12-4138-BK

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

IN RE: THELEN LLP

YANN GERON, as Chapter 7 Trustee of the Estate of THELEN LLP,

Plaintiff-Appellant,

v.

SEYFARTH SHAW LLP,

Defendant-Appellee,

PARTNER DOES,

Defendant.

On Appeal from the United States District Court for the Southern District of New York (New York City)

AMICUS BRIEF OF THE ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK, SUPPORTING AFFIRMANCE IN FAVOR OF APPELLEE

Damian Schaible
THE ASSOCIATION OF THE BAR
OF THE CITY OF NEW YORK
42 West 44th Street
New York, New York 10036
Telephone: (212) 382-6600

David A. Lewis
THE ASSOCIATION OF THE BAR
OF THE CITY OF NEW YORK
42 West 44th Street
New York, New York 10036
Telephone: (212) 382-6600

Attorneys for Amicus Curiae The Association of the Bar of the City of New York

Corporate Disclosure Statement Pursuant to Fed. R. App. P. 26.1

The Association of the Bar of the City of New York has no parent corporation and there is no public company that owns 10% or more of its stock.

TABLE OF CONTENTS

Page(s)

TABLE OF CONTENTS ii

TABLE OF AUTHORITIES iii

INTEREST OF AMICUS CURIAE 1

STATEMENT PURSUANT TO FEDERAL RULE OF APPELLATE PROCEDURE 29(C)(5) 2

ARGUMENT 3

INTRODUCTION 3

I. Applying The Unfinished Business Doctrine To Hourly Fee Matters Conflicts With Established New York Law 5

II. Applying The Unfinished Business Doctrine To Hourly Fee Matters Conflicts With Basic Principles That Govern The Attorney-Client Relationship Under New York Law And The Rules Of Professional Conduct 10

CONCLUSION 17

TABLE OF AUTHORITIES

Page(s)

CASES

Campagnola v. Mulholland, Minion & Roe, 76 N.Y.2d 38 (1990) 11

Cohen v. Lord, Day & Lord, 75 N.Y.2d 95 (1990) 12

Crowley v. Wolf, 281 N.Y. 59 (1939) 11

Demov, Morris, Levin & Shein v. Glantz, 53 N.Y.2d 553 (1981) 10, 11

Denberg v. Parker Chapin Flattau & Klimpl, 82 N.Y.2d 375 (1993) 12, 13

Development Specialists, Inc. v. Akin Gump Strauss Hauer & Feld LLP, 480 B.R. 145 (S.D.N.Y. 2012) 6, 12, 13

Grant v. Heit, 263 A.D.2d 388 (1st Dep't 1999) 8

In re Heller Ehrman LLP, No. 08-32514DM, Adv. Proc. 10-322IDM (Bankruptcy Court, N.D. Cal. March 11, 2013) 6

Jewel v. Boxer, 156 Cal. App. 3d 171 (1984) 3, 4, 10

Kirsch v. Leventhal, 181 A.D.2d 222 (3d Dep't 1992) 8

Liddle, Robinson & Shoemaker v. Shoemaker, 304 A.D.2d 436 (1st Dep't 2003) 8

Martin v. Camp, 219 N.Y. 170 (1916) 11

Mid-Island Hosp., Inc. v. Empire Blue Cross & Blue Shield (In re Mid-Island Hosp., Inc.), 276 F.3d 123 (2d Cir. 2002) 7

Murov v. Ades, 12 A.D.3d 654 (2d Dep't 2004) 8, 9

Musso v. Ostashko, 468 F.3d 99 (2d Cir. 2006) 6

Santalucia v. Sebright Transp., Inc., 232 F.3d 293 (2d Cir. 2000) .... passim

Shandell v. Katz, 217 A.D.2d 472 (1st Dep't 1995) 8

Shaw v. Manufacturers Hanover Trust Co., 68 N.Y.2d 172 (1986) 11

Sheresky v. Sheresky Aronson Mayefsky & Sloan, 2011 N.Y. Misc. LEXIS 6588 (N.Y. Sup. Ct., N.Y. Co., Sept. 13, 2011) 10, 16

