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Conflicting Views as to the Unfinished Business Doctrine

By Thomas E. Rutledge and Tara A. McGuire

As the era of failed law firms, both big and small, continues, so does debate as to the Unfinished Business Doctrine as most famously embodied in *Jewel v. Boxer*. The last six months have seen courts come to diametrically opposing views as to the doctrine's application. This article provides only an introduction of the doctrine and its recent interpretations, but demonstrates why the doctrine's application mandates that law firms and other professional firms consider and address the doctrine in their organizational agreements. Failure to do so only increases the likelihood of disputes, the expense of dispute resolution, and perhaps surprise as to the ultimate determination.

In *Jewel v. Boxer*, 156 Cal. App. 3d 171, 203 Cal. Rptr. 13 (Cal. Ct. App. 1984), the court considered the treatment of a contingency fee earned by one of two successor firms on a case that had been initiated with the predecessor firm. Rejecting a formulaic division devised by the trial court, the California Court of Appeal focused upon the language of the controlling partnership law – the attorneys had no written partnership agreement addressing the division of fees upon dissolution of the firm. Focusing upon the applicable partnership law, the court found that (a) after dissolution, a firm continues for the purpose of completing partnership business (UPA § 30), and (b) no partner is entitled to additional compensation (i.e., compensation beyond the agreed sharing ratio under the original partnership agreement) for completing that partnership's unfinished business. UPA § 18(f). Relying upon prior law, including *Resnick v. Kaplan*, 434 A.2d 582 (Md. App. 1981), the *Jewel* court held that all income derived from cases pending when the firm dissolved constitute firm assets that will be shared among the partners in accordance with their existing agreement. In rendering this decision, the *Jewel* court expressly addressed claims that the rule it espoused interfered with a client's right to select counsel. Initially, it observed that:

> even though the client had the right to the attorneys of its choice, that right was irrelevant to the rights and duties between the former partners with regard to income from unfinished partnership business. . . . [T]he right of a client to the attorney of one's choice and the rights and duties as between partners with respect to income from unfinished business are distinct and do not offend one another.

As for the claim that completing unfinished partnership business on these terms is disadvantageous to the partners performing the work because they would receive "only a portion of the income generated by such work," the court observed, "this is all the former partners would have received had the partnership not dissolved." Further, the burden would be shared by all former partners as to all unfinished business, so there is no particular burden imposed on any particular partner or partners to the exclusion of others.

It should be noted that while it may have been that all of the unfinished business of the Jewel, Boxer and Elkind firm was based upon contingency fee arrangements, that is not stated in the opinion, and the court did not base its determination on the contingency fee basis of the work.

Until recently, most states that have considered the question have applied the rule of *Jewel v. Boxer* as to contingency as well as hourly fees matters pending at the time of the firm's dissolution. It has as well been applied to firms of professionals other than attorneys. One benefit of the *Jewel* rule is that it preserves the agreement of the parties and avoids separate challenges based in bad-faith and breach of fiduciary duty. In fact it is fair to describe the *Jewel* rule as the consensus for the next 30 years. That consensus would be challenged and indeed broken in 2014.

Thelen LLP voted to dissolve in 2008 shortly after adopting a new partnership agreement containing a *Jewel* waiver, i.e., an agreement that the firm would have no claim on the proceeds of any cases or matters ongoing at the time of dissolution save collection of then accrued but unpaid fees. Just less than a year later, Thelen entered Chapter 7 bankruptcy. Thelen's Chapter 7 trustee sought to have the *Jewel* waiver set aside as a constructive fraudulent transfer and to collect for the Thelen estate the fees earned on the transferred unfinished business. Seyfarth, one of the firms to which Thelen attorneys had moved, was successful in its argument to the trial court that the unfinished business doctrine does not apply to hourly matters. *Geron v. Robinson & Cole LLP*, 476 B.R. 732, 742–43 (S.D.N.Y. 2012). The story was largely similar at Coudert Brothers LLP. Its partners agreed to dissolve in August 2005, and granted the executive committee the right to waive partnership claims; although not express in this decision, the granted waivers presumably included claims on fees earned after separation and transfer of cases and matters to different firms. Coudert filed for bankruptcy in September 2006. Developmental Specialists, Inc. (DSI), as administrator of Coudert's estate, brought suit against firms to which Coudert attorneys moved, seeking the proceeds of the transferred work. The defendants asserted that the *Jewel* doctrine does not apply to hourly (as contrasted with contingent) fee arrangements; the bankruptcy court did not accept that argument. Rather, it held that the *Jewel* doctrine did apply, and that "the Client matters were Coudert assets on the dissolution Date. Because they are Coudert assets, the Former Coudert Partners are obligated to account for any profits they earned while winding the Client Matters up at the Firms." *DSI v. Akin Gump Strauss Hauer & Feld LLP*, 477 B.R. 318, 326 (S.D.N.Y. 2012).

