Case No. S236208

IN THE SUPREME COURT OF CALIFORNIA

HELLER EHRMAN LLP,

Plaintiff and Petitioner,

v.

JONES DAY,

Defendant and Respondent.

SUPREME COURT
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Deputy

AND RELATED CASES

AFTER A DECISION BY THE U.S. COURT OF APPEALS FOR THE NINTH CIRCUIT, CASE NOS. 14-14314, 14-16315, 14-16317, 14-16318

APPEAL FROM THE U.S. DISTRICT COURT FOR THE NORTHERN DISTRICT OF CALIFORNIA, SAN FRANCISCO DIVISION
CASE NOS. 14-01236, 14-01237, 14-01238, 14-01239

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QUESTION PRESENTED

Under California law, what interest, if any, does a dissolved law firm have in legal matters that are in progress but not completed at the time the law firm is dissolved, when the dissolved law firm has been retained to handle the matters on an hourly basis?

INTRODUCTION

Heller's clients faced a crisis. The law firm that represented them was collapsing and told them that it could no longer provide legal services. Their relationship with Heller was over, but these clients' legal matters would go on. The clients had no choice but to retain other law firms to handle their matters.

Like any discharged firm, Heller has no right to hourly fees earned by other firms for work that clients chose those firms to handle. Indeed, clients may replace one firm with another for many reasons: The client may be dissatisfied with its current counsel; the law firm may no longer be able to handle the work; or a lawyer working on a matter may move to a different firm. Regardless of the reason, each firm is entitled to be paid for the work it actually performed—no more, no less. Any other rule is incompatible with core principles governing the attorney-client relationship.

Heller attempts to answer the certified question without regard to any of this. But this Court cannot decide the scope of a dissolved firm's

interest—if any—without considering the circumstances of the dissolution and the choices that clients made about who would represent them from that point forward.

Two considerations are critical here. *First*, unlike in cases that Heller cites, the post-dissolution work here was not performed by Heller or on its behalf; clients fired Heller and chose different, pre-existing firms like Jones Day to handle their matters instead. Heller's partnership business was wound up at that point. Heller was fully compensated for all the work that it did, and no case gives it a right to profits for work done subsequently by a third-party firm.

Second, the governing law here is the Revised Uniform Partnership Act (RUPA), not the Uniform Partnership Act (UPA). RUPA eliminates the underpinnings of the cases on which Heller relies, all of which were decided under UPA. Those cases gave the dissolved partnership a share of post-dissolution profits. An essential reason for their holding was that UPA prohibited partners from receiving extra compensation for winding up a dissolved firm's business. RUPA eliminated UPA's no-compensation rule, and granted partners reasonable compensation for any post-dissolution work that they do. That means that, regardless of whether post-dissolution work is considered winding up the old firm's business or not, the partners who actually perform the work are entitled to keep the profits from their skill and labor.

Common sense, precedent, statutory language, and equity all point to the same conclusion: Heller has no right to confiscate Jones Day's profits. When Heller dissolved, it had an interest in being paid for work it actually performed on hourly-rate matters. But it has no right to be paid for work that clients chose other firms to handle going forward.

STATEMENT OF THE CASE

A. Heller Declares Bankruptcy And Formally Abandons Its Clients

Heller failed to satisfy its fundamental obligation to manage itself so it could effectively represent its clients. As Heller's plan administrator explained, "[a] major portion of [Heller's demise] was management, or the lack thereof." SER 37 (Burkart Dep.).[1] According to the plan administrator, Heller's mismanagement created unsustainable debt and should have raised "red flags" for shareholders and creditors alike as early as 2006. SER 39 (*id.*).

In September 2008, Heller defaulted on its multimillion-dollar loan obligations to banks. The banks seized control of Heller's accounts, making it virtually impossible for Heller to represent clients. ER 6, 9 (Dist. Ct. Order ("*Heller V*")).

[1] "SER" refers to Appellee's Supplemental Excerpts of Record filed in the U.S. Court of Appeals for the Ninth Circuit in *Heller Ehrman LLP v. Jones Day*, No. 14-16315. "ER" refers to Appellant's Excerpts of Record filed in the same case. "OB" refers to Heller's opening brief filed in this Court.

Faced with its impending dissolution, Heller was ethically obligated to advise clients to retain new counsel. For that reason, Heller announced that it would "cease providing legal services to all clients." SER 75 (Mem. re. Wind-Down Efforts). Heller's former clients had to find new firms to handle their matters, and some of those clients chose Jones Day. *See infra* 6-7.

B. To Help Ensure An Orderly Dissolution, Heller Includes A *Jewel* Waiver In Its Dissolution Plan

In the midst of Heller's financial collapse, its shareholders began looking to join other law firms. Some of those firms expressed concern about potential liability under *Jewel v. Boxer*, 156 Cal. App. 3d 171 (1984), a case that required former partners to account to a dissolved firm for profits that they earned in "winding up" their former firm's so-called "unfinished business."

At the time of Heller's collapse, no court had extended *Jewel* to impose liability on a third-party firm that had no fiduciary duties to the dissolved firm. Only one major law firm bankruptcy, that of Brobeck, Phleger & Harrison LLP, had involved *Jewel* claims. *See* SER 21-22 (Triantis Rpt.). Many firms, including Jones Day, never considered the prospect of *Jewel* liability for taking on former Heller shareholders. *See* ER 81-83 (Bankr. Ct. Dec. Liability ("*Heller III*")); SER 21-26 (Triantis Rpt.). Other firms, however, were "acutely aware of the Jewel v Boxer

problem" because of Brobeck's then-pending claims, and—even though no court had extended *Jewel* to impose liability on third-party firms—they "want[ed] some assurance that they won't get trapped in that net." SER 73 (9/21/08 email)); *see, e.g.*, SER 66-72 (Baker & McKenzie Proposal); SER 29 (Corwin Decl.).

Shareholders expressed the concerns of their potential new firms to Heller's management. SER 73 (9/21/08 email); SER 77-78 (Levin Dep.). In response, Heller's dissolution plan included a provision waiving "any rights and claims under the doctrine of *Jewel v. Boxer*, 156 Cal. App. 3d 171 (1984) to seek payment of legal fees generated after the departure date of any lawyer or group of lawyers" (subject to an exception, not applicable here, for contingency-fee matters). ER 157 (Dissolution Plan).

Heller—and, ultimately, its creditors—benefitted from the *Jewel* provision. By encouraging shareholders to vote for a prompt dissolution with minimal disruption to clients, the *Jewel* provision reduced Heller's overhead, increased its collection of accounts receivable, and decreased malpractice and other claims against Heller. SER 2-4 (Benvenutti Depo.). Unrebutted expert analysis conservatively estimated that these benefits exceeded $57 million. *See* Mosier Expert Report *Heller Ehrman v. Jones Day*, Adv. P. No. 10-03221 (Bankr. N.D. Cal.), ECF 129-4, at 7.

C. Some Former Heller Clients Choose Jones Day To Handle Matters That Heller Abandoned

Forced to find new law firms to handle their legal matters, some of Heller's former clients chose Jones Day to represent them. Jones Day had previously represented many of these clients on other matters. SER 64-65 (Sims Decl.). Clients attested that they "retained Jones Day, not any particular lawyer, and [they] did so because [they] believed that Jones Day had the resources and expertise to represent [them] and [their] best interests." SER 50 (Goldfischer Decl.); SER 47 (Leibowitz Decl.).

Some former Heller shareholders also joined Jones Day. But those shareholders did not "control" any client's decision to retain Jones Day; rather, clients made that "independent decision." *See, e.g.*, SER 51 (Goldfischer Decl.); SER 48 (Leibowitz Decl.). While an individual lawyer's move to Jones Day "was certainly a factor in [their] decision to retain Jones Day," clients emphasized that "it was not the only factor." SER 47 (Leibowitz Decl.); *see* SER 50 (Goldfischer Decl.). Clients would not have retained a new firm joined by a Heller shareholder if that firm lacked "the capacity to handle [their] work." SER 47 (Leibowitz Decl.); *see* SER 50 (Goldfischer Decl.). Nor would they have hired an individual Heller shareholder who "opened his own office as a solo practitioner" and lacked the "capability of handling [their] legal needs." SER 47 (Leibowitz Decl.); SER 50 (Goldfischer Decl.).

Jones Day's retainer agreements provided that clients would be represented by Jones Day, not by any individual partner. SER 62 (Sims Decl.). Indeed, "Jones Day clients are regularly served by cross-office and cross-practice teams." SER 62-63 (*id.*). Clients with complex matters spanning different practice areas benefit from the expertise of more than 2,400 Jones Day lawyers in 44 locations around the world, as well as from Jones Day's established reputation in the legal profession. *See id.* In short, by hiring Jones Day, clients obtained "significant resources, personnel, capital, and services well beyond the capacity of either Heller or its individual Shareholders." ER 9 (*Heller V*); *see* SER 63 (Sims Decl.).