Shiboleth v. Yerushalmi, 58 A.D.3d 407 (1st Dep't 2009) 8

Stem v. Warren, 227 N.Y. 538 (1920) 12

Teichner v. W & J Holsteins, Inc., 64 N.Y.2d 977 (1985) 11

Wieder v. Skala, 80 N.Y.2d 628 (1992) 13

STATUTES AND CODES

Uniform Partnership Act 3, 4

United States Bankruptcy Code, Section 541 6

RULES AND REGULATIONS

New York Rules of Professional Conduct
- Rule 1.5(g) 15
- Rule 1.16(b)(3) 13
- Rule 1.16(e) 14
- Rule 1.16(d) 13
- Rule 5.6 14
- Rule 5.6(a) 14

Partnership Law § 73 8

OTHER AUTHORITIES

Collier on Bankruptcy § 541.07 6

Constitution of the Association of the Bar of the City of New York, art. II 1

INTEREST OF AMICUS CURIAE

The Association of the Bar of the City of New York ("New York City Bar"), founded in 1870, is a voluntary association of lawyers, judges and law students. Today, the New York City Bar has more than 23,000 members. Its purposes include "cultivating the science of jurisprudence, promoting reforms in the law, facilitating and improving the administration of justice, [and] elevating the standard of integrity, honor and courtesy in the legal profession." (Constitution of the Association of the Bar of the City of New York, art. II.) The New York City Bar has 150 committees that focus on different legal practice areas and issues. Through amicus briefs, testimony, reports, statements, and letters drafted by committee members, the New York City Bar comments on questions of law and public policy. This amicus brief was prepared jointly by two committees: the Committee on Bankruptcy and Corporate Reorganization and the Professional Responsibility Committee. It was approved by those committees and by the President of the New York City Bar.

The Committee on Bankruptcy and Corporate Reorganization focuses on issues relevant to corporate and individual bankruptcies and corporate out-of-court restructurings. Committee members include lawyers who specialize in representing debtors and creditors in restructurings involving large companies and lawyers who focus on bankruptcy cases for individuals, as well as bankruptcy

judges and other government representatives, scholars, and financial advisers. Among other functions, the Committee engages on issues relevant to the development of bankruptcy law through judicial decisions and legislation.

The Professional Responsibility Committee examines legal ethics issues and makes recommendations regarding potential changes in the standards that govern the conduct of lawyers in New York. Among other things, the Committee submits amicus briefs, proposes new rules of conduct or amendments of existing rules, proposes legislation or comments on pending legislative proposals, issues white papers to guide practitioners, and sponsors Continuing Legal Education programs on ethics-related topics.[1]

STATEMENT PURSUANT TO FEDERAL RULE OF APPELLATE PROCEDURE 29(C)(5)

This brief was not authored in whole or in part by counsel for any party. No party or party's counsel contributed money that was intended to fund preparing or submitting this brief. No person contributed money that was intended to fund preparing or submitted this brief.

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[1] Certain members of the New York City Bar practice at firms that may have interests in the outcome of this case. None of the members responsible for preparing this brief practice at firms that have interests in the outcome of this or the parallel case involving Coudert Brothers. The judges and other government officials who are members of the two relevant Committees, valued members of the Committees, did not participate in the preparation of this brief. In addition, this brief does not necessarily reflect the individual views of all of the members of the Committee or any institutions with which Committee members are associated.

ARGUMENT

Introduction

This case presents an issue of first impression for an appellate court in New York and raises important public policy concerns that transcend the facts of this particular case. The issue presented is whether the controversial "unfinished business" doctrine should apply to hourly fee matters under New York law. We respectfully submit that it should not. Applying the doctrine to hourly fee matters improperly treats the clients of a dissolving law firm as property, devalues the attorney-client relationship, and subordinates the interests of a law firm's clients to those of its creditors. These results conflict with New York law and public policy, as embodied in judicial decisions and the New York Rules of Professional Conduct.