Seeking resolution of these determinations, the Second Circuit Court of Appeals certified to the New York Court of Appeals the question:

> Under New York law, is a client matter that is billed on an hourly basis the property of a law firm, such that, upon dissolution and in related bankruptcy proceedings, the law firm is entitled to the profit earned on such matters as the 'unfinished business' of the firm?"

In re Thelen, 24 N.Y.3d 16 at 25, 20 N.E.3d 264 N.Y. 2014).

The New York Court of Appeals would hold in the negative; the proceeds of transferred hourly matters are not assets of the prior firm and may not be claimed by the bankruptcy estate in order to satisfy those creditor claims. Not squarely addressing *Jewel's* reliance on UPA §§ 18(f) and 30, the *Thelen* court focused upon what is "property" of the partnership, holding that as a firm has no enforceable property interest in the matters entrusted to it by clients, there is no property right against which the firm may make a claim after dissolution. Furthermore, the court held that the unfinished business doctrine as applied in *Jewel* "would have numerous perverse effects," including that "By allowing former partners of a dissolved firm, to profit from work they do not perform, all at the expense of a former partner and his new firm, the trustees' approach creates an 'unjust windfall'. . . ." Expanding on this point the court also wrote "[A]ttorneys would simply find it difficult to secure a position in a new law firm because any profits from their work for existing clients would be due their old law firms, not their new employers." Ultimately, the *Thelen* decision rests upon the impact of a *Jewel* doctrine obligation among partners upon the perceived ability of clients to retain counsel of their choosing.

Going against *Thelen* is a recent decision of the Colorado Supreme Court in which it upheld the *Jewel* rule in the context of a law firm organized as a Colorado LLC. *LaFond v. Sweeney*, Case No. 12SC205, 2015 WL 333701 (Colo. Jan. 20, 2015). LaFond & Sweeney LLC (L&S) was organized in 1995 and dissolved in 2008. At the time of its dissolution, several cases, most notably the contingency fee Maxwell False Claims Act action, was pending. The *Maxwell* case went with LaFond to his new firm. Sweeney and LaFond were unable to come to agreement as to the division of any ultimate settlement in the *Maxwell* case. The trial court issued a quantum meruit judgment in favor of the L&S firm in the amount of up to $597,180 to then be divided equally between LaFond and Sweeney. Shortly after this decision was rendered, Maxwell's qui tam action generated a judgment of some $23 million with additional attorney fees of $2.2 million; the case ultimately settled for some $26 million and $2.6 million in attorney fees (with the contingency fee still in place; that percentage is not recited in the decision). Maxwell appealed, and the Colorado Court of Appeals held that the quantum meruit analysis of the trial court was improper, and that all proceeds of the contingency fee arrangement are firm property to be divided in accordance with LaFond and Sweeney's agreed sharing ratios of 50 percent each. This determination would be affirmed by the Colorado Supreme Court.

The Colorado LLC Act requires each member to "hold as trustee for it any property, profit or benefit derived . . . in the winding up" of the LLC's business (Colo. Rev. Stat. § 7-80-404(1)(a); *accord* UPA § 21). Unlike Colorado's current partnership act (an adoption with modification of the Revised Uniform Partnership Act), which does afford a partner the right to compensation for services rendered in completing business pending at the time of the partnership's dissolution (*see* Colo. Rev. Stat. § 7-64-401(8); *accord* RUPA § 401(h)), the Colorado LLC Act is silent as to such a right of compensation.

Substantively, the court first determined that a contingency fee case is firm property:

> That a pending contingency fee case is business of a dissolved LLC follows from the fiduciary nature of the attorney-client relationship. With respect to law firms, absent a special agreement, the client employs the firm and not a particular lawyer. During the dissolution of a law firm, attorneys continue to owe clients ethical and legal duties such as ensuring that the client's matter is handled properly.