When clients retained Jones Day, neither clients nor Jones Day knew about the *Jewel* provision. ER 83 (*Heller III*); SER 51 (Goldfischer Decl.). Had clients known about potential *Jewel* liability for the new firms that they retained, they "would [have] be[en] concerned" about being represented by a firm "that would have to perform work for [them] without any expectation of making a profit on that work." SER 51 (Goldfischer Decl.); SER 48 (Leibowitz Decl.). In compensating Jones Day, clients intended to "provide incentives for the firm to handle [their] matters in a first rate manner and use the best team at the firm to work on the matters." SER 54 (Garten Decl.). They also attested that "[f]orcing [a] law firm to disgorge whatever portion of [the] compensation [that] may be considered 'profits' would change the incentives and economics facing the law firm,"

making it more difficult for former shareholders to join new partnerships, and for clients to find new firms to handle their matters. *Id.*

D. Heller Sues Jones Day In The Bankruptcy Court

On December 1, 2010, the plan administrator for Heller's bankrupt estate ("Heller") brought this adversary proceeding, seeking profits that Jones Day earned on matters that Heller's former clients entrusted to Jones Day. ER 225 (Bankr. Ct. Dkt.). Heller alleged that the *Jewel* provision fraudulently transferred its purported interest in such profits to Heller shareholders, who, in turn, transferred that interest to Jones Day. ER 164-65, 179, 184 (1st Am. Compl.).

The Bankruptcy Court adopted Heller's theory, relying on its own earlier decision in the Brobeck bankruptcy proceedings. ER 106 (Mem. Dec. MTD ("*Heller I*")); ER 46 (*Heller III*); *see In re Brobeck, Phleger & Harrison LLP*, 408 B.R. 318 (Bankr. N.D. Cal. 2009) (Montali, J.). In *Brobeck*, the Bankruptcy Court held that law firms have a property interest in hourly-rate client matters pending at the time of dissolution, and that partners must account to the dissolved firm for profits that they earn on those matters. 408 B.R. at 337-38. The Court further concluded that Brobeck fraudulently transferred the right to those profits to its partners, and that the profits earned by the pre-existing, third-party firms that those partners joined belonged to the Brobeck estate. *Id.* at 338-48. The parties subsequently settled, and *Brobeck* was never subject to appellate review.

Brobeck was the first decision of its kind: Before *Brobeck*, no court had extended the *Jewel* doctrine to impose liability on third-party law firms. Indeed, the Bankruptcy Court acknowledged the novelty of the issue. *Id.*; ER 52 (*Heller III*). Applying *Brobeck* here, the Bankruptcy Court concluded that "matters in progress but not completed when the firm ... dissolved, regardless of whether the firm was retained to handle the matter on an hourly or contingency basis .... [were] property of Heller." ER 55-56 (*Heller III*). It further concluded that the *Jewel* provision was a fraudulent transfer, and that Jones Day was a subsequent transferee of Heller's property. ER 57-84 (*id.*). For those reasons, the Bankruptcy Court recommended granting partial summary judgment on liability to Heller. ER 46-47 (*id.*).

For the next year, the Bankruptcy Court oversaw extensive discovery regarding damages. The Bankruptcy Court concluded that, while Jones Day is not entitled to keep any profit from the matters at issue, it is entitled to "reasonable compensation" for its work, and to credit for overhead expenses directly attributable to that work. ER 26 (Mem. Dec. Damages ("*Heller IV*")). But the Bankruptcy Court further concluded that (1) "reasonable compensation" is less than market billing rates, and (2) deductible overhead expenses are less than those reflected in a firm's profit margin. ER 30-33 (*id.*). Finding disputed factual issues about damages, it

recommended withdrawal of the reference for trial before an Article III court. ER 283 (Bankr. Ct. Dkt.).

E. The District Court Enters Judgment In Favor Of Jones Day

The District Court withdrew the bankruptcy reference on April 4, 2014. *See* ER 221 (Dist. Ct. Dkt.). It reviewed de novo the Bankruptcy Court's decisions on liability. *See* 28 U.S.C. § 157(c); *Stern v. Marshall*, 564 U.S. 462 (2011); *In re Bellingham Ins. Agency, Inc.*, 702 F.3d 553, 565 (9th Cir. 2012).

The District Court entered judgment in favor of Jones Day. ER 3 (*Heller V*). Because Heller's fraudulent-transfer claims require it to identify a specific state-law property interest, the court began and ended its inquiry with the question whether Heller has "a property interest in hourly fee matters pending at the time of its dissolution." ER 4 (*id.*). Heller has no such interest, the court explained, because "[a] law firm never owns its client matters." ER 11 (*id.*). Clients have the "absolute" power to discharge an attorney at any time, and "the most [a] law firm can be said to have is" a right to be paid for services that it actually performs. ER 11-12 (*id.*) (internal quotation marks omitted). To the extent that firms have "an *expectation* of future business," that *expectation* "disappear[s] as soon as either (1) the client removes the business, which it can do at will, or (2) the law firm ceases to be able to perform the work [necessary] to generate [any] expected future profits." *Id.*

The District Court rejected Heller's reliance on California partnership law and cases applying the so-called unfinished business doctrine, which do not create new property interests. ER 9-10 (*id.*). The court further concluded that *Jewel*—which predated RUPA and did not involve claims against third-party firms—was legally and factually inapposite. *Id.* Finally, the District Court observed that it would be inequitable and would contravene public policy to force third-party firms to turn over their profits to a defunct firm that contributed nothing to performing the work. ER 11-15 (*id.*).

Heller appealed. ER 127.

F. The Ninth Circuit Asks This Court To Consider Whether Heller Has Any Interest Under California Law In Profits Earned By Jones Day On Matters Heller Abandoned

The U.S. Court of Appeals for the Ninth Circuit asked this Court for "guidance [as to] whether Heller has a property interest in its unfinished hourly fee matters upon dissolution." *In Matter of Heller Ehrman LLP*, 830 F.3d 964, 973 (9th Cir. 2016). The answer to this question is critical because, without such a property interest, Heller's fraudulent-transfer claims fail as a matter of law. *See id.* at 966, 973.

No California court, the Ninth Circuit explained, has considered whether a dissolving firm has a right under RUPA to future fees on hourly-rate matters. The Ninth Circuit noted that California courts have interpreted RUPA's predecessor, UPA to require former partners to account

for profits they earned on contingency-fee matters previously handled by their dissolved firm. *See id.* at 967-68. Those decisions rested on a provision in UPA precluding partners from receiving "extra compensation for services rendered in completing unfinished business." *Id.* at 967. But the California legislature amended that provision when it enacted RUPA, which allows all partners "'reasonable compensation for services rendered in winding up the business of the partnership.'" *Id.* at 968 (quoting Cal. Corp. Code § 16401(h)). Because this Court had previously held that "'reasonable compensation' means fees 'attributable to the services and skill' of the partner performing the work," RUPA's language "suggests that former partners now have a claim to some or all of their hourly rate for working on unfinished business." *Id.* at 969 (quoting *Jacobson v. Wilkholm*, 29 Cal. 2d 24, 30 (1946)). "Despite the significance of this legislative change, no California court has considered ... whether there remains a basis for holding that a partnership has a property interest in legal matters pending at the time the firm is dissolved." *Id.*; *see id.* at 973.

The Ninth Circuit accordingly asked this Court to decide the certified question. *See id.* at 973.

SUMMARY OF ARGUMENT

Heller's fraudulent-transfer claims are premised on the notion that Heller has a state-law right to be paid for work that clients chose Jones Day to handle after Heller abandoned them. Settled California law and policy

repudiate that notion. A dissolved law firm has no right to hourly fees for work that another firm performed, and to which the dissolved firm contributed nothing.

I. The only property interest a law firm has with respect to hourly-rate matters is to be paid for work that clients allow it to perform. When a client exercises its absolute right to fire one firm and hire another, the discharged firm has no claim—against the client or the firm that replaces it—for the fees earned by the replacement firm.

As the District Court explained, a contrary "rule that prevents third-party firms from earning a profit off of labor and capital investment they make in a matter previously handled by a dissolved firm" would "make it more difficult for partners leaving a struggling firm to find new employment" and would "limit the representation choices a client has available." ER 14-15. It would also unfairly give dissolving firms a risk-free annuity by granting them a right to all future profits on matters they once handled—even if they are no longer capable of doing the work, the client has discharged them, and a different firm does the work. Finally, as Heller concedes, a partner departing outside the dissolution context has no duty to account to his former firm for any profits from matters that clients bring to the new firm; Heller's approach would therefore destabilize firms by encouraging partners "to jump ship at the first sign of trouble." ER 14.

II. Heller relies on the fiduciary duty among partners of a dissolving firm to "wind[] up" the "partnership business" and then "account" to one another for profits that they earn. Cal. Corp. Code § 16404(b)(1). But Heller's partnership business was wound up when it abandoned its clients, forcing them to retain new counsel. From that point, any profits generated by Jones Day's work on matters previously handled by Heller came from Jones Day's partnership business, not Heller's. Moreover, the fiduciary duties to wind up business and then account for profits apply only to former partners. They do not impose any obligations on a third party like Jones Day, which had no duty to complete Heller's partnership business in the first place, and therefore cannot be called to account for profits it earned.

