IN THE SUPREME COURT OF OHIO

Core Funding Group, LLC	:	Case No. 06-927
Appellee,	:	
v.	:	
Diana McDonald, etc., et al.	:	On Appeal from the Lucas County Court of Appeals, Sixth Appellate District
Appellants.	:	

REPLY BRIEF OF APPELLANTS, WILLIE GARY AND GARY, WILLIAMS, PARENTI, FINNEY, LEWIS, MCMANUS & WATSON

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REPLY ARGUMENT IN SUPPORT OF PROPOSITIONS OF LAW

<u>Proposition of Law Number I:</u> An attorney who collects a fee which is partially owed to co-counsel under a contingency fee agreement is not an account debtor for purposes of imposing liability under secured transactions law.

Whether attorneys should be treated in the same manner as any other debtor is not the issue in this case. The issue in this case is whether an attorney who holds a fee collected under a co-counsel fee agreement in a tort claim is an account debtor for purposes of Article 9. The answer is no. The practice of securing loans with tort claims has always been outside of the mainstream custom. As Defendants-appellants, Willie Gary and his law firm, Gary, Williams, Parenti, Finney, Lewis, McManus & Watson (collectively referred to as "Gary"), noted in its merit brief, "[t]he drafters of Article 9 excluded tort claims from its purview because tort claims 'do not customarily serve as commercial collateral'." *Bluxome Street Associates v. Fireman's Fund Insurance Company*, 206 Cal. App. 3d 1149, 1156; 8 U.C.C. Rep. Serv. 2d (Callaghan) 822, citing UCC official comments.

Article 9 is particularly ill-suited for an attempt to obligate an attorney debtor's co-counsel on a tort claim. The basic problem in the attempt of Plaintiff-appellee, Core Funding Group, LLC ("Core"), to use Article 9 is that Core confounds the co-counsel fee agreement with an account receivable that falls under the purview of secured transactions law. Core forgot that the obligor under the fee agreement is the client. Gary did not owe a debt to Diana McDonald ("McDonald") on a previous liability. McDonald is not Gary's creditor. McDonald's specific pledge of accounts receivable to secure her obligations to Core identifies the contingent attorney fees owed by the clients in the tort actions. (See, Security Agreement, Appellant's Supplement to the Merit Brief, at p. 5.) The money received by Gary included the fees owed by the client to both attorneys. When Gary forwarded McDonald's fee to her it was not satisfying an obligation from its own resources for services rendered on its behalf. Instead, Gary was discharging its fiduciary obligation owed to McDonald as an attorney in a co-counsel fee agreement to hold her portion of the collected fees in trust.

Core's chief contention is that McDonald's accounts receivables did not consist of the attorney fees owed in the tort action but rather the obligation of Gary to turn over McDonald's share of any money which it collected. However, Core had no answer to the controlling rules cited by Gary in its merit brief. Those rules provide: "[A]n agreement to divide fees establishes a trust agreement between the attorneys respecting the fees collected, in which both are entitled to share." *Gugle v. Loeser* (1944), 143 Ohio State 362, 368; and, "Payments due or made to a person who must hold or apply payments in a fiduciary or representative capacity are not 'accounts receivable' of the recipient of the payments." *Anderson on the Uniform Commercial Code*, Third Edition, Vol. 8A, §9-106:15.

Since the above-stated rules help to determine this issue, they are worth a more detailed examination. In *Gugle*, this Court held at paragraph two of the syllabus that: "Ordinarily, an agreement between two attorneys at law, representing the same interests, for a division of the fees received is neither unethical nor illegal, and where both attorneys have rendered services and one collects the entire fee, he is liable to the other in accordance with the terms of the agreement."

In explaining the basis for its holding, this Court quoted from 7 Corpus Juris Secundum, 1039, 1040, "*Attorney and Client,*" §174:

> "The terms of the contract determine the rights to claim a division of the fees, and when the right was to accrue on the happening of a certain event, which happened, counsel is entitled to his share[.] * * *
>
> "Such an agreement to divide fees establishes a trust agreement between the attorneys

respecting the fees collected, in which both are entitled to share, * * * and an attorney who repudiates his obligation to divide the fees may be subject to action and constrained to account. It is immaterial that the order fixing the fee allowed it as for services rendered solely by one attorney, where the other was not a party to the arrangement under which the fee was allowed or collected."

Gugle, at 367-368.