The unfinished business doctrine as applied to law firms has its genesis in an interlocutory ruling by an intermediate court in California, *Jewel v. Boxer*, 156 Cal. App. 3d 171 (1984). *Jewel* involved a dissolving four-partner firm without a written partnership agreement. Under the Uniform Partnership Act, absent a partnership agreement to the contrary, any withdrawal of a partner is deemed a dissolution. In *Jewel*, the court concluded that the former partners were entitled to an allocation of profits from engagements pending at the time of dissolution in proportion to their interests in the partnership. The court reasoned that under the

Uniform Partnership Act, partners have a fiduciary duty to complete the partnership's unfinished business without additional compensation for doing so.

The *Jewel* court did not address bankruptcy law or creditors' remedies. Over time, however, courts in California and elsewhere have applied the doctrine as a remedy in bankruptcy. In that context, the doctrine benefits the dissolved law firm's creditors to the detriment of the firm's former partners (a surplus distribution being highly unusual) and – most important – to the detriment of the firm's former clients. As a result, the doctrine undermines the attorney-client relationship in violation of basic principles governing client rights and attorney obligations under New York law.[2]

By treating client engagements as "property," the unfinished business doctrine conflicts with the cardinal principle of "client choice" – a client's unilateral right to retain or change lawyers and law firms at any time. Additionally, the doctrine encourages partners in a struggling law firm to "jump ship" before the firm reaches the point of dissolution, potentially hastening the demise of firms that might otherwise survive. As a result, clients of struggling firms are more likely to suffer problematic interruptions in service. The doctrine

[2] The District Court in this case applied New York rather than California law based on a choice-of-law analysis tied to the particular facts presented here. This brief does not address the choice-of-law issue. We focus instead on the broader issues of law and public policy raised by the unfinished business doctrine insofar as it applies under New York law.

also discourages a dissolved firm's partners from diligently pursuing clients' pending matters because any further profits generated by those matters will be expropriated by the dissolved firm's creditors. Similarly, the doctrine discourages other law firms from accepting the dissolved firm's partners and their engagements, thereby further disrupting client services. All of these effects are inconsistent with the fundamental principles of client choice and lawyer mobility established by New York law and public policy.

I. APPLYING THE UNFINISHED BUSINESS DOCTRINE TO HOURLY FEE MATTERS CONFLICTS WITH ESTABLISHED NEW YORK LAW

Appellant (the "Thelen Estate") argues that the unfinished business doctrine already governs contingent fee matters under New York law, and that the doctrine should be extended to hourly fee matters, because there is no relevant difference between the two types of engagements. (Thelen Estate's Br. at 15 *et seq*.) The Thelen Estate's argument misconstrues New York law as recognized, for example, by this Court in *Santalucia v. Sebright Transp*., *Inc*., 232 F.3d 293 (2d Cir. 2000).

The unfinished business doctrine in the context of a law firm bankruptcy rests on the following propositions: (1) partners who leave a law firm at the time it dissolves have a fiduciary duty to complete pending client engagements for the firm's benefit; (2) that duty is enforceable by the firm itself or by its successor, *i.e.*, the bankruptcy estate or trustee (collectively, "the estate"); (3) the right to enforce

that duty constitutes a property right of the estate; and (4) whenever other firms receive fees as a result of taking on a departing partner with pending engagements, those firms receive a conveyance of "property" that belongs to the estate and is subject to being clawed back under fraudulent conveyance or other principles.[3]

Thus, the threshold question confronting this Court is whether the Thelen Estate has a continuing property interest under New York law in Thelen's client engagements following the firm's dissolution. The *Santalucia* decision firmly establishes that it does not.

What constitutes "property" in the bankruptcy context must be analyzed with reference to state law. The Bankruptcy Code does not create property rights; it simply gives effect to those rights insofar as they are recognized by state law.[4] *See, e.g., Musso v. Ostashko*, 468 F.3d 99, 105 (2d Cir. 2006) ("Whether the debtor

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[3] In the parallel case involving the Coudert Brothers bankruptcy Judge McMahon discussed the unfinished business doctrine at length in the course of deciding that it should apply to hourly fee engagements. *See Development Specialists, Inc. v. Akin Gump Strauss Hauer & Feld LLP*, 480 B.R. 145, 160 *et seq.* (S.D.N.Y. 2012) ("*Coudert*"); *see also In re Heller Ehrman LLP*, No. 08-32514DM, Adv. Proc. 10-322IDM (Bankruptcy Court, N.D. Cal. March 11, 2013). Although *Coudert* involves the same issues as those presented here, the New York City Bar was not aware of its status until it was too late to prepare and file a motion for leave to file an amicus brief.