A. Cases imposing a duty to account on former partners for profits that they earned themselves while winding up the business of the dissolving firm are inapposite. In each case, the court found a breach of fiduciary duty under UPA where the same attorneys continued to perform the same work, sometimes under the original fee agreement, and a single partner (or group of partners) attempted to appropriate profits and cut off the rights of the former firm.

By contrast, Heller's implosion forced clients to take their work elsewhere. Heller's partnership business was wound up at that point. Moreover, clients did not retain former Heller shareholders (or a subset of

Heller shareholders) who diverted profits away from Heller for their own personal gain; clients retained different third-party firms, which had their own resources and new attorneys to handle the matters. The cases that Heller cites do not extend *Jewel* liability to a third-party firm under these circumstances.

B. The cases on which Heller relies have also been superseded by California's adoption of RUPA. When requiring former partners to account for post-dissolution profits, *Jewel* and its progeny relied on two aspects of UPA. *First*, *Jewel* held that a partner could not be compensated on a quantum meruit basis for post-dissolution work because UPA barred partners from receiving any compensation for winding up their dissolved firm's business. *Second*, *Jewel* and other cases found the former partners' conduct particularly egregious because they had violated their fiduciary duty under UPA not to take action with respect to unfinished business for their personal gain.

RUPA eliminated both aspects of UPA. RUPA grants all partners "reasonable compensation" for their post-dissolution efforts, meaning that the partner who performed the work is now entitled to profits attributable to his skill and services. Here, *all* of the profits are attributable to Jones Day's skill and services; Heller contributed nothing. RUPA also allows former partners to compete with the partnership, without limitation, immediately upon dissolution. Thus, even if a former Heller shareholder had solicited a

former Heller client for a matter that Heller had been handling, that would not have violated any fiduciary duties under RUPA. It goes without saying that RUPA imposes no restrictions on the ability of a third party like Jones Day to represent Heller's former clients.

III. Finally, Heller cannot brush aside the policy problems that its proposed rule would cause. Heller claims that *Jewel* and other California cases have rejected concerns about client choice and equity. That is wrong: No California case has considered the ramifications of imposing a 100% tax on profits earned by third parties on matters previously handled by a defunct firm. Such a rule would have made it more difficult for the clients that Heller left in a lurch to find new representation. And while Heller insists that the new firm handling a matter is entitled to reasonable compensation, Heller's understanding of reasonable compensation would require complex litigation and often leave the new firm empty-handed. None of Heller's remaining policy arguments justifies imposing a rule that would so severely harm clients and lawyers alike.

ARGUMENT

I. HELLER HAS NO RIGHT TO PROFITS EARNED BY THIRD-PARTY FIRMS FOR WORK THAT HELLER DID NOT PERFORM

Heller's federal and state fraudulent-transfer claims require it to identify a specific state-law property interest that was allegedly transferred to Jones Day. *See Barnhill v. Johnson*, 503 U.S. 393, 398 (1992). The

Ninth Circuit asked this Court to determine whether any such property interest exists here. It does not. Under California law, a law firm has a right to be paid only for the work that clients entrust to it and that it performs. When a client exercises its unfettered right to terminate one firm and retain another, the discharged firm has no claim—against either the client or the firm that replaces it—for the resulting loss.

A. Client Matters Belong To Clients, Not Law Firms

A law firm has a right to be paid only for work its client has allowed it to perform. It does not have a property interest in client matters themselves. A law firm accordingly has no right to future profits, much less the right to future profits derived from work performed by another firm.

This Court has long recognized that "[t]he relation of attorney and client is one of special confidence and trust," and "'the client is justified in seeking to dissolve that relation whenever he ceases to have absolute confidence in ... the capacity of the attorney.'" *Fracasse v. Brent*, 6 Cal. 3d 784, 789-90 (1972) (quoting *Gage v. Atwater*, 136 Cal. 170, 172 (1902)). Clients therefore have "absolute" "power to discharge an attorney, with or without cause." *Id.* at 790; *see also* Cal. Standing Comm. on Prof'l Resp., Formal Op. 1994-135 ("[L]awyers serve at the pleasure of their clients; a client always maintains the right to terminate the services of a lawyer at any time.").

To safeguard this absolute right, California law provides that a client's choice to discharge an attorney cannot constitute a breach of contract, and a discharged attorney is not entitled to any lost profits resulting from his discharge. *Fracasse*, 6 Cal. 3d at 790-91; *see also Kallen v. Delug*, 157 Cal. App. 3d 940, 950 (1984). Rather, the attorney "only has a right to quantum meruit recovery" representing the value of past work. *Jalali v. Root*, 109 Cal. App. 4th 1768, 1777 (2003); *see Fracasse*, 6 Cal. 3d at 791; *Oliver v. Campbell*, 43 Cal. 2d 298, 304 (1954); *Cazares v. Saenz*, 208 Cal. App. 3d 279, 285 (1989). Otherwise, as this Court has recognized, "[t]he right to discharge is of little value if the client must risk paying the full contract price for services not rendered upon a determination by a court that the discharge was without legal cause." *Fracasse*, 6 Cal. 3d at 790; *see Federal Sav. & Loan Ins. Corp. v. Angell, Holmes & Lea*, 838 F.2d 395, 397 (9th Cir. 1988) (applying California law).

This same principle is reflected in the rule that a law firm has no right to fees for work it does not perform. *See* Cal. R. Prof. Conduct 3-700(D)(2) (providing that an attorney violates ethical rules by refusing to "[p]romptly refund any part of a fee paid in advance that has not been earned"); *see also* Cal. Standing Comm. on Prof'l Resp., Formal Op. 1996-147 ("[A]n attorney may charge a client only for that work the attorney actually does for the client."). Indeed, it is unconscionable to allow "fees [that] have no relationship whatsoever to the amount of service provided or

to be provided by the partnership to the client." *Champion v. Superior Court*, 201 Cal. App. 3d 777, 783 (1988); *see* Cal. R. Prof. Conduct 4-200(B)(1) (unconscionability of fee depends on, among other things, whether "[t]he amount of the fee [is] in proportion to the value of the services performed"). "The division of fees without regard to services actually rendered is [therefore] contrary to [California] public policy," and agreements that attempt to circumvent these principles are unenforceable. *Fraser v. Bogucki*, 203 Cal. App. 3d 604, 610 (1988) (superseded by statute on other grounds); *see also, e.g., Champion*, 201 Cal. App. 3d at 783 (invalidating agreement giving firm interest in future fees earned by withdrawing partner); *Kallen*, 157 Cal. App. 3d at 951 (refusing to enforce fee-sharing agreement giving discharged attorney interest in potential recovery that exceeded value of work he had performed). For these reasons, a discharged firm has no claim against another firm that a client chooses to replace it. *See Kallen*, 157 Cal. App. 3d at 951.

B. The Only State High Court To Consider Heller's Theory Rejected It Based On Universally Applicable Principles

Based on the same principles discussed above, the New York Court of Appeals held that a defunct law firm has no interest in profits earned by third-party firms on hourly-fee matters. *See In re Thelen LLP*, 24 N.Y.3d

16, 22, 28-29, 33 (2014).[2] *Thelen* is the only decision from a state's highest court addressing claims involving Heller's theory, and the reasons it gave for rejecting those claims apply equally under California law.

Thelen explained that, as a matter of law, "a client's legal matter belongs to the client, not the lawyer." *Id.* at 29. Because clients have the "unqualified right to terminate the attorney-client relationship at any time without any obligation other than to compensate the attorney for the fair and reasonable value of the *completed services*," the court held that "no law firm has a property interest in future hourly legal fees." *Id.* at 28 (internal quotation marks omitted). Rather, the law firm's only interest is in "yet-unpaid compensation for legal services already provided." *Id.* at 29.

The court further held that any other rule "would have numerous perverse effects" and "would cause clients, lawyers, and law firms to suffer." *Id.* at 31-32. A rule granting the first firm to work on a matter a right to all future profits would create "a major inconvenience for ... clients and a practical restriction on a client's right to choose counsel." *Id.* at 32. Unless the second firm to handle a matter were willing to disgorge its profits to the first firm (which few if any firms would be willing to do), a client would not be able to retain a new firm joined by its lawyer of choice. *See id.*

[2] The New York Court of Appeals issued a single opinion addressing the identical certified questions arising from the Thelen and Coudert Brothers bankruptcy proceedings.

The court explained that these consequences would be particularly severe when the original firm has collapsed in bankruptcy, forcing both its clients and its partners to find new firms. In those instances, the departing attorneys would "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." *Id.* And "[t]he notion that law firms will [take on] departing partners or accept client engagements without the promise of compensation ignores common sense and marketplace imperatives." *Id.* *Thelen* accordingly refused to endorse a rule that would unfairly grant a firm that clients fired a right to "windfall" profits "from work [it] d[id] not perform" while simultaneously penalizing the third-party firms that assisted clients in need. *Id.* at 31-32.

