

FBA Ethics and Civility Program: Hypotheticals

Hypo 1:

You are sitting in your law office on a November afternoon, proud to have finally been able to open your own law firm after working for 2 years as an associate at a small law firm which recently closed its door. Your practice at that firm had consisted exclusively of reviewing mortgage files and assisting a litigation partner and paralegal in preparing to file foreclosure lawsuits and then motions for summary judgment. Your phone rings, and it is Sylvia Stone, the mother of a girl from your daughter's 4th grade class. She remembers meeting you at meet the teacher night last week when you were busily handing out your freshly printed cards. She says she and her husband Sly have just agreed to purchase a home from Mr. and Mrs. Jones. Neither one is using a real estate agent so they can save the commissions. She asks you "Can me and Mrs. Jones come to your office to draw up a sales contract?" Before you answer, in your head you are thinking to yourself, Mrs. Jones, Mrs. Jones, Mrs. Jones, why is that name familiar? Not placing the name, you set up an appointment.

Sylvia and Sly Stone and Norah and Davey Jones arrive as scheduled. They explain that their agreement is that the Stones are paying \$300,000 for the house, and closing is to be after the current school year ends, at which time title will be transferred to the Stones. The Jones mention that they are a bit behind on their mortgage and will be ready to move out the day after closing. Both sides want you to draw up the sales contract, mentioning money is tight and they can't afford to have separate lawyers, but that everything is agreed and there will be smooth sailing to get to closing. They have

already agreed on an inspector. No one mentions whether the Joneses are going to bring their mortgage current. You agree to prepare a sales contract and quote a fee of \$3,000 for the entire transaction through closing, but only if both sides sign a letter waiving any conflicts of interest. They agree, and each side writes you a check for \$1,500. The next day, you send each side a conflicts waiver letter you create on your own, along with a draft sales contract. Within 2 weeks, you have signed waivers and a signed sales contract, and a picture of your first 2 checks on your smart phone!

Two months later, Sarah, the foreclosure litigator you used to work for, calls you on your cell. After a couple of minutes of idle how-you-doing chit chat during which she tells you she is still doing foreclosure work but at a different firm, she asks you if you know what happened to a file regarding a foreclosure for Bank of All Capital (“BAC”) against Norah and Davey Jones which she is supposed to handle at her new firm. Ding! A bell goes off. Now you remember the reason Mrs. Jones’ name sounded familiar was that you had reviewed her mortgage file to help prepare a foreclosure lawsuit for BAC. Because you had fallen way behind on your work due to a summer vacation, the Jones’ file was one of about a dozen files you had taken home with you to work on. When you did start on the file you noticed her address would put her in the same school district as your kids; you never got much past the street address before you found out the law firm was closing its doors, at which point you put this and the other files away – somewhere. You don’t mention to Sarah having met Mrs. Jones or the pending sale or your recollection about having had the file, but just say you’ll have to check at home and will call her back. Sarah asks if you would check ASAP, because Mrs. Jones has filed bankruptcy and they need the file so they can have their

bankruptcy department file a claim and do whatever the bankruptcy folks need to do for BAC. Before she hangs up, Sarah nervously says, “That file has all the original loan documents in it and if it got lost we’re toast.”

You are not sure what to do. You have never handled any matters in bankruptcy court, and now Mrs. Jones is your client. So is her buyer, the Stones. When you get home, you run down to the basement and open the box marked “MISC.” that you have not had time to open in the last few months. Sure enough, under several months of unread bar journals, you find 11 files from your former employer, including a file marked, BAC vs. Jones. In it are an original promissory note she appears to have signed in favor of Joyous Mortgage, which has a hand written endorsement “pay to the order of _____”, which blank, then a signature block indicating it was signed by Joyous, but no one filled in the name of the transferee. There is also an original mortgage to Joyous, but nothing indicating if it was ever recorded.

What do you do? What are the ethics issues involved?