[4] Section 541 of the Bankruptcy Code defines the "estate" as consisting of "all legal or equitable interests of the debtor in property as of the commencement of the case" (subject to certain exceptions). In many cases (including this one), the law firm has shut down and dissolved by the time it enters bankruptcy. In theory, however, any claim owned by the debtor as of the petition date would vest as "property" of the estate. *Collier on Bankruptcy* § 541.07.

has a legal or equitable interest in property such that it becomes 'property of the estate' under [Bankruptcy Code] section 541 is determined by applicable state law."); *Mid-Island Hosp., Inc. v. Empire Blue Cross & Blue Shield (In re Mid-Island Hosp., Inc.)*, 276 F.3d 123, 128 (2d Cir. 2002) (the estate's legal and equitable interests in property are "determined by state law").

As *Santalucia* demonstrates, when a contingent fee matter moves from one firm to another, New York law entitles the second firm to keep whatever it earns for its work on the matter, while the first firm (now dissolved) has a right to whatever it earned for ***its*** work on the matter. There is no presumption that ***all profits*** generated by the engagement go to the first firm. The Thelen Estate's argument is, in effect, that the first firm maintains an enduring ownership interest in work for the client even after the client has chosen to go elsewhere. That result cannot be squared with New York law governing contingent fee matters. It also cannot be squared with New York law and public policy governing the attorney-client relationship, as discussed in Point II below.

Santalucia succinctly sets forth the principles applicable to contingent fee matters in New York: A dissolved firm's property interest in contingent fees received by a subsequent firm is limited to the amount owed by the client for services ***previously rendered*** by the dissolved firm. 232 F.3d at 298. Nothing in *Santalucia* suggests that the first firm has a right to fees for services ***subsequently***

rendered by the second firm. Indeed, *Santalucia* specifically holds that "the dissolved firm is entitled only to the value of the case at the date of dissolution, with interest." 232 F.3d at 298 (citing *Shandell v. Katz*, 217 A.D.2d 472 (1st Dep't 1995), and *Kirsch v. Leventhal*, 181 A.D.2d 222 (3d Dep't 1992)); *see also Shiboleth v. Yerushalmi*, 58 A.D.3d 407, 408 (1st Dep't 2009); *Murov v. Ades*, 12 A.D.3d 654, 655 (2d Dep't 2004) ("That is not to say, however, that the full fees ultimately received as a result of collections on these judgments must be remitted to the dissolved firm") (citing *Santalucia* and *Kirsch*); *Liddle, Robinson & Shoemaker v. Shoemaker*, 304 A.D.2d 436, 441 (1st Dep't 2003) (a withdrawing partner was not entitled to a full partnership share of the contingent fee ultimately received but only "a portion" of the fee, namely, "the value of his interest at the date of dissolution . . . with interest," or alternatively, "in lieu of interest, the profits attributable to the use of his right in the property of the dissolved partnership" pre-dissolution) (quoting Partnership Law § 73).

To properly allocate fees between firms in the context of a contingent fee matter, *Santalucia* requires an evaluation of "the efforts undertaken by the former law firm prior to the dissolution date, or any other relevant evidence to form a conclusion as to the value of these cases to the law firm on the dissolution date." *Santalucia*, 232 F.3d at 298 (citing *Grant v. Heit*, 263 A.D.2d 388 (1st Dep't 1999)); *see also Shiboleth*, 58 A.D.3d at 408. "The lawyer must remit to his

former firm the settlement value, ***less that amount attributable to the lawyer's efforts after the firm's dissolution***." *Santalucia*, 232 F.3d at 298 (emphasis added); *see also Murov*, 12 A.D.3d at 656 (it is proper to "deduct the amounts attributable to the [departing partner]'s post-dissolution efforts, skill, and diligence"). The subsequent firm's entitlement to compensation for "post-dissolution efforts, skill and diligence" ensures the client's ability to retain and compensate successor counsel, unaffected by the prior firm's dissolution. The allocation reflects the principle that no one "owns" the client or the engagement, and that each firm is only entitled to keep what it earns for services actually rendered.

