
APPENDIX T

TRANSFER OF A LAW PRACTICE

For all time prior to the last decade, lawyers in America were perhaps the only corps of professional people who were prohibited from recognizing any financial value from their good names and the goodwill of their practices. We were told that clients were not chattels or vendible commodities, that lawyers were not tradesmen, and that the sale of law practices would necessarily involve the disclosure of client confidences and secrets, a serious violation of a core principle of our profession. Lawyers, therefore, had nothing to sell but their desks, their chairs, their typewriters and their libraries.

In 1989, however, the Supreme Court of California promulgated a new rule of professional conduct that for the first time permitted the sale of the goodwill aspects of a deceased lawyer's practice by his or her surviving spouse or estate. In 1990, given that impetus, the American Bar Association adopted a new Rule 1.17 to its Model Rules of Professional Conduct that proposed, even more expansively, to permit the sale of law practices. Since the ABA has no authority to promulgate rules enforceable in any of our jurisdictions, each had to decide for itself whether it would follow California's and the ABA's lead. Indeed, it was not long before a substantial number of them did, and now no fewer than 41 jurisdictions permit such transfers, whether by rule or otherwise, New York included. New York's rule governing the sale of a law practice can be found at 22 NYCRR §1200.15-a. It is more readily recognizable as Disciplinary Rule (or DR) 2-111. See also Ethical Considerations (or ECs) 2-34 to 2-36.)

What the rule means, in general terms, is that lawyers, their personal representatives and their estates may transfer for value, under specifically stated limited conditions, not only the property comprising the physical plants in which they practice, but also the value of their own good names, their reputations and the cases and matters they have in their offices, and they can do so whether upon a lawyer's retirement, disability, or death. Attorneys licensed to practice in more than one jurisdiction, therefore, should take extreme care to identify the conditions under which they may transfer their respective practices for value. The following information pertains only to the New York rule.

Who May Transfer a Law Practice for Value?

Lawyers retiring from the private practice of law, or law firms one or more of whose members are retiring from the private practice of law within the firm, or the personal representatives of deceased, disabled or "missing" lawyers may sell the lawyers' or firms' law practices, including their goodwill.

We deal here primarily with solo practitioners, however. For many years, law firm partners have found legitimate ways, though not authorized by rule, to transfer the value of their practices upon retirement, disability or death, usually by means of in-house contractual arrangements with their long existing or even newly acquired partners or associates. Until now, solo practitioners have never had that opportunity, and that was the inequity of the former rule. Now they may do so.

But not only may solo practitioners or their personal representatives, by specific rule, and for value, transfer the goodwill and other proprietary aspects of their practices upon retirement, disability or death; so also may non-solo law firms by specifically stated means. It would appear, therefore, that the inclusion in the new rules of a specific grant of right to members of non-solo law firms represents merely the drafters' acknowledgment of the existence of an already acceptable, long-standing end, but not necessarily its means.

Interestingly, the rule also applies to situations wherein lawyers are missing, but it does not define the term “missing.” We will use “missing” to refer to attorneys absent without explanation of reason for more than 21 days.

To Whom May a Law Practice be Transferred for Value?

A private practice may be sold to one or more other lawyers or law firms. That obviously includes any practitioner licensed and in good standing to practice law in the State of New York and any similarly situated New York law firm. Does it mean that a practice may be sold to a non-New York lawyer or law firm? The rule doesn’t address the question, but since those unlicensed in New York are generally considered not to be lawyers for purposes of practicing here, presumably they would be excluded.

What about multi-jurisdictional firms, i.e., those with offices in more than one jurisdiction, where each such office is staffed by attorneys licensed to practice in the state wherein they are assigned by the firm as, for example, in New York? Presumably they would qualify for such purpose.

And what about firms whose professional staffs are not licensed to practice in New York and who do not have a presence here? Under newly proposed multi-jurisdictional practice rules, out-of-state attorneys would be authorized to represent clients in New York in specially restricted ad hoc situations. Would they qualify as purchasers? Obviously the rule does not address that unforeseen issue either, but again, since unlicensed out-of-state lawyers cannot maintain ongoing practices in New York, presumably the application of the rule would prohibit such transfers to them as well.

Clients’ Confidences and Secrets; Conflicts

Most sensitive is the issue of clients’ confidences and secrets. Rule 2-111(B) states the conditions under which confidences and secrets may be disclosed in the course of negotiations involving the transfer of law practices. It is a critical section of the Code that cannot be ignored. Initially, Rule 2-111(B)(1) provides that the seller of a law practice may provide prospective buyers with any information not protected as a confidence or secret under DR 4-101. DR 4-101 is the key disciplinary rule in New York’s Code of Professional Responsibility that governs the preservation of clients’ confidences and secrets. It defines “confidence” as information protected by the attorney-client privilege under applicable law. It defines “secret” as other information gained in the professional relationship that the client has requested be held inviolate or the disclosure of which would be embarrassing or likely to be detrimental to a client. DR 4-101 then recites when and when not confidences and secrets may be revealed by a lawyer. Reference to it is virtually mandatory in the practice transfer process.