Hypo 2:

You have been a partner in Practice, Wah, Chu and Preech for 11 years, having been with the firm for 19 years since graduating from law school, with the last 16 spent primarily as a bankruptcy lawyer. The firm’s partnership agreement provides that 50% of your income as an equity partner is based upon originations, meaning the amount of money your clients pay the firm each year, and 30% is based on productivity, meaning the amount of hours you individually bill that result in money being paid to the firm. The other 20% is based on “touchy feely” intangibles that are decided by the compensation

committee. One of your law partners, Sid, has been a commercial real estate lawyer for 10 years, with all of his experience having been representing purchasers and developers, meaning they are also borrowers from real estate lenders. Since the economy turned sour, new deals have been hard to come by, and loans even harder. Every few weeks at lunch, Sid tells you he has to retrain himself and pick up another skill set, because he can't feed his family with what he takes home based on his share of what he brings in doing loan "amend and extends." While you have always liked Sid, as a new member of the compensation committee, you know his originations and productivity have been down again, and that his intangibles are not scored very highly.

One morning before you get to finish your first cup of coffee, Sid bursts into your office, excited as you have seen him since the Giants won the Superbowl. "Tom. Great news, great news. My biggest client, NuMall Ltd, has to file bankruptcy and they want me to handle it. Can you believe it? NuMall?"

You sip from your coffee, happy for Sid, but knowing what has to come next. "Sid, that's great. I mean for you, not them. So, why don't you sit and let's talk about this." Sid sits, but can barely stay in his seat. "So, you understand that you will need a lot of help on this file, since you really don't know much about bankruptcy. Do you want me to work on it with you?"

"Oh, sure, I mean if you can help guide me through it would be great. I went to 2 bankruptcy seminars last year and you've helped me with bankruptcy issues on work outs before. I thought maybe I could borrow your paralegal to fill out the forms and then you could come to hearings with me since I've never done a hearing. I've been in court

and watched you, and think I learned a lot. But I figured otherwise I would handle the file.” You take 2 more sips from your coffee before you respond.

“Sid, uhm, look. Bankruptcy is pretty complicated stuff, and chapter 11 is really complicated stuff. Any mistake could hurt your client an awful lot.”

“I know, Tom. That’s why I need you to help guide me through it. But they were very clear that they want me to do the bulk of the work. They have a lot of confidence in me, and I can’t tell them I’m not competent to handle the file or they’ll take it somewhere else. They want me doing the negotiating, going to hearings, talking to the judge, drafting the agreements. They plan to be at every hearing and they always scrutinize every document I draft for them. They’ll know if someone else handles any important part.” Sid stands up. “Tom, I need this case or my numbers for the year will end up with me getting my draw cut again. You know that, you’re on the compensation committee. I just can’t afford another pay cut.”

What do you tell Sid? What are the ethics issues involved?

Hypo 3

Settlement talks have just broken down on trying to resolve a potential fraudulent transfer lawsuit the chapter 11 trustee has threatened to bring against your clients, May Flower and James Town, two of the richest residents of East Kwagh, Long Island, a ritzy enclave even by The Hamptons standards. The dispute arose over a land acquisition May and James made from their former friend and bridge partner, Langdon Simmons, just over a year ago, to help Langdon with some financial problems he was having.

May, James and Langdon played bridge together for several years. One day over the July 4th holiday in 2009, after a rather raucous match, Langdon confided in May and James that his Wall Street firm, a self described strategic debt acquirer, had a miserable year in 2008 and that 2009 was not looking well at all. Langdon felt exposed because he had married Missy, his second wife, at the beginning of 2007 (which everyone in East Kwagh knew), and that, under his divorce agreement of late 2006, he had to pay his first wife, Matilda, \$4,000,000 by the end of 2009, or she would get 100% ownership of their house and the Park Avenue apartment (which everyone in East Kwagh also knew). This payment was in addition to indemnifying her against federal and tax liabilities he had been contesting for about 2 years. Langdon had been confident in 2006 when he made his divorce settlement that the development property he had acquired an interest in back in 2002 far on the east end of Long Island would have been subdivided and well into the development stages by early 2009, and would have generated more than enough money to pay Matilda and the taxing authorities; however, delays in getting permission from the zoning board to begin the project and the proposed project financing falling through in 2008 left him in quite a predicament. He told May and James that he had offered Matilda \$200,000 to give him a two-year extension of his payment deadline, but she said not a chance. He then went to his partners in the east end project to see if they would loan him the \$4,000,000 secured by his 1/3rd interest in the project, but the only offer he received was to cash him out for \$2,000,000. "Can you believe that? What snakes. My interest is easily worth 5 times that and they know it." After a few minutes of silence, Langdon said, "Look. My interest is worth over \$10,000,000. But I need \$4,000,000 in the next 90 days or I lose my

