 1140, 1155 (2004) (quoting Cal. Civ. Code § 3426.1(d)(1), (2).
  - Can violate USTA by “using the list to solicit clients or to otherwise attain an unfair competitive advantage.” *Reeves*, 33 Cal. 4<sup>th</sup> at 1155 (internal citations omitted).

## Client List

- “[T]he USTA does not forbid an individual from announcing a change of employment, even to clients on a protected trade secret client list.” *Reeves*, 33 Cal. 4<sup>th</sup> at 1156.
- But lawyer may not use trade secret list to solicit clients. *Reeves*, 33 Cal. 4<sup>th</sup> at 1156.
- *Reeves* court noted that lawyer had not coordinated announcement with his former law firm.

## Play Nice



## Play Nice

- Generally no duty to provide additional services to client after new law firm takes over. Comment, Rule 3-700(D).
  - *But see* Cal. State Bar Formal Opinion 1992-127 (discussing criminal law context).
  - Must promptly sign substitution of counsel if asked to do so by client. *Kallen v. Delug*, 157 Cal. App. 3d 940, 950-51 (1984).

## Law Firm Dissolution

The Go Get 'Em Law Firm has just decided to  
“go no more.”

**GO GET 'EM**  
Attorneys at Law



Management has scheduled a partner meeting for the next week to vote on whether to dissolve the law firm. The firm believes that it has plenty of money in outstanding accounts receivable to meet its debts, but the landlord is cranky and, in one conversation, muttered something about bankruptcy. So everyone is a little nervous.



## HYPOTHETICAL NO. 1

Partners Able and Cain are anxious about what personal liabilities they might face if the firm dissolves and/or goes into bankruptcy.

Able is a senior transactional partner. Cain is a junior partner with a handful of clients who give her their litigation matters. She has three major lawsuits in progress.

Able and Cain show up in your office for advice.



Their first question is: “We keep hearing scary things about an old case called “*Jewel v. Boxer*.”

What does it say?

Does it have any application to us?

*Jewel v. Boxer*, 156 Cal. App. 3d 171 (1984).

- 4 partners
- Split up and formed 2 new firms.
- No partnership agreement, no unfinished business agreement.
- One firm completed several contingency fee matters that had originated at the dissolved firm.
- The other two sued their former partners, seeking an accounting of the profits earned on the unfinished business matters.

*Jewel v. Boxer*, 156 Cal. App. 3d 171 (1984).

- Under the Uniform Partnership Act (UPA); “absent a contrary agreement, any income generated through the winding up of unfinished business is allocated to the former partners according to their respective interests in the [old] partnership.” *Id.* at 176.
- Rationale for decision: fiduciary duty and an equitable principle – the “extra” compensation should be shared among all the partners
- The former partner’s overhead can be deducted from the profits he or she derives from completing any unfinished business. *Id.* at 180.

The Unfinished Business Landscape Prior to Current Wave of “Jewel Litigation”

- When a law firm dissolves, it may have work that is not finished.
- Issue: If the partners take that work to their new firms, do they have to share the income with their former partners?

### The Answer: Unfinished Business Rule

- The partners and partnership are free to decide whether there is—or isn't—a duty to account for those profits.
- *If they don't agree as of date of dissolution*, the Revised Uniform Partnership Act supplies the answer: the former partners of a dissolved law firm have a fiduciary duty to account back to each other.

### “Profile” of Typical *Jewel* Case

- Firm breaks up without an agreement about unfinished business
- Some of the partners finish some contingency fee cases and bring in a recovery
- The other partners – now at other firms – want a piece of the recovery
- They sue for an accounting

## Equitable Accounting Required

- Full and mutual accounting by *all* former partners.
- Pool profits/losses of each partner.
- Deduct each partner's overhead
- RUPA: also deduct reasonable compensation for finishing work

## Lay of Land Prior To Recent Suits

- Courts encouraged lawyers to have Unfinished Business Agreements.
- No published *Jewel* case involved a law firm break-up where they *had* an Unfinished Business Agreement
- No California case had decided whether RUPA's "reasonable compensation" rule eliminates need for accounting

### What is Issue Being Litigated Today?

- Can creditors of a law firm use the Unfinished Business Rule as a creditor s remedy?
- Can they argue fiduciary duty to account = property interest of dissolved law firm that was improperly “transferred” away?
- Can they collect those profits not from the former partners, but from their new law firms?