Tellingly, and here significantly departing from the *Thelen* decision, the Colorado court found that notwithstanding Maxwell's decision that LaFond should after the dissolution handle the matter:

> Maxwell's choice in this regard did not alter the contingent fee agreement that was in existence at the time of L&S's dissolution; nor did it alter the rights and duties LaFond and Sweeney owed to each other under their business arrangement. The contingent fee agreement remained in place, and LaFond had a duty to carry forward the representation undertaken by the LLC. Accordingly, the *Maxwell* case constituted business of the LLC for the purposes of determining the rights and duties of LaFond and Sweeney toward each another.

In response to LaFond's argument that this application of the unfinished business doctrine interferes with the client's right to counsel in that "an attorney would be unwilling to represent the client unless the attorney is entitled to additional compensation for his work," the Colorado Supreme Court wrote:

> We are unaware of any authority for the proposition that fiduciary duties attorneys owe to their firms may be eschewed under the circumstances of a case like the one before us. The division of the contingent fee between LaFond and Sweeney does not affect the amount of money Maxwell had to pay upon successful resolution of his case. Hypothetical harm, as opposed to actual harm to the client's ability to choose counsel in the case, is not a pertinent consideration when determining the rights and obligations of attorneys to their firms. *See Jewel*, 203 Cal.Rptr. at 17 ("[T]he right of a client to the attorney of one's choice and the rights and duties as between partners with respect to income from unfinished business are distinct and do not offend one another.").

Clearly, *In re Thelen* and *LaFond v. Sweeney* cannot be easily reconciled. While at first blush it might be said that one is a case about hourly fee arrangements and the other contingency fees, that differentiation does not stand up to scrutiny. The determination made in *Thelen* as to what is firm property is applicable to both types of engagements. Likewise, the *LaFond v. Sweeney* determination as to what constitutes ongoing business at the time of dissolution is equally applicable to contingent and hourly arrangements.

As is often the rule in business organizations, this question can be avoided by careful drafting of the organic document. Some firms will include a *Jewel* waiver. *See also* Robert W. Hillman, *Hillman on Lawyer Mobility* § 4.6.1.1 (2nd Ed. 1998 and 2024 supp.) (discussing *Jewel* waivers). To include such a provision is their decision and one which should be taken only after consideration of the impact of that provision on firm unity and possible negative consequences to those attorneys who post-dissolution do not share in the fee generated on a case pending at the time of dissolution. Imagine the firm of ABCD, which dissolves while a significant fee matter (whether it is contingent or not does not matter) is ongoing, is party to a lease on which each of A, B, C, and D are personally responsible either by reason of partner status or a personal guarantee. At the time of dissolution the remaining obligation on the lease is $200,000. A month after dissolution that fee comes in; by happy coincidence it is $200,000. If the $200,000 goes to successor firm CD, each of C and D has income with which to discharge their obligations under the lease; neither A nor B is so benefited. Conversely, if the $200,000 is property of ABCD, all of their obligations under the lease can be extinguished. In light of that eventuality, it can be determined that a *Jewel* waiver should be rejected in the organic agreement.

But then these cases address what happens when the members of the firm do not enter into an agreement as to resolution of the matter. Clearly there is now a split as to the proper default rule. In California, New York, and Colorado, it is in part clear as to what is the default rule. Obviously, the questions remains open in the vast majority of jurisdictions in this country, and as well in different organizational forms; how might *LaFond* be decided under Colorado's enactment of RUPA, and how might *Jewel* be decided under California's new LLC Act?

While available space does not permit a complete explication of the question, the *LaFond* decision, in continuing the rule of *Jewel*, is the better policy. Simply put, the *Thelen* court's reliance upon client ability to select counsel is a red-herring. The fact that a firm to which an attorney has transferred his or her practice may be unwilling to permit an attorney to continue working an engagement because the proceeds thereof will go back to the predecessor firm presents no greater impediment than does a firm setting a billing rate that clients may not be able to afford. The *Thelen* court's analysis could also support a client's ability to dictate that none of the fees it pays are to be applied to firm overhead or shared with other attorneys in accordance with the firm's agreement; in that way the client could enhance the degree to which the attorney is focused on its issues and that engagement. Further, *Thelen* would treat law partnerships as somehow "different" even though they are governed by the same partnership law as governs other partnerships. *LaFond/Jewel* protect the agreement of the parties to the venture and protect against potentially abusive conduct in timing firm dissolutions even as they protect the rights of third-party creditors of the now dissolved firm.

Thomas E. Rutledge is a member of Stoll Keenon Ogden PLLC – resident in the Louisville, Kentucky office. Tara A. McGuire is a student at the University of Louisville School of Law who will graduate in the spring of 2015.