DR 2-111(B)(2) then provides that, notwithstanding the provisions of DR 4-101, the seller may provide the prospective buyer with information as to the identity of his or her individual clients (the word “individual” not meant to exclude corporate, partnership or other similar entities) except where the seller has reason to believe that such information or the fact of such representation is itself a confidence or secret (which usually it is not). In that instance, if the client has first been advised of the identity of the prospective purchaser and has granted consent to the proposed disclosure, such information may be provided.

DR 2-111(B)(2) also states, again notwithstanding the provisions of DR 4-101, that the selling attorney may provide information concerning the status and general nature of an individual client’s matter, together with information that is available in public court files and information concerning the financial terms of his or her attorney-client relationship and the payment status of the individual client’s account. But there are rather complex qualifications. DR 2-111(B)(3) provides in substance that prior to disclosing any disclosable confidences or secrets, a selling attorney must provide the prospective purchaser with informa-

tion regarding matters involved in the proposed sale that [hopefully] will be sufficient to enable the prospective purchaser to determine whether any conflicts of interest exist. Where sufficient information cannot be disclosed without revealing client confidences or secrets, however, the seller may make such disclosures as are necessary for the prospective purchaser to determine whether any conflicts of interest exist, subject, however, to the provisions of DR 2-111. If the prospective purchaser determines the existence of conflicts of interest prior to reviewing such information, or determines during the course of review that a conflict of interest exists, the prospective purchaser cannot review or continue to review the information unless the seller has obtained the consent of the client in accordance with the provisions of DR 4-101(C)(1). All that language easily lends itself to confusion in any given situation, and we clearly lack sufficient guidance to make it all meaningful.

Since the identity of clients is normally not deemed to be a confidence or secret, it would appear that the revelation of the identity of a seller's clients (presumably from a client list) would normally be among the first items of information to provide a prospective purchaser so that he or she might exclude conflicted clients from the transaction or at least render further consideration as to whether their representation would indeed present an impermissible conflict. Not necessarily so, however, under the Rule. It is particularly when the identity of a client is itself a confidence or secret that the complexity is at its greatest. No one said such transactions would always be simple.

What other identifications might be necessary? Certainly the identities of opposing parties. Some observers believe that the identity of all lawyers representing the parties, as well as of judges and hearing officers, should be disclosed. See *Simon's New York Code of Professional Responsibility Annotated* (West Group) at 338.

The protection of confidences and secrets has always been the core of our professional obligation to our clients, unlike in the accounting profession. That is primarily what our profession's eventual resistance to multidisciplinary practice with accountants was about.

The point to be made about DR 2-111(B)(3), particularly its second sentence, is that this segment of the negotiation process can be very delicate and the seller should take extreme care in disclosing the very kind of revelations that the prospective purchaser may require not only to determine whether a conflict exists, but whether he or she even wishes to pursue the business aspects of the proposed transaction. It clearly would not be difficult to fall into a violative trap that subsequently could result in disciplinary proceedings commenced by a discontented client.

It also is important to note that where confidences and secrets are disclosed to a prospective purchaser, he or she must maintain the same confidentiality of such information as if he or she represents the client. That appears clear enough from the rule and it should not be difficult to adhere to unless, of course, such information will somehow impact upon a prospective purchaser's representation of another client in another unrelated matter. Temptation frequently leads to misconduct.

"Reasonable Restrictions" and Geographic Considerations

DR 2-111(A) provides that a seller and buyer may agree upon reasonable restrictions on the seller's private practice of law notwithstanding any other provision of the Code of Professional Responsibility. Obviously this speaks to the seller's subsequent practice of law and thus to the issue of non-compete agreements. DR 2-111(A) also provides that "[r]etirement" shall include the cessation of the private practice of law in the geographic area, meaning the county and city, and any other county and city contiguous thereto, wherein the practice to be sold has been conducted.

DR 2-108(A) prohibits attorneys from participating in a partnership or being party to an employment agreement with other attorneys that restricts the right of any of them to practice law after the termination of a relationship created by the agreement except as a condition to payment of retirement benefits. DR 2-111(A) overrides that rule with respect to the sale of law practices. The right of clients to select their own lawyers has always been considered paramount to the right of lawyers to participate in non-compete agreements of their own. What is “reasonable” within the context of the sale of a law practice, of course, has never been tested in New York, at least not in published opinions up to this writing.

But DR 2-111(A) does define as reasonable a geographic area that includes the county and city wherein a lawyer practices, together with a county and city contiguous thereto. Thus, for example, a retiring New York City attorney would “reasonably” be restricted from practicing law in all five counties within the city, as well as in the City of Yonkers, and in Westchester and Nassau counties as well. Note in the rule the use of the mandatory third person “shall” as to the stated geographic areas. Whether a contractual restriction beyond the mandated geographic limits would be “reasonable” has not been decided but probably would be fact intensive.

Note also N.Y. State Bar Op. 707 (1998) which opines that a lawyer may not retire from one part of a law practice and continue to practice in another part within the same geographic area. DR 2-111(A) thus is said not to contemplate retirement from one or more areas of practice without retirement from all others within the same geographic area.