Finally, *Thelen* observed that any other approach would destabilize law firms. The trustees in *Thelen* conceded (as Heller does here, *see* ER 53-55 (*Heller III*)) that a partner who leaves a law firm before dissolution has no duty to account for profits earned after his departure. *Thelen*, 24 N.Y.3d at 32. Indeed, a contrary rule would severely impede the ability of lawyers to make lateral moves (including between financially stable firms) that are common in the legal profession. Thus, a partner who departs a firm before dissolution would have no duty to account, but a partner who stays until dissolution would have this burden. *Thelen* concluded that the

instability created by this perverse result would disserve law firms, individual attorneys, and clients alike. *See id.*

All of these principles apply universally across jurisdictions, including California. *See supra* 17-19. This Court should not depart from them here. Like the New York Court of Appeals, this Court should reaffirm that a defunct law firm has no property interest in hourly fees earned by third-party firms on matters that the defunct firm abandoned.

* * *

In sum, "given the client's unfettered right to hire and fire counsel," "no law firm has a property interest in future hourly legal fees." *Thelen*, 24 N.Y.3d at 28. That rule applies regardless of whether the discharged firm is capable of continuing to perform the work. *See Cazares*, 208 Cal. App. 3d at 285. But it has particular force when, as here, the discharged firm's financial collapse prevents it from representing clients and leaves them "no choice but to seek new counsel." ER 9. Heller has no right to confiscate the profits that Jones Day earned for work that clients chose Jones Day to perform after Heller abandoned those clients.

II. HELLER'S CONTRARY ARGUMENTS ARE UNAVAILING

Heller nevertheless insists that it can reach out from the grave to seize Jones Day's profits. It relies on the state-law fiduciary duty among former partners to "wind up" the "partnership business" and then to "account" to one another for profits they earn. But Heller's "partnership

business" was terminated and wound up when it announced that it could no longer represent its clients and the clients hired new firms. Moreover, even if there were (and there is not) a duty in these circumstances to complete a dissolved firm's business and then account for profits, it would be personal to former partners; a third party like Jones Day, with no fiduciary relationship to Heller, has no duty to "wind up" Heller's work and thus has no profits for which to account. For these reasons, Heller's reliance on cases applying the so-called unfinished business doctrine—all of which imposed a duty under UPA on former partners to "wind up" the business of the dissolved partnership and account for profits that they earned—is likewise unavailing.

A. Partnership Law Does Not Give Heller Any Right To Jones Day's Profits

Heller argues that partnership law gives it a perennial property right to the matters at issue and to Jones Day's profits from those matters. Heller relies on the fiduciary duty among partners of a dissolving firm to "wind[] up" the "partnership business" and then "account" to one another for profits. Cal. Corp. Code § 16404(b)(1). But these duties do not give Heller any property interest in Jones Day's profits. *First*, Heller's theory assumes that client matters are the "partnership business" of a discharged law firm. That is wrong: Heller's partnership business was completed when it fired its clients. *Second*, RUPA imposes fiduciary duties only on former

partners, not on third parties like Jones Day. Because Jones Day never had any obligation to wind up Heller's partnership business, it cannot be called to account for profits it earned working on matters that Heller previously handled.

1. RUPA imposes a duty to account only for profits derived from the conduct of "partnership business." RUPA § 404(b)(1). When a client fires one firm and hires another, the work on the matter is no longer the discharged firm's "partnership business": From that point on, there is no more work for the discharged partnership to do. *See supra* 17-19. And there is no duty to account to the discharged firm for the new firm's profits.

To illustrate this point, imagine that Heller's former clients replaced it with a firm, "Smith & Smith," that never took on any former Heller shareholders. Heller concedes that such a firm "would have no exposure" under its theory. ER 55 (*Heller III*). Heller would have no claim to profits earned by Smith & Smith on matters that clients no longer wanted Heller to handle.

Indeed, as soon as clients discharged Heller and retained Smith & Smith, the work on the matters would have ceased to be Heller's partnership business and become Smith & Smith's partnership business. Even if a Heller shareholder were to join Smith & Smith *after* clients retained Smith & Smith, that shareholder would not have a duty, upon arriving at Smith & Smith, to account for his new firm's profits. Those

profits would simply not be a result of "services performed for the [Heller] partnership." Cal. Corp. Code § 16401(h). By the same token, if a Heller shareholder joined Smith & Smith before a former Heller client retained Smith & Smith, that fact would not convert Smith & Smith's profits into profits from Heller's partnership business.

This is particularly true where the dissolving firm expressly fires its clients. *See* SER 75 (Mem. re. Wind-Down Efforts) (Heller announced that it would "cease providing legal services to all clients"). Heller closed its premises, liquidated its assets, terminated its staff, and dispersed its lawyers. There was no identifiable successor firm. Indeed, the sheer number of law firms that Heller has sued shows how widely its shareholders were spread.[3] Because Heller could not handle its engagements, its clients *had* to take their work elsewhere. ER 9 (*Heller V*). And when clients did so, Heller's partnership business was wound up—regardless of whether clients then hired Jones Day, Smith & Smith, or another firm.

2. Partnership law does not support Heller's claims against Jones Day for another reason: The fiduciary duties on which Heller relies apply only to former Heller shareholders. Nothing in RUPA binds, or

[3] Heller initiated adversary proceedings against approximately 50 law firms, the vast majority of which have settled.

imposes fiduciary duties upon, third parties like Jones Day, which were never partners of Heller.

RUPA, as codified in California law, creates "a series of 'default rules' that govern the relations *among partners* in situations they have not addressed in a partnership agreement." RUPA (1997), prefatory note (emphasis added). For example, RUPA requires *partners* to account to one another for the use of "partnership property," which it defines as "[p]roperty acquired by a partnership." Cal. Corp. Code § 16203; *see id.* § 16204. It also requires *partners* "[t]o account to the partnership and hold as trustee for it any property, profit, or benefit derived by the partner in the conduct and winding up of the partnership business or derived from a use by the partner of partnership property." *Id.* § 16404(b)(1). The obligation to wind up partnership business is likewise a duty that partnership law imposes on *partners*. *See, e.g.*, *Osment v. McElrath*, 68 Cal. 466, 470 (1886); *Little v. Caldwell*, 101 Cal. 553, 560 (1894); *see also* Cal. Corp. Code § 16801(1). These obligations of a fiduciary relationship go hand in hand with the benefits of partnership. *Cf. Jewel*, 156 Cal. App. 3d at 179 (noting that it is fair to require former partners to account for profits they earn while winding up the dissolved firm's business because they also "will receive … their partnership share of income generated by the work of the other former partners").

Thus, when courts have required an accounting for profits derived from partnership business, they have imposed the duty only on a partner, not a third-party law firm, because of the partner's fiduciary duties to the partnership. *See, e.g.*, *Grossman v. Davis*, 28 Cal. App. 4th 1833, 1835-37 (1994); *Rothman v. Dolin*, 20 Cal. App. 4th 755, 756, 758 (1993); *Fox v. Abrams*, 163 Cal. App. 3d 610, 612, 617 (1985); *Jewel*, 156 Cal. App. 3d at 178-79; *Rosenfeld, Meyer & Susman v. Cohen*, 146 Cal. App. 3d 200, 210, 215-18 (1983); *Little*, 101 Cal. at 557-62; *Osment*, 68 Cal. at 467-68.[4] These cases emphasize that a partner's duty to account for profits directly follows from his "duty to wind up and complete the unfinished business of the dissolved partnership." *Jewel*, 156 Cal. App. 3d at 179; *see Rosenfeld*, 146 Cal. App. 3d at 217; *Little*, 101 Cal. at 560; *Osment*, 68 Cal. at 470. Without the duty to complete his dissolved firm's business, a former partner would have no duty to account upon dissolution.

It is undisputed that Jones Day never had any fiduciary duties to Heller and never entered into any partnership agreement with Heller. ER 57 (*Heller III*). To the contrary, before Heller collapsed, Jones Day was its competitor. Because Jones Day never had an obligation to wind up

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[4] Likewise, at common law, subject to limited, obscure exceptions not applicable here, courts did not order an accounting absent a fiduciary relationship between the parties. *See* C.C. Langdell, *A Brief Survey of Equity Jurisdiction*, 2 HARV. L. REV. 241, 248 (1889) ("[T]here must be a fiduciary relation between the plaintiff and the defendant, or, as the books of the common law express it, there must be a privity between them.").

Heller's partnership business, there is no basis for requiring Jones Day to account for any profits.

B. Cases Applying The So-Called Unfinished Business Doctrine Do Not Support Heller's Demand For Jones Day's Profits

To overcome these basic principles of partnership law, Heller looks to cases applying the so-called unfinished business doctrine. But those cases do not give Heller any property interest in Jones Day's profits. They are inapplicable on their facts and, in any event, have been superseded by RUPA.