### Recent Decisions

- Brobeck
- Coudert
- Thelen
- Heller

*In Thelen LLP Bankruptcy (SDNY 9/4/12)*

“Over the last three decades, courts have cited *Jewel* reflectively and uncritically. Thus, from modest beginnings in a dispute involving a small Alameda County general practice firm, the *Jewel* doctrine has grown to ensnare some of the largest law firms in the United States.”

*In Thelen LLP Bankruptcy (SDNY 9/4/12)*

“Notwithstanding its humble beginnings, some lower courts have applied the *Jewel* doctrine expansively, with untoward consequences for the bar and clients. In this Court’s view, there is good reason to believe that the highest courts of New York and California would decline to follow suit.”

## *Thelen's* Holdings: New York Law

- “Concept of hourly rate matters being the law firm’s ‘property’ collides with the essence of attorney-client relationship. That relationship stems from agency law, not property law.”
- A pending client matter “is not an ordinary article of commerce.”

## *Thelen's* Holdings – New York Law

- If “asset,” would infringe client’s right to terminate attorney at will
- If “asset,” would violate fee-splitting rule.
- If “asset,” would restrict practice of law.
- If “asset,” would be inconsistent with rule for contingency fee matters – value as of date of dissolution, not after.
- If “asset,” bankruptcy trustee could sell client matters to highest bidder

## *Thelen's View of California Law*

- California law recognizes hourly rate matters as “assets of a dissolving firm,” citing *Jewel, Rothman and Fox v. Abrams*.
- California law firm defendant (Robinson & Cole) argued that RUPA’s enactment allowing reasonable compensation for finishing up unfinished business abrogated the *Jewel* doctrine and its progeny, which rely on the “no extra compensation” rule.
- Court found that argument persuasive, but found what is reasonable compensation is fact-intensive, so could not grant motion to dismiss.

## *Thelen's Holdings: California Law*

- As for all of the policy arguments used for deciding the question under New York law?
- They are “less persuasive in the context of California law, because California cases have rejected them” – *Jewel, Fox*.
- “NY’s commitment to attorney mobility appears to be stronger than California’s.” *Howard v. Babcock*.
- Certification of question to highest courts of NY and California is warranted because those courts have not squarely addressed these issues, and the scope of the Unfinished Business Rule is of great importance to both the legal profession and the clients.

### *Brobeck's* Dissolution (2003)

- Working toward a merger.
- On January 29, 2003, merger discussions fell apart.
- Firm dissolved 11 days later.
- Brobeck had approximately 163 partners.
- Brobeck had more than 10,000 clients.

### Brobeck's Unfinished Business Agreement

“Except as specifically set forth below, neither the Partners nor the Partnership shall have any claim or entitlement to clients, cases or matters ongoing at the time of the dissolution of the Partnership other than the entitlement for collections of amounts due for work performed by the Partners and other Partnership personnel on behalf of the Partnership prior to their departure from the Partnership. **The provisions of this Section 9(e) are intended to expressly waive, opt out of and be in lieu of any rights any Partner or the Partnership may have to “unfinished business” of the Partnership, as that term is defined in *Jewel v. Boxer*, or as otherwise might be provided in the absence of this provision through interpretation or application of the California Revised Uniform Partnership Act.**”

## Defendants' Contentions

- The Unfinished Business Agreement was a lawful agreement under RUPA.
- Brobeck did not have a property right in future profits other firms would earn on hourly work Brobeck could not do and such a right would violate ethical rules.
- The Unfinished Business Agreement did not transfer any property in which Brobeck had a property interest.
- If Brobeck had an interest in matters pending on the date of its dissolution, then Brobeck received reasonably equivalent value in exchange for any transfer of that interest.