share of the house and apartment and that's a loss of about \$7,000,000. So, I'd like to know if you would buy 1/2 of my interest in the project for \$4,000,000; you get a \$5,000,000 interest for \$4,000,000, I get to save \$3,000,000 by not losing my house and apartment, not to mention all the grief I avoid getting from Missy if we have to move and find a new escape place in the city. All in all, it's well worth it to me. What do you think?" They say they will talk to their spouses, lawyers and financial advisors and get back to him within 2 weeks.

Before July is over, a deal is unenthusiastically agreed to by Langdon under which Langdon gets \$4,500,000 for 60% of his interest in the east end project, with closing to occur within 45 days; the deal closes two weeks before Langdon's divorce payment is due to his ex-wife; however, because of problems and investigations at his investment firm which had cropped up during the summer, Langdon does not use the money to pay Matilda; instead, he uses the bulk of it to resolve potential lawsuits by the SEC and the New York State Attorney General. The day before his divorce payment is due to Matilda, he files chapter 11 bankruptcy.

After a dispute-filled year in bankruptcy fighting with Matilda, his employer, and his business partners, the court appointed a chapter 11 trustee. The trustee then managed to negotiate a settlement with Matilda for her to receive \$5,000,000 for her interest in the house and apartment, which he would finance with a buy out of Langdon's interest in the east end project; he had negotiated a deal for Langdon's partners in that venture to pay \$11,000,000, conditioned on the trustee selling them the entire interest Langdon originally had, which includes the 60% he sold May and James. That deal would enable him to settle with the state and federal taxing authorities, clear

the path for him to sell the house and apartment, generate a substantial dividend for unsecured creditors, and, potentially, create a healthy distribution to Langdon.

The trustee was very forthright in his game plan. He thought it fair for May and James to make a healthy profit on their distressed purchase, but could not justify them keeping all of the upside from his sale to Langdon's former business partners. His last, take it or leave it offer to pay May and James \$5,300,000 for their share of the \$11,000,000 sales price, generating for them a profit of \$800,000 in less than 2 years, has been rejected, resulting in the threat to file the fraudulent transfer suit.

Your meeting with May and James ends this way: "Look. We are not afraid of litigation. We are in the right here. We helped Langdon out when he needed us, and it's not our fault he didn't pay Matilda with our money. Now she seems to think we conspired with Langdon to not pay her, and our relationship with her was strained enough before all of this happened. Plus, there is no reason for us to let that trustee keep our profit, and certainly not to help Langdon with his tax problems or, even worse, to put any of our profits in his pocket. Under an \$11,000,000 sale, we should get \$6,600,000, not \$5,300,000. We agreed to put \$300,000 of our profit on the table to settle, figuring it would cost us about that much to defend a lawsuit. The trustee said no, so it's clear he wants a war on his hands. So, if you want to handle the defense of the lawsuit, here are our conditions – there will be no more talk of settlement; there will be no agreements of any kind on any thing. That means if he wants to take our depositions, he needs a court order. If he wants records from us, he needs a court order. If he wants anything, you are to put him and his lawyers to the maximum effort humanly possible. Time is on our side. In fact, we have heard rumors that Langdon's

east end partners have a buyer waiting in the wings to buy the whole project for \$50,000,000 to \$55,000,000, but they won't wait forever. You can't breathe a word of that to the trustee, and we will deny knowing anything about it if asked; plus we doubt it will come up -- the trustee would be an idiot to sell out now at a \$33,000,000 value if he knew there was a buyer in the wings for far more than that. So, you see, delay works to our advantage. Plus, we just didn't do anything wrong. So, if you want to handle this case, we don't care what you do so long as you make it as painful and expensive for the trustee as possible, and drag it out as long as possible. We are prepared to pay you \$300,000 right now to handle the case. Do we have a deal? And, if you're not comfortable with our requirements, can you refer us to someone who is?"