By contrast, the Thelen Estate argues that its property interest extends not merely to fees actually earned by Thelen, but rather to all profits for the entire engagement, irrespective of how much time and effort Thelen invested and how much time and effort the subsequent firm invested -- or, for that matter, how much Thelen has already been paid. To illustrate, assume that a client engaged Thelen to handle a business transaction and paid it $10,000, but Thelen dissolved while the transaction was in its early stages, and the responsible partner moved to law firm Smith & Jones LLP. Assume further that the client, in order to mitigate its damages from Thelen's dissolution, engaged Smith & Jones LLP and paid it $90,000. The Thelen estate would argue that its property includes the entire

$90,000, less only the costs incurred by Smith & Jones LLP -- in other words, ***all*** of the profits the latter firm earned from the engagement. (See Thelen Estate's Br. at 3.) The District Court correctly held that acceptance of the Estate's argument would create a property right not merely in earned fees but in the client engagement itself, a right not recognized by New York law and repugnant to New York public policy.[5]

II. APPLYING THE UNFINISHED BUSINESS DOCTRINE TO HOURLY FEE MATTERS CONFLICTS WITH BASIC PRINCIPLES THAT GOVERN THE ATTORNEY-CLIENT RELATIONSHIP UNDER NEW YORK LAW AND THE RULES OF PROFESSIONAL CONDUCT

As a general matter, a client has the unfettered right to hire and fire counsel at any time. The client's fundamental right to choose counsel is "well rooted" in New York jurisprudence. *Demov, Morris, Levin & Shein v. Glantz*, 53 N.Y.2d 553, 556 (1981). This freedom of choice is essential to maintaining a relationship in which the client places "utmost trust and confidence" in the attorney:

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[5] Some New York cases use the term "unfinished business" in the context of contingent fee matters. *See, e.g., Sheresky v. Sheresky Aronson Mayefsky & Sloan*, 2011 N.Y. Misc. LEXIS 6588, at *13-14 (N.Y. Sup. Ct., N.Y. Co., Sept. 13, 2011). Even under the reasoning of those cases, however, extending the doctrine to hourly fee matters would lead to improper and unfair results: "[T]o the extent that compensation for the case is based solely on the amount of hourly work performed post-dissolution, compensating a former partner out of that fee would reduce the compensation of the attorneys performing the work." *Id.* at *14. Thus, the reasoning in *Sheresky* was narrow, and consistent with *Santalucia* (and inconsistent with *Jewel v. Boxer*).

> The unique relationship between an attorney and client, founded in principle upon the elements of trust and confidence on the part of the client and of undivided loyalty and devotion on the part of the attorney, remains one of the most sensitive and confidential relationships in our society. A relationship built upon a high degree of trust and confidence is obviously more susceptible to destructive forces than are other less sensitive ones. It follows, then, that an attorney cannot represent a client effectively and to the full extent of his or her professional capability unless the client maintains the utmost trust and confidence in the attorney.

Id.

This essential element of the attorney-client relationship cannot be subordinated to creditors' interests, as advocated by the Thelen Estate. Under settled New York law, the attorney-client relationship is terminable at will by the client -- not the lawyer -- at any time, for any reason. A client's right to terminate the relationship is "absolute" and cannot be restricted for the benefit of the attorney or the attorney's law firm. *See, e.g.*, *Campagnola v. Mulholland, Minion & Roe*, 76 N.Y.2d 38, 43 (1990); *Shaw v. Manufacturers Hanover Trust Co*., 68 N.Y.2d 172, 177 (1986); *Teichner v. W & J Holsteins, Inc*., 64 N.Y.2d 977, 979 (1985); *Demov*, 53 N.Y.2d at 556-57; *Crowley v. Wolf*, 281 N.Y. 59, 64-65 (1939); *Martin v. Camp*, 219 N.Y. 170, 176 (1916).

