

CASE NOTES

Summary Judgment Denied in Case Filed Against Partners of Bankrupt Law Firm

By Lynn J. Hinson

In re: Thelen LLP, 2014 WL 2178156 (Bankr.S.D.N.Y. May 23, 2014)

In *In re: Thelen LLP*, 2014 WL 2178156 (Bankr.S.D.N.Y. May 23, 2014), the United States Bankruptcy Court denied the bankruptcy trustee's motion for summary judgment on contract and constructive fraudulent transfer claims filed against equity partners of a law firm that filed under Chapter 7.

Background

On October 28, 2008, the firm's partners voted to voluntarily dissolve the firm. The firm was dissolved on November 30, 2008, and filed under Chapter 7 ten months later.

The partners entered into partnership agreements prior to dissolution of the firm. After the firm filed, the Chapter 7 trustee commenced adversary proceedings against the partners to recover damages based on breach of the agreements and constructive fraudulent transfers. The constructive fraudulent transfer claim was based on the advances that each of the partners received prior to a determination of their entitlement to an allocation of the net profits of the firm.

The trustee sought to recover damages from each partner based on the difference between the advances they received and their allocation of the net profits. The trustee asserted that failure to return the difference was a breach of the agreements and that the advances were made for less than reasonably equivalent value when the firm was insolvent.

The parties agreed that the fraudulent transfer claims should be decided prior to the contract claims. The trustee thereafter moved for summary judgment, including deciding the date of the transfer of the alleged overpayments for fraudulent transfer purposes.

Breach of Contract Claims

The agreements provided that each of the partners would receive their proportionate share of the net income of the firm and that the partners could receive periodic advances as draws against their share of the net income. According to the agreements, the allocation of net income to a partner would be reduced by "prior draws or other advances."

It was uncontested that in 2008, the partners generally received draws twice a month. The trustee contended that the partners were entitled only to their share of the net income for the calendar

year 2008, and that the draws exceeded the net income. The trustee claimed that according to the agreements, the partners' allocable share of net income was to be determined as of December 31, 2008.

Using this calculation, the trustee argued that the netting resulted in a deficiency that each partner was required to repay because each partner received advances in excess of his or her allocable share of the net income. The partners argued, inter alia, that the agreements provided that a partner's obligation to repay was dealt with exclusively by an adjustment to the partner's capital account. The court decided that it was not possible to rule on the competing positions except by construction of the agreements. Based on the parties' agreement that the contract claims would be determined only after the fraudulent conveyance issues, the court stated that it would be unfair to first rule on the contractual construction issues.

Fraudulent Transfer Claims

The trustee sought summary judgment finding that the date of the alleged transfers for fraudulent conveyance purposes was December 31, 2008. The basis for the trustee's motion was that the final determination of net income was to be made at the end of the 2008 calendar year and that the advances made to the partners should be netted against the net income calculated as of December 31, 2008.

The court found that under the facts of the case, it would be inappropriate to deem year-end 2008 as the relevant date for fraudulent conveyance purposes. If summary judgment was granted, December 31, 2008, would become the date for determining solvency or insolvency. The court held that the trustee could not be relieved of the obligation to prove insolvency by moving that date to the end of 2008. Therefore, the motion for summary judgment as to the fraudulent transfer date was denied.

The trustee also sought summary judgment declaring that the agreements conclusively established the reasonably equivalent value of each partner's services for fraudulent conveyance purposes. The court denied the summary judgment motion based on its finding that the partners should not be bound by the agreements because the contract was never fully performed. In addition, the firm was dissolved before the end of the year, and the partners were called on to perform under extraordinary circumstances.

Finally, the court determined that the contract issues dominated the disputes. A hearing was scheduled to decide whether the appropriate resolution of the case would be to decide the contract issues immediately, reserving the fraudulent transfer issues for later determination.

Keywords: bankruptcy and insolvency litigation, fraudulent transfer claims, Chapter 7

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