What do you do? What are the ethics and civility issues involved?

Hypo 4:

You have recently filed a chapter 13 case for a nice young couple from Nassau County, Tim and Tia Bowe (for the Brooklyn program, read that as Queens). Based on some bad advice they received, they had filed a pro se chapter 13 case, which was dismissed about 2 months before they met you. They are very nervous about whether they will be able to keep their house and cars, believing that they had always been careful to not overextend themselves financially, but the economic downturn made them victims of the bad economy. They file their schedules and other required financial information on time. You get the stay extended for the duration of their case. They dutifully attend their 341 meeting, and begin their plan payments on time. You work out deals for them to keep the cars and pay those arrears through the plan, and to pay the

mortgage arrears over a workable period of time while they apply for a loan modification. You smell victory on this file.

Two days before their scheduled confirmation hearing, Tim shows up unexpectedly at your office. Your secretary tells you he is very insistent that he has to talk with you. You tidy your desk up a bit, and have him brought in. “Tim, what seems to be the problem?”

“Look, Mr. Mason. I hate to barge in on you like this, but, well, here’s the thing. I lost my job yesterday. My boss called me in and told me he was really sorry but he had to let me go. So, there’s no way we can afford to keep the house and make all our plan payments anymore. What should we do?”

You lean back in your chair, assessing the situation. “Tim, where are you guys on your loan mod?”

“We turned all the paperwork in about 3 or 4 weeks ago. But without my job we can’t even make the reduced payments.”

“Alright. I’ll contact the trustee’s office and let them know we can’t go forward with confirmation. What are your job prospects?”

“In this economy? Hard to tell. I mean if construction picks up, probably pretty good. But right now? I just really don’t know. But I already started looking and may have some leads. I just don’t know, though.”

As soon as Tim leaves, you place a call to the chapter 13 trustee, vaguely describe the situation and ask for an adjournment, hopeful Tim will find a new job by the next

confirmation hearing. A month goes by, and Tim has no new job. You call the bank's lawyer and the trustee and tell them Tim has lost his job and can't make mortgage or plan payments, but you are hopeful he will find something, so you want to keep the 13 open. They agree, but the bank's lawyer says they will be moving for stay relief since the loan mod is now moot, and they already had a foreclosure judgment before the pro se case was filed. The trustee says unless he has a new job within a month they will move to dismiss.

Another month and no new job. The bank moves for stay relief and the trustee moves to dismiss. The hearings are held together. You attend both and tell the Judge your clients just have no current ability to make payments, so you have no good faith basis to oppose either motion. The stay is lifted and the case is dismissed.

Two months later, Tim appears in your office, but this time after having called ahead. "Mr. Mason, I have great news. I just landed a new job, and I start next Monday."

"Terrific, Tim. That's just great."

"Yeah, but our house is supposed to be sold at foreclosure on Monday also. Can you help us?" You do not hide your surprise, since your firm is not handling the foreclosure case for Tim and Tia.

"Tim, it's 4:00 o'clock on Friday. Why didn't you tell me before?"

"I didn't know until about 2 hours ago myself."

"I mean about the foreclosure. I didn't know it was this soon."

“Well, without a job it really didn’t matter. But, look; now I have a job. It’s not as much money as I made before, but it’s enough to pay the reduced payments if we get our loan modification. Plus Tia is making some extra money tutoring. Can you help us? We really don’t want to lose our house.” You take a deep breath. You check the file intake information on the computer, and realize they are a few weeks shy of being more than a year since the dismissal of their pro se case, so filing a new case is not an option.