1. There is no basis for treating the work Jones Day performed as it were done on Heller's behalf

In all of the cases on which Heller relies, an essential element of a firm's right to post-dissolution profits was that the profits were earned in performing work that *remained the business of the dissolving firm.* In some cases, the work remained the dissolved firm's business because former partners performed it under the original retainer agreement with the dissolved law firm. In other cases, courts treated the work as the dissolved firm's business as a matter of equity because a former partner or subset of partners violated fiduciary duties under UPA by cutting off their former partners' right to profits and diverting profits to themselves. Neither of these situations is present here. Those cases—which should be read in light of, and limited to, their facts—provide no basis for treating Jones Day's work as if it were performed on Heller's behalf.

a. *Osment* was a case in which a former partner continued to perform work under the *original* retainer agreement. A two-partner firm dissolved; one of its partners moved across the country, and the other continued to work on matters that clients still "intrusted to the [dissolved] firm." 68 Cal. at 467, 469. Although the parties initially agreed that they would share any contingency fee awards ultimately collected, the partner who completed the dissolved partnership's business later refused to share "*any*" of those fees—even though his former partner had never been paid for his earlier work on those matters.[5] *Id.* at 470 (emphasis added). The court rejected the partner's effort to appropriate the contingency fee awards for himself. *Id.* at 472.

b. In *Little*, the surviving partner of a two-partner firm attempted to cut off his deceased co-partner's entire interest in a contingency fee by signing a new retainer agreement diverting all profits to himself. The original retainer agreement gave the partnership 15% of any ultimate recovery. 101 Cal. at 557. Both partners worked on the case, but one of them died while it was pending and before either of them had been paid for their work. *Id.* The surviving partner signed a new agreement with the client allocating *all* fees to himself. *Id.* at 557-58. He refused to share any

[5] Heller incorrectly suggests that fees from hourly-rate matters were also at issue in *Osment* (OB 25). Although the former firm appears to have handled some non-contingency-fee matters, the parties disagreed only as to whether the plaintiff was "entitled to any share in the fees which were contingent." *Osment*, 68 Cal. at 467, 470.

of the contingency fee with his deceased partner's estate—not even a quantum meruit share of the award for his deceased partner's work—because, in his view, the new contract had cut off that partner's right to be paid. *Id.* at 558. The court rejected the surviving partner's attempt "make gain for himself at the expense of the estate of the deceased partner, by consenting to the extinguishment of a contract belonging to the partnership, and the substitution therefor of another relating to the same subject matter, and in the profits of which he *alone* is to participate." *Id.* at 561-62 (emphasis added).

c. *Jewel* likewise involved an attempt by former partners to misappropriate profits. A four-person partnership that primarily handled personal injury and workers' compensation cases split into separate two-partner firms. 156 Cal. App. 3d at 175. "[E]ach former partner sent a letter to each client whose case he had handled for the old firm, announcing the dissolution [and enclosing] a substitution of attorney form." *Id.* The only apparent effect of the partners' actions was to "cut off the rights of the other partners in the dissolved partnership": The same attorneys continued to handle each matter under the same fee arrangements. *Id.* at 175, 178. Nothing changed about the representations except that two partners kept all the profits at the expense of the others. Under these circumstances, the court held that the former partners violated their "fiduciary duty not to take any action with respect to unfinished partnership business for personal

gain." *Id.* at 178-79. It required partners to account for profits that it deemed in equity to have been earned on behalf of the dissolving partnership. Thus, a central premise of *Jewel* was that individual partners violated their fiduciary duties under UPA when they solicited clients during the dissolved firm's wind-up period, solely to cut off their co-partners' rights to profits and arrogate those profits to themselves. *See* ER 7 (*Heller V*).

d. The same is true of *Rosenfeld*, 146 Cal. App. 3d 200, which also involved a dispute about a dissolved partnership's interest in a contingency fee. Two partners from the original 17-partner firm handled the matter for many years, and the firm made substantial investments in the case. *Id.* at 209. But as the case neared its conclusion, the two partners handling it decided that they did not want to share *any* recovery with their co-partners. *Id.* at 209-10. Although the firm stood ready to continue handling the matter, the two partners forced its dissolution "for the very purpose" of cutting off their former co-partners' interest in any recovery. *Id.* at 210, 218. The two departing partners continued to perform the remaining work, and the only apparent intent and effect of the new retainer agreement that they signed with clients was to "cut off the rights of the other partners in the dissolved partnership." *Id.* at 219. Under these circumstances, the court found "an obvious and essential unfairness in one partner's attempted exploitation of a partnership opportunity for his own

personal benefit and to the resulting detriment of his copartners." *Id.* at 213. It thus required the former partners to account for the profits that they earned. *See id.* at 210, 215-18.

e. The other cases on which Heller relies involve similar breaches of fiduciary duty by individual partners. In several of those cases, former partners violated their fiduciary duties by arrogating profits to themselves and cutting off their co-partners' interests. *See, e.g.*, *Dickson, Carlson & Campillo v. Pole*, 83 Cal. App. 4th 436, 445 (2000) (two partners solicited firm's biggest client before their withdrawal); *Grossman*, 28 Cal. App. 4th at 1835-37 (partner refused to share contingency fee with his former partner, who had not yet been fully paid for his work on the matter); *see also, e.g.*, *Fox*, 163 Cal. App. 3d at 615. These and other cases involved individual partners who continued to perform the same work on the same matters that they had handled pre-dissolution; they were not situations in which clients retained a different third-party firm. *See, e.g.*, *Rothman*, 20 Cal. App. 4th at 756, 758; *Frates v. Nichols*, 167 So.2d 77, 79 (Fla. 1964); *In re Mondale & Johnson*, 437 P.2d 636, 638 (Mont. 1968); *Hurwitz v. Padden*, 581 N.W.2d 359, 360 (Minn. 1998). And in some cases, like *Osment*, the work remained the business of the dissolved firm as a matter of contract, because it was performed under the *original* retainer agreement. *See, e.g.*, *Denver v. Roane*, 99 U.S. 355, 356 (1878); *Beckman v. Farmer*, 579 A.2d 618, 636 (D.C. 1990). Thus, in each case, the former

firm's right to post-dissolution profits was based on the court's determination—as a matter of contract or equity—that the profits were earned in completing the work that *remained the business of the dissolving firm.*

f. Here, there is no similar basis to treat the work performed by Jones Day as if it were done on Heller's behalf.

Unlike in cases applying the so-called unfinished business doctrine, clients did not retain individual former Heller shareholders; they retained Jones Day and thereby entered into substantively new representations with a third-party firm that provided vast resources, personnel, capital, and services beyond those of the liquidated Heller. ER 9 (*Heller V*). Indeed, clients testified that they would not have hired an individual Heller shareholder who "opened his own office as a solo practitioner" and lacked the "capability of handling [their] legal needs." SER 47 (Leibowitz Decl.); SER 50 (Goldfischer Decl.). Instead, they "retained Jones Day, not any particular lawyer, and [they] did so because [they] believed that Jones Day had the resources and expertise to represent [them] in [their] best interests." SER 50 (Goldfischer Decl.); SER 47 (Leibowitz Decl.).

The new agreements that clients signed with Jones Day thus had nothing to do with wrongfully diverting profits from Heller: Clients chose to retain and pay a new firm with new resources and new attorneys to perform their work. "Jones Day clients are regularly served by cross-office

and cross-practice teams," SER 62-63 (Sims Decl.); and by compensating Jones Day for the work it did on their matters, clients intended to "provide incentives for the firm to handle [their] matters in a first rate manner and use the best team at the firm to work on the matters," SER 54 (Garten Decl.). Heller shareholders did not "cut off the rights of the other partners in the dissolved partnership by the tactic of entering into a 'new' contract" that merely diverted profits to those individuals without changing anything else about the representation. *Jewel*, 156 Cal. App. 3d at 178.

Moreover, clients *had* to engage new representation: Heller expressly abandoned them, announcing that it could no longer provide any legal services. ER 9 (*Heller V*); ER 58 (*Heller III*). When Heller closed its premises, liquidated its assets, fired its staff, and dispersed its lawyers, it "le[ft] clients with ongoing matters no choice but to seek new counsel." ER 9 (*Heller V*). Heller had no rights or opportunities that could have been "cut off." Far from usurping an opportunity from Heller (which Jones Day would have been free to do anyway), Jones Day's conduct in responding to the needs of the clients that Heller abandoned is beyond reproach.

Finally, Heller's cases overwhelmingly involved situations where the dissolved firm had never been compensated for work it performed and risk it assumed in handling contingency-fee matters. In that context, it is unsurprising that a firm's interest in the contingency fee recovery constitutes an "asset" that former partners cannot appropriate for

themselves. *Cf. Siciliano v. Fireman's Fund Ins. Co.*, 62 Cal. App. 3d 745, 759 (1976) (discharged attorney entitled to enforce lien for "the reasonable value of the services performed by him to the date of discharge"). Here, by contrast, Heller has already been paid for its work on the hourly-rate matters at issue. And it has no enforceable right to profits that might be earned on future hourly-rate work. *See supra* 17-19.