What does “. . . in which the practice to be sold has been conducted” mean? Does it mean the city or county of one’s primary office? Does it mean, more likely, any office locale from which one practices? Does it mean any city or county wherein a lawyer regularly or even occasionally has appeared during the course of his or her private practice even though it is not the city or county wherein this office is located? If a Queens County litigator appears regularly throughout Long Island but maintains his or her only office in Queens, can he or she be foreclosed by agreement from practicing in Suffolk County? Would that be a “reasonable” restriction? We do not yet know. If a lawyer maintains offices in several counties throughout New York State, as some do, are the geographic areas wherein those offices are located included within the rule? May a lawyer retire from the practice of law in Westchester County where he or she maintains an office, but not in Albany County where he or she also maintains an office? Such issues have not yet been determined by precedent.

Notification to Clients

When financial evaluations finally have been completed along with other details of the transaction and a basic agreement has been reached for it to be consummated, it is necessary for both participants, jointly and in writing, to notify each of the seller’s clients of the proposed sale. DR 2-111(C). Such notice must include a statement as to the client’s right to retain other counsel or to take possession of his, her or its file, and also as to the fact that the client’s consent to such a file transfer will be presumed if the client, upon such notice, neglects to take action or fails otherwise to object to it within ninety days from the sending of such notice, subject, however, to any court rule or statute mandating express approval by a client or a court. That imposes upon each client the obligation to take an affirmative step to prevent the transfer of his or her file to the purchasing attorney if that is desired. The rule obviously is intended to avoid prevention of the transaction merely by reason of a client’s neglect, inaction or lack of concern in the approval process. And, of course, despite their own neglect, inaction or lack of concern resulting in the transfer of their files to the purchasing attorney, clients may thereafter always terminate the services of the purchasing attorney.

With regard to fees, clients must also be notified in writing, jointly by both the seller and the buyer, that the existing fee arrangement with the selling attorney will be honored, or that proposed fee increases will be imposed. Obviously that is of particular concern to clients in the grant or withholding of consent. It is important to note that the fee charged to a client by the purchaser cannot be increased by reason of the sale unless permitted in the original retainer agreement with the client or otherwise specifically agreed to by the client. DR 2-111(E).

The joint written notice to each of the seller's clients must also include the identity and background of the purchasing attorney, the location of his or her principal office address, his or her bar admission(s), his or her number of years in practice within the jurisdiction, whether the prospective purchaser has ever been disciplined for professional misconduct or convicted of a crime, and whether the prospective purchaser intends to re-sell the practice.

Finally, attorneys should be aware that the rules that for decades proscribed the sale of a law practice revolved primarily upon issues attendant upon improper disclosure of confidences and secrets. The current rule that permits the transfer of law practices is clearly in derogation of the prior philosophy. Accordingly, the current rule should ideally be construed strictly and should be expected to result in disciplinary action should it be violated. All doubts as to the propriety of a proposed transfer, or of any ingredient of it, should reasonably be resolved against the transfer.

Valuation

A fundamental consideration in the entire negotiation process involves the question as to what value may be ascribed to a selling practice. That is an issue requiring outside expertise in most instances. It is not the purpose of this material to describe the various means by which a practice may be appraised. Suffice it to say that the determination may become very complex. The reader is referred to various of the materials listed at the end of this segment.

Conclusion

The rules relating to the transfer of law practices in New York are relatively new and, at this writing, are not yet the subject of judicial interpretation. Nor do we yet have any authoritative statistics as to the extent to which DR 2-111 has been utilized. The rule was intended primarily to place solo practitioners on an equal footing with non-solo practitioners in terms of their ability to obtain monetary value from their years of private practice. It probably is fair to state that most solo practitioners are general practitioners, and that most of them have relatively few institutional clients. Assuming that to be true, one cannot help but wonder what monetary value most solo practices may have where they consist of an ever-changing clientele, and where (unlike non-solo firms wherein a continuing firm name and its continuing professional staff may provide value) the good will aspect of the practice to be sold consists exclusively of the character and professional reputation of the selling attorney who, upon sale, will no longer be an element of the practice. That factor, it would seem, tends to place the solo practitioner on something other than the equal footing that the rule was intended to provide. But for those who can somehow find value to sell, the rule exists to be used. While nothing may be gained from it in many situations, nothing can be lost, and all solo practitioners should at least consider the marketable value of their practices before simply shutting down.

References

New York's Lawyer's Code of Professional Responsibility, DR 2-111 and DRs cited therein, and ECs 2-34, 2-35 and 2-36.

N.Y. State Bar Ethics Op. 707 (1998).

N.Y. State Bar Ethics Op. 699 (1998).

N.Y. City Bar Ethics Op. 1999-04 (1999).

ABA Model Rules of Professional Conduct, Rule 1.17

Edward Poll, *The Business of Buying, Selling, Merging or Closing a Law Practice*, published by the American Bar Association.

Robert L. Ostertag, *Sale of a Law Practice*, GPSOLO (ABA) Vol. 17, No. 1 (Feb. 2000) at 22.