“I’ll do what I can, Tim. But, I have to be honest with you. It’s a Hail Mary pass. Your time is really running out to get anything done.” You lead him to your secretary’s desk for them to work on an affidavit to support a motion for emergency reinstatement of the case and/or imposition of the stay. Back in your office, you try to call the bank’s lawyer. Out of the office at a meeting, not expected back. Since it is after 4:00 pm, you assume that is code for went home early. And, you are told, it is office policy to not give out cell numbers. You leave a detailed message to please call you ASAP about the Bowe case, and start typing a letter to fax to the bank’s lawyer about the need for an emergency hearing. At the same time, you try to reach the chapter 13 trustee’s office. At 4:15 pm, the answering machine picks up. By 4:30 pm, your fax has gone out to the bank’s lawyer and trustee, alerting them an emergency has arisen and you are going to seek an expedited hearing on Monday morning in bankruptcy court to stop the foreclosure; you give your office and cell numbers in the fax. Then you start typing the emergency motion, giving as much detail as you can, recognizing that you cannot allege the Bowe’s have the funds to cure the plan and mortgage arrearages. You consult the Judge’s procedures posted on the court’s website regarding how to request an emergency

hearing. You help your secretary finalize Tim's affidavit, and finish the pleadings so they are filed by 6:00 pm as well as emailed and faxed to the bank and the trustee. You then contact the Judge's courtroom deputy in accordance with the Judge's posted procedures, and hope for the best.

First thing Monday morning, you check your emails but find nothing from the court, the bank's lawyer or the trustee. Same results with your office and cell voice mails. You send another email and call the Judge's courtroom deputy at 8:15 am, and leave a message. You head out to court and go the Judge's courtroom, finding it locked. Docket is not until 9:30, and it is 9:15, so you go into the hallway and buzz at the security intercom. When asked to state your business, you explain you have an emergency situation and really need to be heard by the Judge ASAP. A law clerk's voice says, "Just go into the courtroom and someone will speak with you in a few minutes." You comply. In a few minutes the courtroom deputy unlocks the doors. She tells you she has advised the Judge of the matter and you will be told what will happen when he/she takes the bench. You take a seat at counsel table.

At 9:35, the Judge comes in for calendar. When told to be seated, you instead go to the lectern. Although the Judge does not appear happy you have jumped the line, the Judge asks you why this is an emergency, and why do your clients want this case reinstated. "Circumstances have changed, Judge, and my clients require the protection of this Court on an emergency basis."

"Yes, that's what your papers say, Mr. Mason. But this is all a bit vague, don't you think?"

“A bit, yes, your honor. But if you don’t reinstate this case right now, my clients will lose their house in about 30 minutes.”

“Have you spoken to the bank’s attorney or the chapter 13 trustee?”

“I tried, Judge. I faxed them these pleadings Friday night.”

“Friday night?”

“Uhm, well, yes, but I called and tried to reach both of them before that, and no one was in.”

“How much before?” You can feel yourself sweating.

“About 4:30.”

“4:30 Friday night?”

“Yes. I tried to reach them right after my client came to me and told me of these material changes in circumstances.”

“Oh, I see. So your client waited until the last minute and made this into an emergency fire drill for all of us?” Now you feel yourself getting angry, thinking the Judge hasn’t even read your papers.

“With all due respect, in about 30 minutes this is all going to be moot. If the bank forecloses, my clients will be out on the street and won’t have a chance to keep their house. All I ask is that Your Honor reopen their case and let them have a chance to reorganize.” Before you even finish the sentence, you know it is too late; the words came out, and your tone sounded indignant.

The Judge remains motionless and expressionless for several long, painful seconds. “I see. Well, Mr. Mason, here’s what I will do. I have 73 other hearings on this morning. Go out in the hall and try to get the bank’s lawyer on the phone; if you can, then come in with them on your speaker and I’ll take it up then, and the Court will attempt to patch the trustee in. But I am not going to deprive the bank and the trustee of their due process rights just because your clients waited until the last second and made this an emergency for my court. Oh, and by the way, when you file for an emergency hearing, please don’t contact my courtroom deputy multiple times to find out if we have looked at your motion. We have thousands of cases and hundreds of motions to attend to, and hundreds of orders to process, each as important as yours. Contacting us on multiple occasions just distracts us from the other important work we have to do. Once is plenty; we will always get back to you or whoever needs our attention. But don’t wait until the last second and expect us to drop everything for you.” The Judge turns to the deputy, who calls the next case. You slink out of the court room, and start trying to reach the bank’s lawyer.

What do you do? What are the ethics and civility issues involved?

