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Firms to see shift on unfinished business claims

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In recent years, there have been a number of spectacular collapses of top-quality, large international law firms: Howrey LLP, Dewey & LeBoeuf LLP, Thelen LLP, Coudert Brothers and Heller, Ehrman LLP come to mind.

Several such failures have brought waves of claims by bankruptcy trustees on behalf of firm creditors against former partners and their new law firms under the so-called unfinished business doctrine.

This doctrine grows out of principles of partnership law and an often-cited California appellate opinion, *Jewel v. Boxer,* 156 Cal.App.3d 171 (Cal. App. 1984). The doctrine holds that, in the absence of a partnership agreement provision to the contrary, fees from ongoing client matters of a dissolved law firm are to be shared by the former partners, regardless of which partner performs legal work for the client after dissolution.

A *Jewel* claim is based on the premise that hourly client matters are the property of the dissolved law firm, and profits received for post-dissolution work on those matters at other firms belong to the dissolved firm and, hence, to that firm's creditors.

Initially, trustees litigating *Jewel* claims met with considerable success. One federal judge in the Southern District of New York and one bankruptcy judge in the Northern District of California found in 2012 that these claims were sound. Many large law firms where former partners of failed firms had gone to practice rushed to settle these cases.

However, two recent opinions — one by the New York Court of Appeals construing state law, *In re Thelen LLP*, and one by a federal district judge construing California law, *Heller, Ehrman LLP v. Davis, Wright, Tremaine LLP* — have dealt severe blows to the viability of the unfinished business doctrine and the vitality of *Jewel*.

Where do these developments leave Illinois law? What is the likely result of such a claim governed by Illinois law?

Currently, these are unanswered questions in Illinois. *Jewel* construed the Uniform Partnership Act, which was then in effect in California. Since that time, California and many other states, including Illinois, have adopted the Revised Uniform Partnership Act, also known as the Uniform Partnership Act (1997).

One Illinois Appellate Court opinion and one opinion by a federal judge in the Northern District of Illinois both considered and followed *Jewel* before the UPA was repealed in Illinois in 2008 and replaced by the RUPA. *Ellerby v. Speizer*, 138 Ill.App.3d 77 (2nd Dist. 1985); *Sufrin v. Hosier*, 896 F.Supp. 766 (N.D. Ill. 1995).

Significantly, while *Thelen* involved the construction of the UPA still in effect in New York, the district court in *Heller, Ehrman* analyzed unfinished business claims in California under the RUPA.

There, the court noted five reasons to distinguish *Jewel*, one of which was that *Jewel* applied the UPA. According to the court, the RUPA has the distinction of allowing partners to obtain reasonable compensation for helping wind up partnership business "and thus undermines the foundation on which *Jewel* rests."

The statutory provisions on which the *Heller, Ehrman* court relied are also now the law in Illinois. First, a partner is entitled to compensation for services rendered in closing out partnership business. 805 ILCS 206/401(h). This means that a partner at a new firm is entitled to be paid for work winding up the post-dissolution business of his or her old firm.

Second, a partner's obligation not to compete with the partnership ends upon dissolution. 805 ILCS 206/404(b)(3). This means a partner of a dissolved firm violates no duty when he or she signs a retainer agreement for an ongoing client matter at a new firm. Therefore, the sound reasoning of *Heller, Ehrman* should apply in Illinois as well.

Whether under the UPA or RUPA, other strong policy reasons favor rejection of unfinished business claims for hourly fee matters, as both the New York Court of Appeals and the district court in California explained.

First and foremost is the principle that engagements by clients of law firms are not property because clients always retain the right to discharge their attorneys for any reason or no reason at all. Clients own matters, and at most, law firms have expectations of future business.

Second, a practical reason follows from this principle, which is the lawyers and law firms who do clients' work ought to be paid for it. No one can expect that the lawyers chosen by clients, and their firms, will continue the work in a matter but not be paid for that work. Nor should a client be denied the lawyer of its choosing because, in effect, under the *Jewel* rule, the client cannot pay the lawyer for services performed.

That there is no property interest in client matters is obvious in other scenarios apart from dissolution. When a partner resigns from one firm in good standing and joins another, it is no breach of duty if a client then retains the lawyer's new firm to continue a matter. Similarly, if a client discharges a law firm and hires another, the firm has no right to be paid for anything other than work already done.

The last chapter in this debate is yet to be written. The trustee has appealed *Heller, Ehrman* to the 9th U.S. Circuit Court of Appeals. Illinois has not squarely confronted the question since the enactment of the RUPA. But Illinois is likely to follow *Thelen* and the district court's reasoning in *Heller, Ehrman*, and it should.

Rejecting *Jewel* claims in the context of defunct law firms benefits clients, lawyers and law firms. Doing so does disfavors creditors of bankrupt firms, but so do the equities.