Under these circumstances, there is no basis to treat Jones Day's work as if it were Heller's partnership business. Heller concedes that it would not have any right to Jones Day's profits if Jones Day had not taken on any former Heller shareholders. ER 55 (*Heller III*). There is no reason for a different result here merely because some Heller shareholders joined Jones Day. When a former client terminates a dissolved partnership and enters a new contract, with a new firm that has new management, partners, associates, resources, and expertise, there is no more partnership business for the dissolved partnership to handle; the matter is wound up.

2. RUPA supersedes all of the decisions on which Heller relies

All of the decisions on which Heller relies also interpreted and applied UPA,[6] which has been superseded by California's subsequent adoption of RUPA. Even under a proper understanding of UPA, Heller's

[6] *See, e.g., Dickson*, 83 Cal. App. 4th at 445 n.6; *Rosenfeld*, 146 Cal. App. 3d at 216 n.4; *Jewel*, 156 Cal. App. 3d at 176; *Fox*, 163 Cal. App. 3d 610; *see also Little*, 101 Cal. at 560-61 (applying no-compensation rule that was later codified by UPA); *Osment*, 68 Cal. at 471 (same); OB 25 n.19, 39 (collecting cases from other jurisdictions interpreting and applying UPA).

claims would fail. *See Thelen*, 24 N.Y.3d 16 (applying UPA, which still governs in New York). The claims are all the more unsupportable under RUPA, which eliminated the statutory underpinnings of the *Jewel* line of cases. Indeed, although it is "the most widely cited unfinished business decision in California" (OB 21), no published decisions from any California court applying RUPA cite *Jewel* for its unfinished business holding.

Two aspects of UPA were essential to *Jewel* and its progeny. *First*, UPA did not allow partners any extra compensation for "winding up" the business of a dissolved partnership unless a partner had died. UPA § 18(f) (1914). UPA's no-compensation rule was central to *Jewel*'s determination that a partner could not be compensated based on his post-dissolution efforts (i.e., on a quantum meruit basis), and instead was entitled only to his partnership share of any post-dissolution profits. *See Jewel*, 156 Cal. App. 3d at 176-77; *see also Fox*, 163 Cal. App. 3d at 613-14. *Second*, *Jewel* found the former partners' conduct particularly egregious because they had violated their fiduciary duty under UPA "not to take any action with respect to unfinished partnership business for personal gain." 156 Cal. App. 3d at 178-79; *see also Rosenfeld*, 146 Cal. App. 3d at 217-18; *Fox*, 163 Cal. App. 3d at 616. RUPA eliminated both of these provisions.

a. Many courts and commentators perceived UPA's no-compensation rule as inequitable and unfair, "particular[ly]" "in law firm

partnerships" and other service partnerships where the burden of winding up often fell disproportionately across partners. UPA Revision Subcommittee of the Committee on Partnerships & Unincorporated Business Organizations, *Should the Uniform Partnership Be Revised?*, 43 BUS. LAW. 121, 148 (1987); *see, e.g.*, *Bushard v. Reisman*, 800 N.W.2d 373, 382 (Wis. 2011) (collecting sources). RUPA addressed those concerns by providing that all partners are entitled to "reasonable compensation" for services they provide in "winding up" the business of a dissolved firm. Cal. Corp. Code § 16401(h). In other words, RUPA codifies the very rule that UPA prohibited. It thereby provides that a partner should be paid according to the amount of post-dissolution work he actually performs. *See Jewel*, 156 Cal. App. 3d at 176-77.

Moreover, in the competitive market for hourly-rate legal services, reasonable compensation means the rate that a firm charges clients. That follows not only from economic common sense, but also from longstanding California law construing reasonable compensation to include all profits "attributable to the services and skill" of the partner who performs services in winding up partnership business. *Jacobson*, 29 Cal. 2d at 30 (discussing UPA § 18(f)).

In *Jacobson*, a two-partner construction business dissolved upon one partner's death, and the surviving partner wound up the business by completing a pending project. *See id.* at 26-27. *Jacobson* explained that

the "reasonable compensation" due to the surviving partner depends upon "how much of the profits is attributable to [his] services and skill … , and how much to the capital invested in the business." *Id.* at 30 (quoting *Whittaker v. Jordan*, 104 Me. 516, 522 (1908)). While a surviving partner is entitled to all profits attributable to his "time, labor, and skill" in winding up the dissolved firm's business, *id.* at 29, 31, "the most that the representatives of the deceased partner can justly demand is that [the surviving partners] … account to them for the[] [use of the former partnership's] capital, and, in addition, for whatever it has earned," *id.* at 30 (quoting *Whittaker*, 104 Me. at 522). *Cf. Vangel v. Vangel*, 45 Cal. 2d 804, 808-09 (1955) (distinguishing between profits attributable to labor and skill as opposed to use of a partnership's capital). In other words, the only profits owed the dissolving partnership are those post-dissolution profits attributable to partnership capital. *See Jacobson*, 29 Cal. 2d at 30-31; *see also Urzi v. Urzi*, 140 Cal. App. 2d 589, 592-94 (1956).

The California legislature is presumed to have been aware of this understanding of "reasonable compensation" when it enacted RUPA. *See Ketchum v. Moses*, 24 Cal. 4th 1122, 1135 (2001). And in the context of legal services, all post-dissolution profits are attributable to the skill and

services of the attorney who actually performs the work. The defunct firm therefore has no interest in those profits.[7]

Here, it is undisputed that Jones Day used entirely its own capital to earn the profits at issue. Heller contributed no resources of any sort—capital, labor, or otherwise—to help Jones Day represent its clients. Nor did Heller bear any of the risks of representing clients, like nonpayment or malpractice claims. Yet it now claims a right to all of Jones Day's profits—essentially, a risk-free annuity in perpetuity for profits from the matters that it abandoned. The equitable concerns that prompted RUPA's abrogation of the "no-compensation" rule repudiate this unfair result. *See supra* 36-37.

b. RUPA also makes clear that the duty at issue in *Jewel*—"not to take any action with respect to unfinished business for personal gain," *Jewel*, 156 Cal. App. 3d at 178-79—no longer applies. Specifically, § 404(b)(3) of RUPA provides that a partner must "refrain from competing with the partnership in the conduct of the partnership business *before the dissolution of the partnership*." *Id.* (emphasis added). As the drafters of

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[7] Reasonable compensation may be less than all profits in two circumstances, neither of which is at issue here. First, in the contingency-fee context, a former firm has an interest in being paid for risk it assumed, in addition to the quantum meruit value of work it actually performed. Second, in the hourly-fee context, a former firm has a right to compensation if its former partners generate post-dissolution profits using the former firm's capital (e.g., office space, computer equipment, etc.).

RUPA explained, this provision means that "[t]he duty not to compete … does not extend to winding up the business, as do the other loyalty rules." RUPA § 404 cmt. n.2. Accordingly, "a partner is free to compete immediately upon an event of dissolution." *Id.* The freedom to compete means that a former partner can solicit his former firm's clients, including by signing new retainer agreements regarding matters previously handled by the former firm.

Thus, even if an individual Heller shareholder were to solicit a former Heller client for a matter that Heller had been handling, RUPA provides that this would not, as *Jewel* and other cases stated, violate the "fiduciary duty not to take any action with respect to unfinished partnership business for personal gain." *Jewel*, 156 Cal. App. 3d at 178-79. Under RUPA, the dissolved firm would have no right to demand an accounting for profits earned by its former partner under a new retainer agreement with the client. The new agreement *would* "transform[] the old firm's unfinished business into new firm business" and eliminate any duty to account. *Id.* at 176. And it is even more apparent that *Jewel* does not apply where Jones Day—a third party with no "fiduciary obligations" to Heller—agreed to represent clients. *See* ER 57 (*Heller III*); ER 10 (*Heller V*).

* * *

In sum, "there is no provision of the RUPA that gives the dissolved firm the right to demand an accounting for profits earned by its former

partner under a new retainer agreement with a client," much less under a new retainer agreement between a client and a third-party firm. ER 10.

C. Heller's Efforts To Sidestep Critical Legal And Factual Differences Between This Case And Others Involving Partnership Law Fail

Heller's attempts to overcome the critical legal and factual differences between this case and the *Jewel* line of cases are wrong at every turn.