## The Trustee's Contentions Regarding Fraudulent Transfer

- Estate/creditors entitled to recover all profits new firms earned on work clients transferred.
- Reason: Brobeck estate had a "property interest" in those matters.
- Brobeck did not receive reasonably equivalent value in exchange for the transfer.

## The Bankruptcy Court's July 2, 2009 Memorandum Decision

- “This case presents the court with a matter of apparent first impression: a dramatic intersection of well-established and necessary rules appropriate for the winding up and dissolution of a law firm with the equally well-established principles recognizing rights of third-party creditors that protect them from the adverse financial consequences of an otherwise valid transaction.”
- “In a time when the financial collapse of legacy institutions can occur quickly, a last minute attempt at order rather than chaos cannot prevail over the rights of that firm’s creditors”

### *Brobeck*: Key Rulings

- Hourly rate matters are assets of firm
- Not persuaded by ethical arguments
- The *Jewel* Agreement did not impart value to Brobeck – no consideration
- Dismissed some claims but granted partial summary judgment to Trustee

Coudert case: *Development Specialists, Inc. v. Akin Gump Strauss Hauer & Feld LLP*, 2012 WL 2952895 (S.D.N.Y. Jul. 18, 2012)

- Coudert firm did not adopt a Jewel agreement, so no fraudulent transfer claims
- Issue: whether pending hourly rate client matters belonged to Coudert at the time of dissolution.

Coudert case: Key Rulings

- *In the absence of any evidence that Coudert's partners intended to exclude pending client matters from the firm's assets*, those matters are assets of the firm. *Id.* at \*4.
- Under New York law, former partners are obligated to account for any profits they earned while winding up pending client matters, regardless of whether the matter is hourly rate or contingent fee. *Id.* at \*10.
- Application of the duty to account to hourly rate matters is not contrary to New York public policy. *Id.* at \*23.
- Damages are not zero as a matter of law. *Id.* at \*5.

Coudert case: Take-away Points

- But this is a difficult issue, and I could be wrong.
- The District Court certified the case to the Second Circuit
- Second Circuit granted the parties' cross-motions for leave to appeal.

Heller Case – 3/18/13 Order

- Despite *Coudert* and *Thelen* decisions, simply re-adopted *Brobeck* decision on property issue.
- Property: the duty to account.
- Transfers occur (1) when firm “releases” duty to account and (2) shareholder joins new law firm and “brings along” the unfinished business free of a duty to account.

## Summing Up

- New York law:
  - (a) hourly rate matters are assets (*Coudert*)
  - (b) hourly rate matters are not assets (*Thelen*)
  - (c) Second Circuit granted review in *Coudert*
- California law:
  - (a) hourly rate matters are assets
  - (b) dismiss ethical arguments – Court of Appeal decisions; *Brobeck*; and *Heller*
  - (c) no California Supreme Court decision on point
  - (d) *Thelen* predicts Supreme Court would agree with it

## HYPOTHETICAL NO. 2:

Reeling with shock, Able and Cain rapidly pepper you with more questions.

“Is there anything we can do to avoid the implications of these various decisions?”

“When will these issues be resolved?”



### HYPOTHETICAL NO. 3:

Able is nearing retirement. He asks, “Do I face any other financial risks of losing money the firm owes me?”

Able continues – “I’ve socked a lot of money away in my capital account to help fund the firm’s operations. I also got a nice bonus last month for being such a good mentor to the associates. Is that at risk?”



Cain pipes up: “Hey, I’m just a non-equity partner. The firm advanced me some additional money the last three months on the understanding that certain clients who were behind on their bills would come current before the end of the year.”

Cain asks, "Am I at risk?" "If so, for what?"

Able chimes in – "Yes, what are the risks to me personally?"



#### HYPOTHETICAL NO. 4:

As they gather their papers to leave your office, Able turns to you and asks, "Is it better to hang in at Go Get 'Em or should we skedaddle now?"

Cain asks, "What are the pros and cons?"



**THE END**

