

SDNY Issues Conflicting Opinions Regarding Rights to Dissolved Firm Hourly-Fee Matters

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[*Development Specialists, Inc. v. Akin Gump Strauss Hauer & Feld LLP*, ___ B.R. ___, 2012 WL 1918705 \(S.D.N.Y. May 2012\)](#)

[*Geron v. Robinson & Cole LLP*, ___ B.R. ___, 2012 WL 3800766 \(S.D.N.Y. Sept. 2012\)](#)

Brief Summary

Within the span of a few months, the U.S. District Court for the Southern District of New York issued two opinions (from different judges) regarding whether a dissolved law firm has a property interest in its unfinished hourly fee matters at the time of dissolution. The opinions came to opposite conclusions under New York law and an important new conclusion under California law.

Complete Summary

Judges Colleen McMahon and William H. Pauley III, both of the Southern District of New York, have come to opposite conclusions under New York law regarding whether a dissolved law firm has a property interest in its unfinished hourly fee matters at the time of dissolution. Judge Pauley also rejected the so-called “*Jewel* doctrine” under California’s Revised Uniform Partnership Act (RUPA) and held that there is no basis to require former partners to remit all fees and profits on hourly matters to the bankruptcy estate of their former law firm.

The judges used similar analytical frameworks and points of authority for New York law, the most central being the duty of former partners to account to one another for the winding up of the former partnership’s unfinished business (the “unfinished-business” rule), including the rule prohibiting former partners from receiving special compensation for their post-dissolution efforts (the “no-compensation” rule). Applying the unfinished business rule, the New York Court of Appeals has held, in the context of a *non-law* firm partnership dissolution, that

executory contracts to perform professional services are partnership assets. Similarly, the U.S. Court of Appeals for the Second Circuit and three New York Appellate Divisions have held that law firm contingent fee contracts are partnership assets upon dissolution.

In May 2012, Judge McMahon held that Coudert, a dissolved law firm partnership first organized in 1853, has a property interest in its pending hourly fee matters. Judge McMahon relied on the aforementioned authorities and held that there were no persuasive legal bases for distinguishing between non-law partnerships and law firm partnerships, or between contingent fee and hourly fee matters in this context. She further noted that:

Every court in a UPA jurisdiction that has considered the precise question posed here has concluded that billable hours matters are partnership assets in the absence of any expressed intention that they should be treated otherwise.

In September 2012, Judge Pauley addressed the same issue with respect to the bankrupt law firm Thelen LLP, also under New York law, and held that the dissolved law firm does not have a property interest in pending hourly fee matters. Judge Pauley held that applying the unfinished business doctrine to hourly fee matters would: (1) result in a windfall for the dissolved firm and reduced compensation for the attorneys performing the post-dissolution work; (2) violate the New York Rules of Professional Conduct prohibiting division of fees between different firms without client consent; and (3) violate New York public policy against restrictions on the practice of law.

Judge Pauley distinguished the aforementioned contingent fee authorities, noting that in those cases the dissolved firm generally only has a property interest in the value of the case upon dissolution and no property interest in the fees resulting from the surviving partner's post-dissolution efforts, skill and diligence. And regarding New York authority dealing with non-law firm partnerships, Judge Pauley held that contracts for legal services are categorically different from contracts for other professional services and should not be treated as "ordinary articles of commerce" because of New York's strong policy favoring client autonomy and attorney mobility.

Importantly, Judge Pauley also addressed the same issues under California law and rejected the so-called "*Jewel* doctrine" that had allocated the fees from unfinished hourly business to the estate of the bankrupt firm. Although *Jewel* arose in California under the Uniform Partnership Act, Judge Pauley held that the subsequent adoption of the Revised Uniform Partnership Act in California "transformed the law ... and eroded the theoretical underpinnings of the *Jewel* doctrine." Judge Pauley left open for factual determination in this case whether there were any profits earned by the successor attorneys' work that exceeded "reasonable compensation" such that the dissolved firm may have some right to those excessive profits.

Significance of Opinions

These district court opinions thoughtfully address important issues for bankrupt law firms under both New York and California law. Although the district court was not authorized to certify the questions of New York law to the New York Court of Appeals, the Second Circuit does have that option if it chooses to do so. Whatever the ultimate decision under New York law, Judge Pauley's decision repudiating the *Jewel* doctrine in California under RUPA may have significant persuasive value in other jurisdictions that have adopted RUPA.

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