Hypo 5:

You represent John Smith, a successful real estate developer with many projects in Brooklyn and Queens. His brother, Fred, did not do so well, and had to file for chapter 7 bankruptcy. John, who is a long-standing client and friend, is sitting in your office, explaining to you that he, his wife and several of his affiliated companies have been named as defendants in an adversary proceeding brought by Fred’s chapter 7

trustee. Fred, who now works for one of John's companies, was a high-flying real estate developer in his own right, who got involved in a number of risky co-op and condo conversion projects in the mid-2000's. When the market began to soften in 2007, Fred struggled to hang on to his projects, which were at various stages on the road to completion and sale. After the market crashed in the last quarter of 2008, Fred gave up, and filed chapter 7.

The chapter 7 trustee's adversary proceeding against John and his companies arises out of a transaction between John and Fred in May 2007. John explains to you that, at that time, Fred was in need of cash to finish his pet project, a waterfront condo development in trendy Williamsburg. Desperate to raise a crucial \$1,000,000, Fred asked John to buy his beachfront weekend house in Atlantic Beach, at that time worth \$2,000,000, for \$1,100,000. Motivated by brotherly loyalty, and seeing a good deal, John agreed. Although Fred lost his investment in the Williamsburg condo deal, including the \$1,000,000, in the real estate downturn and his resulting bankruptcy, the beach house arrangement has worked out well; John's and Fred's families are very close (their kids are about the same age), and the two families share the spacious vacation home. Though John does not tell you this, you suspect there is a tacit understanding that if Fred gets back on his feet, he will buy the beach house back from John at or about the amount he paid for it. Although in an excellent location, the house's value has declined, and John thinks it is now worth about \$1,600,000.

You agree to take on this case for John. He gives you the complaint, which he and his wife received by mail a few weeks ago at the beach house, and which seeks \$2,000,000 plus attorneys' fees. You see that an answer is due tomorrow. John also

gives you orders signed by the bankruptcy judge directing that John, his wife, his aged mother and teenage daughter appear for 2004 examinations in two weeks, with a long list of documents to be produced the week before, which also arrived by mail at the beach house.

After John leaves your office, you call the trustee's counsel to get an extension of time to answer the complaint, to postpone the depositions and document production, and to find out, if you can, what it would take to settle the case. The partner is not available to speak with you, and you are transferred to an associate, who tells you she has no authority to give any extension of any deadline, but that she will discuss and get back to you. A day goes by with no return call. You call the associate again, and then the partner, but can't reach either of them. The next morning, you get an email from the associate saying the trustee has said that there will be no extensions of time in this case. You quickly prepare and file a bare-bones answer, one day late. You call John and ask him to get together the documents that he has that would be responsive to the trustee's document requests. John tells you that he doesn't have much relating to the transaction, and that what little he has would be with his accountant, who is very busy this time of year. You tell him to do the best he can.

You then fire off a letter to the trustee and his counsel requesting an extension of time to respond to the document request and a postponement of John's deposition. You also ask the trustee to withdraw his request for the depositions of John's wife, mother and teenage daughter, which you believe are intended to harass and intimidate. You receive no response.

The next week, two days after the response is due to the document request, is the first scheduled pre-trial conference in the adversary proceeding. Early in the morning on the day before the conference, you hand deliver to the trustee the few documents that John's accountant has been able to gather together. You prepare to raise all of these issues with the judge at the conference.

On the day of the conference, you go to court at the appointed time. You have never appeared before this judge before, and you see that the trustee and his counsel are already at counsel table, having had other matters on before the judge that morning. When your matter is called, you go to counsel table, ready to raise your concerns about what you see as the trustee's and his counsel's unreasonable litigation tactics. Before you can open your mouth, the trustee launches into an attack on you and your client—for filing your answer late, not producing all of the documents called for and sending over a minimal production just yesterday; the trustee argues vehemently that you and your clients are generally trying to evade discovery on what he considers to be an open and shut intentional fraudulent conveyance case, which fraud, he says, is bolstered by the fact that the debtor, John's brother, works for the defendants, and that the debtor's family has had free use of the beach house since the day of the supposed sale. You are not sure, but based on the judge's facial expression, you think the judge might be buying this, and pre-judging the whole case before a single witness has even been called.

What do you do? What are the ethics and civility issues involved?