Heller first overlooks the stark factual differences between this case and the ones on which it relies, by insisting that questions about the liability of third-party firms are "issue[s] of federal [fraudulent-transfer] law." OB 37. But fraudulent transfer law merely allows a debtor to trace money or property that otherwise belongs to it as a matter of state law. Any interest that a dissolved firm has in post-dissolution profits is based on its *former partner's* completion of the *dissolved partnership's business*. Here, Heller's partnership business was wound up when Heller fired its clients. And, in any event, Heller's former partners did not complete the partnership business themselves; a third party handled the work instead. In those circumstances, a dissolved firm has no interest in Jones Day's profits. Heller cannot use fraudulent-transfer law to hide behind the fact that it has no state-law property interest on these facts.[8]

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[8] Moreover, this Court routinely considers the factual context in which certified questions arise. *See, e.g.*, *Sentry Select Ins. Co. v. Fid. &*

Heller disregards the one case that does involve facts similar to those at issue here—*Thelen*—because it applied New York law. OB 38. But *Thelen* is based on principles that California law has long embraced, including a client's "unqualified right to terminate the attorney-client relationship at any time." *Thelen*, 24 N.Y.3d at 28; *see supra* 17-19. Because of this right, *Thelen* explained that "future hourly legal fees" are "too contingent in nature and speculative to create a present or future property interest." *Id.* The same is true under California law, which likewise recognizes that someone "who merely foresees that he might receive a future beneficience" has no enforceable property right. *In re Marriage of Brown*, 15 Cal. 3d 838, 845 (1976); *see also, e.g., In re Marriage of Spengler*, 5 Cal. App. 4th 288, 299 (1992).[9] While Heller

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Guar. Ins. Co., 46 Cal. 4th 204, 214 (2009); *Murray v. Alaska Airlines, Inc.*, 50 Cal. 4th 860, 866 (2010); *Minkler v. Safeco Ins. Co. of Am.*, 49 Cal. 4th 315, 333 (2010). There is no basis for ignoring the facts here. *Cf. Thelen*, 24 N.Y.3d at 30 (distinguishing cases applying the so-called unfinished business doctrine based on factual differences).

[9] In light of a client's "absolute" "power to discharge an attorney, with or without cause," *Fracasse*, 6 Cal. 3d at 790, cases involving contracts that could *not* be terminated unconditionally are inapposite, *see H&M Assocs. v. City of El Centro*, 109 Cal. App. 3d 399, 414 (1980) (Staniforth, J. concurring) (discussing restrictions on termination of public utilities contract); *Anton v. San Antonio Cmty. Hosp.*, 19 Cal. 3d 802, 824-25 (1977) (finding that admission privileges at hospital could be revoked "only after a showing of adequate cause … in a proceeding consistent with minimal due process requirements"). So, too, are cases imposing liability on third parties who intentionally cause a client to discharge his attorney: The cases Heller cites involve non-payment of legal services *already* rendered; they do not support the sort of guaranteed stream of windfall profits Heller seeks here. *See Abrams & Fox, Inc. v. Briney*, 39 Cal. App.

claims that *Thelen* is out-of-step with the law of other jurisdictions, none of the cases it cites (OB 39-40) supports imposing liability on a third-party firm that clients chose to handle their matters after firing a defunct firm. Indeed, *LaFond v. Sweeney* recognized that a different situation arises when a "client … terminate[s] representation by the [dissolving] law firm and enter[s] into a new contract with a different law firm." 343 P.3d 939, 948 (Colo. 2015).

Finally, Heller argues that RUPA did not expand a partner's ability to compete with his former firm. OB 16, 31-32. But Heller's own authorities recognize that RUPA "provides significant changes and additions to the [UPA] statutory formulation" of fiduciary duties. Senate Rules Committee, Senate Floor Analysis, AB 583 (Aug. 23, 1996), at 5. Those same authorities also acknowledge that "it is difficult to say with certainty if RUPA will have any significant impact on existing law." *Id.* In particular, the Senate Floor Analysis highlighted changes regarding the freedom to compete: At least one California case applying UPA "held that a partner's duty not to compete survives his withdrawal from the partnership," but RUPA allows a partner to compete *immediately* upon dissolution or withdrawal. *Id.* at 7; *see* RUPA § 404(b)(3) & cmt. 2; *id.*

3d 604, 609 (1974); *Skelly v. Richman*, 10 Cal. App. 3d 844, 850 (1970). Moreover, whatever rights a law firm has to protect its client engagements from interference by third parties, it surely has no right to protect a client engagement that it has expressly abandoned.

§ 603(b)(2). That freedom is particularly obvious where, as here, Heller imploded and announced that it would no longer provide legal services, and thus could not itself handle or compete for any matters. And in any event, none of the cases Heller claims RUPA codified supports its effort to confiscate fees earned by a third-party firm on hourly-rate matters that Heller abandoned. *See supra* 28-35.

D. Heller's Policy Arguments Are Wrong

Heller's attempts to minimize the adverse policy consequences of its theory are also unavailing.

First, Heller asserts that *Jewel* and other California cases have rejected concerns about client choice and equity. OB 23, 41. Not so. *Jewel* considered only the effects of applying the so-called unfinished business rule to former partners in the dissolution context before it: Former partners sharing profits on work that was their former firm's partnership business. *Jewel* does not speak to the implications of depriving a third-party firm of profits it earns for work that is the third party's partnership business.

Depriving a third-party firm of profits for its work will severely impair a client's choice of counsel. Third-party firms have no duty to take on any matters previously handled by a dissolving firm, and imposing a 100% tax on profits from such matters would obviously discourage firms from taking them on. That, in turn, would make it less likely that clients,

left in the lurch by a firm like Heller, could retain a new firm while simultaneously benefitting from the services of a partner already familiar with the pending matter. *See* SER 54 (Garten Decl.) (explaining that if Heller's rule were adopted, "lawyers working on my companies' matters at a firm that dissolves will find it more difficult to join another law firm," and "the new law firm would have an incentive not to take on my companies' matters, forcing us to find new counsel and incur additional expenses and delay in the handling of our matters").

This does not mean that a "lawyer's competence and commitment will rise or fall depending on the profitability of a given client matter." OB 41. Rather, it recognizes that "[l]aw firms accepting a new client, even for an hourly-fee matter, must be prepared to invest considerable resources: attorney salaries; malpractice insurance; administrative support; research fees; document preparation; space allocation; opportunity costs; and so on." ER 15 (*Heller V*). In light of these investments, "[n]o firm can be expected to contribute those resources if they are not entitled to retain the corresponding profits." *Id.* And while Heller claims that its position has had no impact on client choice (OB 41), that is because no appellate court has ever adopted it. Indeed, before *Brobeck* was decided in 2009, *no* court had imposed liability on third-party firms for profits earned from their own work. *Brobeck* was never reviewed on appeal, and—as *Thelen* demonstrates—it was wrongly decided.

Moreover, the record in this case dispels any doubt that clients care if their law firms are forced to work on a nonprofit basis. Clients attested that they "have always expected" the law firms they retain to "keep the fees that [their] company paid for hours that the firm worked." SER 53 (*id.*); *see* SER 47-48 (Leibowitz Decl.) ("I believe it is in the interests of [my company] for its outside counsel to retain all of the fees that we pay for the resources and expertise they bring to bear in its engagement for us."); SER 50-51 (Goldfischer Decl.) (same). Forcing a law firm to "disgorge" profits would harm clients by giving a firm "less financial incentive to devote its best people to [a] matter[]" or causing it to refrain from taking on the matter altogether. SER 54 (Garten Decl.).

Second, Heller's argument that a third-party firm may keep "reasonable compensation" before remitting its profits to the dissolved firm provides little consolation.[10] OB 38, 41. Working at a discount is still a disincentive for taking on matters. And at least under the Bankruptcy Court's understanding, the discount would be enormous: That court believed that reasonable compensation is limited to expenses directly attributable to work on matters formerly handled by Heller, *see* ER 30-33, such that Heller's net recovery would be "the amount it would have recovered if it had completed the Unfinished Business" itself, ER 35. On

[10] The same is true regarding the prospect that firms might secure future business from clients. *See* OB 7. Future business is never a guarantee, and many clients do not have recurring legal needs.

top of that, there is no way for the firms to predict how long they must forfeit their profits on matters previously handled by a defunct firm (e.g., until the case is appealed? Until the U.S. Supreme Court denies certiorari? And what about open-ended retainer agreements for ongoing counseling?). Making these determinations would require complex litigation, as the extensive proceedings in the Bankruptcy Court demonstrate. The prospect of having to litigate in order to secure any remuneration at all would further discourage firms from taking on such matters in the first place.

Third, Heller speculates that, unless it prevails, law firms will accumulate debt with impunity and creditors will never be repaid. OB 32-33. But as Heller's plan administrator admitted, lawyers already have strong disincentives to engage in such conduct, including the possibility that they would be denied a discharge through bankruptcy and the virtual certainty that they would lose all the capital they had invested in their law firms. SER 42-43 (Burkart Dep.). Moreover, lenders—who have their own incentives to conduct due diligence—are unlikely to enable such behavior. In any event, contrary to Heller's suggestions (OB 13, 32), RUPA is not a bankruptcy statute, and the winding up process has many purposes beyond paying creditors—the most obvious of which is providing closure and finality to former partners. Heller's theory thwarts that objective by prolonging wind-up for the life of any legal matter previously handled by the dissolved firm—an "indefinite continuation of the partnership business

[that] is contrary to the requirement for winding up of the affairs upon dissolution." *King v. Stoddard*, 28 Cal. App. 3d 708, 712 (1972).