It follows from this principle that law firms cannot claim a continuing right to benefit from client engagements once the client has chosen to move the engagement elsewhere. Client engagements cannot be bartered or sold or assigned to the highest bidder. Reducing client engagements to the status of inventory items

demeans both clients and the legal profession. Treating a client's "unfinished business" as the property of a dissolved firm would undermine the special trust and confidence that clients place in their attorneys and the special duties attorneys owe their clients.[6]

The principle of client choice is so entrenched in New York's jurisprudence that courts routinely reject arrangements that prevent – or even merely inhibit – a lawyer's ability to move from one firm to another. In the leading case of *Cohen v. Lord, Day & Lord*, 75 N.Y.2d 95 (1990), New York's Court of Appeals invalidated the provision in a law firm's partnership agreement that required a departing partner to refrain from competing with the firm as a condition for receiving a withdrawal payment. Although the partner remained free to join another firm, the Court found that the financial burden imposed on his doing so conflicted with the paramount principle of client choice and thus violated public policy. New York law is clear: Even indirect restraints on lawyer mobility harm clients and are therefore prohibited. *Id.* at 98; *see also Denberg v. Parker Chapin Flattau & Klimpl*, 82 N.Y.2d 375, 380-81 (1993) ("restrictions on the practice of

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[6] Given the special trust clients place in attorneys and the unique ethical rules that govern that relationship, partnership cases in the context of non-legal professionals are not relevant to this analysis. Thus, for example, Judge McMahon's reliance in the *Coudert* decision on a New York case addressing architects, *Stem v. Warren,* 227 N.Y. 538 (1920), is misplaced. *Development Specialists*, 480 B.R. at 161-62.

law, which include 'financial disincentives' against competition . . . are objectionable primarily because they interfere with the client's choice of counsel"). The unfinished business doctrine imposes just such restraints.[7]

New York courts routinely limit doctrines of substantive law when they conflict with public policy and with ethical rules that ensure confidence and trust in the legal profession. *See, e.g., Wieder v. Skala*, 80 N.Y.2d 628, 637-38 (1992) (rules of professional conduct superseded ordinary contract rules regarding lawyer's employment by his law firm). The unfinished business doctrine conflicts with New York public policy as embodied in the New York Rules of Professional Conduct in at least three ways.

First, as discussed above, the doctrine contravenes the long-established public policy favoring a client's right to discharge an attorney and the attorney's obligation to abide by the client's decision. Rule 1.16(b)(3) imposes on a lawyer an absolute obligation to withdraw from the attorney-client relationship whenever

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[7] In the *Coudert* case, Judge McMahon concluded that *Cohen* and *Denberg* are distinguishable because they did not address the unfinished business doctrine, "are not dissolution cases," and involved ongoing competition between two active firms. *Denberg* was also distinguished on the ground that it involved a fee sharing provision with respect to new business as well as old, "in effect treating the *client*, not the *matter*, as the firm's property." *Development Specialists*, 480 B.R. at 170-71 (emphasis in original). As shown in this brief, however, the unfinished business doctrine improperly treats clients as property and impairs client interests even with respect to "old" matters that are transferred from a dissolved firm. Thus, the principles of client choice enunciated in *Cohen* and *Denberg* remain relevant in this context.

"the lawyer is discharged."[8] Even if the client discharges the attorney "unfairly," the attorney must withdraw and "must take all reasonable steps to mitigate the consequences to the client" of the withdrawal. Rule 1.16, Comment 9 (citing Rule 1.16(e)).[9] The Rule thus preserves the client's fundamental right to choose counsel unilaterally and without restraint, even at the expense of a law firm's profits. As applied to hourly fee engagements, the unfinished business doctrine conflicts with this essential public policy.