Fourth, Heller claims that its rule is necessary to "avoid asset-grabbing and other misconduct during partnership dissolutions." OB 34. Of course, client matters do not belong to firms or lawyers in the first place—they belong to the clients. *See supra* 17-19. And RUPA expressly *allows* partners to compete with one another upon dissolution. *See supra* 39-40; RUPA § 404(b)(3); *id.* cmt. 2. The unfairness that occurs when a partner surreptitiously competes with his partners *before* departing, *see Dickson*, 83 Cal. App. 4th at 440-41, is actionable without regard to the so-called unfinished business doctrine, *see* RUPA § 404(b)(3). To the extent Heller believes its approach "promotes orderly dissolution," OB 35, the record in this case demonstrates that—at least when a law firm implodes—the opposite is true. *See supra* 5 (discussing expected benefits of *Jewel* provision).

Finally, Heller attempts to mitigate the consequences of its position by noting that parties are free to contract around its proposed default rule. OB 34-35. But Heller's theory that client matters are law firm "property" is incompatible with public policy, and thus creates "a deficiency" that cannot be "cure[d]" by agreements contracting around it. *Thelen*, 24 N.Y.3d at 33. Furthermore, default rules are fashioned to provide an equitable or efficient arrangement for the vast majority of cases, in the absence of an express

agreement. Richard A. Epstein, *In Defense of the Contract at Will*, 51 U. CHI. L. REV. 947, 951 (1984). A default rule that the parties must routinely modify to comport with public policy and preserve client choice contravenes the very purpose of default rules in the first place.

E. *Howard v. Babcock* Provides No Support For Heller's Claims

Finally, Heller's extensive reliance on *Howard v. Babcock*, 6 Cal. 4th 409 (1993), is misplaced.

In *Howard*, this Court upheld an express agreement that required withdrawing law firm partners to forego certain benefits if they immediately competed with the firm within one year of their departure. *Id.* at 413. Acknowledging the importance of the public policy in favor of client choice, *Howard* nevertheless held that the parties' agreement, which was presumptively enforceable as a matter of contract, did not contravene public policy enough to be "void on its face." *Id.* at 425.

But *Howard* did not, as Heller claims, prioritize a law firm's interest in preventing partners from leaving above all other considerations, including client choice. OB 26-28 & n.20, 35. Rather, on the particular facts before it—involving the enforceability of an express agreement that narrowly circumscribed the permissible competition between a law firm that remained in business and its former partners—*Howard* "balance[d] … the interest of clients in having the attorney of choice, and the interest of law firms in a stable business environment." *Howard*, 6 Cal. 4th at 425.

A different balance applies here, where Heller's proposed default rule for partnership agreements places a 100% tax on profits earned by third parties on matters previously handled by a defunct firm in perpetuity. Indeed, *Howard* "consider[ed] it obvious that an absolute ban on competition with the partnership would be per se unreasonable, and inconsistent with the legitimate concerns of assuring client choice of counsel and assuring attorneys of the right to practice their profession." *Id.* Moreover, any "balance" of interests here must account for (1) the absence of any fiduciary relationship between Jones Day and Heller, let alone an express agreement between them; and (2) Heller's express abandonment of its clients, leaving them no choice but to find new counsel. Heller's demand for profits for work that it did not perform would undermine the rights of the very clients that it left in the lurch. *See supra* 17-19. And because a partner who leaves a law firm before dissolution has no duty to account, Heller's proposed rule would encourage "partners to get out the door" at the first sign of financial trouble, jeopardizing the stability Heller claims is so important. *Thelen*, 24 N.Y.3d at 32.

Contrary to Heller's assertion (OB 26), *Howard*'s shorthand reference to matters as "assets" in its recitation of the facts says nothing about whether a law firm has a property interest in future fees for work not yet performed on pending matters. That was simply not at issue in the case. *Cf. People v. Knoller*, 41 Cal. 4th 139, 155 (2007) ("An appellate decision

is not authority for everything said in the court's opinion but only for the points actually involved and actually decided."); *Elisa B. v. Superior Ct.*, 37 Cal. 4th 108, 118 (2005) ("Language used in any opinion is of course to be understood in the light of the facts and the issue then before the court, and an opinion is not authority for a proposition not therein considered."). Nor does *Howard* cite *Jewel* for this proposition. *Howard*'s passing citation of *Jewel* in a footnote, *see* 6 Cal. 4th at 424 n.8, cannot be read as an endorsement of *Jewel*'s analysis of an issue that *Howard* never considered. By its terms, *Howard*'s footnote observed that a dissolved partnership's interest under *Jewel* may operate as a disincentive on the withdrawing partner to continue to represent his former firm's clients. *Id.* But *Howard* neither discussed the scope of that interest nor said anything about the consequences of extending *Jewel* to *third-party* firms. *See supra* 44.

Heller's assertion that *Howard* rejects any attempt to treat law firms differently than any other partnership is irrelevant. OB 27, 36-37. The question here is not whether law partnerships (of whatever size) are subject to different rules governing the division of partnership property. Indeed, they are not: When it comes to cognizable property interests (e.g., a firm's accounts receivables, or the use of its office buildings or computers), former partners have a duty to account. The question here, however, is whether a defunct firm has any cognizable property interest in client

matters or future hourly fees—a question about which "Partnership Law itself has nothing to say." *Thelen*, 24 N.Y.3d at 28.

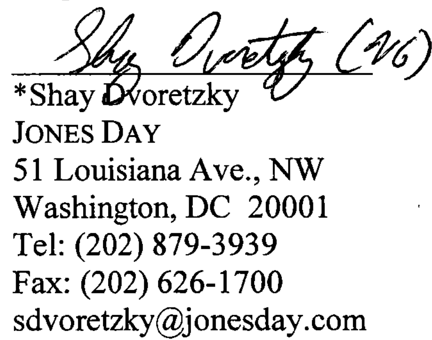
Finally, Heller also relies on *Anderson, McPharlin & Connors v. Yee*, 135 Cal. App. 4th 129 (2005), and *Haight, Brown & Bonesteel v. Superior Court*, 234 Cal. App. 3d 963 (1991). But, like *Howard*, those cases considered only whether attorneys may *voluntarily* agree to incur a reasonable penalty for competing against their former firm; they say nothing about whether such a penalty can be imposed on a *third-party* firm as a *default rule*. *Cf. Ruby v. Abington Mem. Hosp.*, 50 A.3d 128, 136 (Pa. Super. Ct. 2012) (upholding partnership provision allocating contingency fees upon partner's withdrawal, and distinguishing *Mager v. Bultena*, 797 A.2d 948 (Pa. Super. Ct. 2002), which did not involve a specific agreement and rejected firm's claim that it was entitled to fees earned by former partner after he withdrew). And, also like *Howard*, both cases involved penalties that were limited in time and scope. *See Haight*, 234 Cal. App. 3d at 966 (forfeiture of withdrawal benefits for competing within three years in certain cities); *Anderson*, 135 Cal. App. 4th at 131 (damages based on 25% of fees realized over two-year period following partner's departure). Neither case supports requiring an attorney to perpetually forfeit all fees earned on any client matter previously handled by his former firm—the sort of "absolute ban on competition" that *Howard* condemned. *Howard*, 6 Cal. 4th at 425.

CONCLUSION

For these reasons, this Court should hold that, where a law partnership dissolves and its clients hire another pre-existing law firm, the dissolved firm has no interest in fees earned by the replacement firm on hourly-rate matters previously handled by the dissolved firm.

February 2, 2017

Respectfully submitted,



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CERTIFICATE OF COMPLIANCE

I hereby certify that this brief complies with Rules 8.204(b) and 8.520(b)(1) because it has been prepared using proportionately spaced, 13-point Times New Roman typeface. This brief complies with the volume limitation of Rule 8.520(c) because it contains 12,850 words, as counted using the word-count function on Microsoft Word 2007 software.

I declare under penalty of perjury that this Certificate of Compliance is true and correct.

February 2, 2017

Shay Dvoretzky

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I am more than eighteen years old and not a party to this action. My business address is Jones Day, 555 California Street, #26, San Francisco, CA 94104. On February 2, 2017, I served true copies of **ANSWER BRIEF OF JONES DAY** on the interested parties of this action by placing a true copy thereof in sealed envelopes, addressed as follows:

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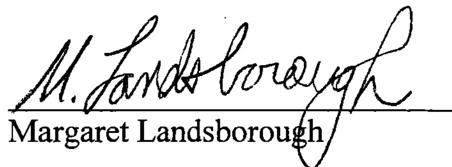
I am employed in an office of a member of the bar of this court at whose direction the service was made.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct, and that this declaration was executed on February 2, 2017, at San Francisco, California.



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