Second, the doctrine conflicts with the public policy embodied in Rule 5.6(a), which prohibits restraints on lawyer mobility in the interest of protecting client choice. The Rule bars lawyers from participating in "[any] type of agreement that restricts the right of a lawyer to practice after termination of the relationship." Such restrictions are improper because they limit "the freedom of clients to choose a lawyer," as well as a lawyer's "professional autonomy." Rule

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[8] The only stated exception involves situations where withdrawal requires permission of a tribunal, in which case the attorney may only withdraw if and when such permission is granted. Rule 1.16(d).

[9] Rule 1.16(e) provides:

> Even when withdrawal is otherwise permitted or required, upon termination of representation, a lawyer shall take steps, to the extent reasonably practicable, to avoid foreseeable prejudice to the rights of the client, including giving reasonable notice to the client, allowing time for employment of other counsel, delivering to the client all papers and property to which the client is entitled, promptly refunding any part of a fee paid in advance that has not been earned and complying with applicable laws and rules.

5.6, Comment 1. A lawyer's freedom to move from one firm to another safeguards clients' ability to retain counsel of their choice and the lawyer's ability to continue zealous representation of those clients. The unfinished business doctrine creates perverse incentives that undermine these objectives by limiting client choice and disrupting client services.

In particular, the doctrine would encourage partners to abandon a struggling but not-yet-insolvent law firm as they attempt to beat the start of any dissolution or insolvency clock. The doctrine would also discourage lawyers in a dissolving firm from acting diligently to serve clients whose matters may be subject to unfinished business claims. Similarly, the doctrine would discourage other law firms from accepting lawyers and client engagements from a dissolved firm because the resulting profits will be subject to expropriation by the dissolved firm and its creditors. All of these effects would be detrimental to clients and the profession as a whole. When lawyers must confront the Scylla of abandoning their clients or the Charybdis of losing future compensation on hourly fee matters, both clients and lawyers suffer. New York law and public policy seek to avoid such results.

Third, application of the unfinished business doctrine to hourly fee matters would conflict with a lawyer's obligations under Rule 1.5(g). In relevant part, the Rule prohibits fee splitting without client consent unless "the division is in proportion to the services performed by each lawyer," or unless "each lawyer

assumes joint responsibility for the representation" in a writing given to the client. The Thelen Estate's claim for profits on all unfinished business violates these provisions. The Estate is not seeking an allocation of fees "in proportion to the services" that Thelen provided – indeed, as shown above, it seeks a grossly disproportionate allocation of fees. Moreover, the Estate is obviously not planning to assume "joint responsibility" for any future representation. As the *Sheresky* court noted, Rule 1.5(g) precludes an unfinished business claim by a partner in a dissolved law firm against his fellow partners. For that reason and others, the *Sheresky* court specifically declined "to recognize a cause of action for unfinished business for hourly fee cases which has, hitherto, not been recognized by New York courts." *Sheresky*, 2011 N.Y. Misc. LEXIS 6588, at *15. The same conclusion should prevail here.

CONCLUSION

The unfinished business doctrine would have unacceptable consequences when applied to law firms' hourly fee engagements. In the bankruptcy context, the doctrine would elevate creditor interests over client interests. The doctrine's perverse consequences would turn the attorney-client relationship on its head. This Court should hold that application of the unfinished business doctrine to hourly fee engagements is improper under New York law and public policy.

Dated: New York, New York
June 12, 2013

Respectfully submitted,

/s/ Damian Schaible
DAMIAN SCHAIBLE
Chair, Committee on Bankruptcy and
Corporate Reorganization

DAVID A. LEWIS
Chair, Committee on Professional Responsibility

THE ASSOCIATION OF THE BAR OF
THE CITY OF NEW YORK
42 West 44th Street
New York, NY 10036
(212) 382-6600

Attorneys for Amicus Curiae The Association of the Bar of the City of New York

Certificate of Compliance

This brief complies with Fed. R. App. P. 32(a)(7)(B) because it contains 3,911 words, exclusive of the parts exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

This brief complies with Fed. R. App. P. 32(a)(5) because it is in a proportionally spaced 14 point typeface.

/s/ Damian Schaible
Damian Schaible