The above-stated rules settle the question presented in this case. By entering into a co-counsel agreement Gary and McDonald had an identity of interests in the collection of the fee. Gary never asserted an interest in the fee owed to McDonald while he held the funds in trust, and it was undisputed that the money belonged to McDonald from the time it was paid by the client until it was delivered to her by Gary. Thus, Gary was not in McDonald's debt either at the time that Core served Gary with notice of its first loan to McDonald [1] or after he collected the fee.

Core's response to these rules was limited to questioning the precedential value of *Gugle* in light of the adoption of Disciplinary Rules regarding fee-splitting. That question was firmly resolved by the Opinion of this Court in *King v. Housel* (1990), 52 Ohio St.3d 228. In *King*, the Court expressly applied the holding in paragraph two of *Gugle* to thwart a defense raised under the Disciplinary Rules pertaining to the division of fees among lawyers, DR2-107. Accordingly, it must be concluded that the Supreme Court's adoption of the Disciplinary Rules did not extinguish the precedential value of that prior law.

In summary, Gary is not asking the Court to change Article 9. This review is necessary because of the manner in which Core has sought to employ the provisions of that Article which

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Although Gary never acknowledged even receiving a notice of Core's second loan to McDonald, the lower appellate court found Gary to be also liable for the full amount of that loan simply because Core alleged that it had notified Gary that McDonald had borrowed more money.

obligate account debtors for creditor's obligations. A debtor has an obligation to pay for services rendered to it. McDonald did not provide any services to Gary. Gary did not owe any of its own money to McDonald. As attorneys in a co-counsel fee agreement, McDonald and Gary owed contractual and professional duties to each other. They agreed to jointly represent their client and to share any fee earned from that representation. Their services are rendered to their client, not each other, and neither one agreed to pay the other its own money for any services. In order to recover under Article 9, Core needed to show that Gary owed its own money to McDonald for something she provided to it.

Furthermore, the co-counsel agreement between McDonald and Gary does not obligate Gary to collect and distribute the client's fees. Under the common law of Ohio governing attorneys in co-counsel agreements, whoever receives the total fee holds co-counsel's portion of it in trust until it is distributed. The portion of the client's fee owed to McDonald which came into Gary's possession was not owned by Gary. It belonged to McDonald. McDonald had the right and claim to that money while it was held by Gary. If Core wished to utilize the provisions of the secured transactions law contained in former O.R.C. 1309.37(C), then it needed to provide notice of McDonald's assignment of her fee to the person who was obligated for payment of the fee under the contingency fee agreement, i.e., the client. Core can not pursue McDonald's co-counsel for her debt just because the circumstances of the fee payment made Gary a holder of McDonald's portion of the fee under a constructive trust. Gary's performance of his professional duty does not make him an account debtor subject to the liabilities imposed under Article 9. Accordingly, Core's attempt to use secured transaction law to go after its debtor's co-counsel is ill-founded.

<u>Proposition of Law Number II:</u> An agreement between co-counsel to share fees earned under a contingent fee agreement is expressly excluded from the scope of secured transactions law.

Even if Gary could be treated as an account debtor, then the transaction between Gary and McDonald still does not fall within the scope of secured transactions law. Article 9 expressly excludes assignments of liens for services and transfers of any claim arising out of tort. See, former O.R.C. §1309.04(B) and (J). The Official Commentary to the 2000 Article of the UCC expressly emphasized that although Article 9 now recognizes commercial tort claims, "this Article continues to exclude tort claims for bodily injury and other non-business tort claims of a natural person." (Official Comment following O.R.C. §1309.101, comment 4a.)

Core concedes that the attorney lien for services on the underlying tort obligation is not subject to Article 9, however, it argues that any money paid in satisfaction of that obligation can be assigned under Article 9. Thus, Core's argument on the exclusion issue turns the focus in this matter back to whether Gary becomes a debtor on McDonald's accounts receivable by virtue of the co-counsel fee agreement. Core's reasoning becomes so convoluted that it concludes its argument under Proposition II by asserting that McDonald's sale and assignment to Core of the fee owed to her from the Valujet tort claim was not a transfer of a lien for services or any part of the proceeds from a tort claim. Instead, Core awkwardly contends that McDonald was just assigning her right to Gary's distribution of her portion of any fee which it collected. (Core's Merit Brief, at p. 14.)

In making that argument, Core is obviously trying to get around Article 9's limitation on an attorney debtor's assignment of an accounts receivable owed by a tort client. However, Core never explains how the client's payment of the contingent fee through Gary's constructive trust transformed the co-counsel agreement into an assignable interest against Gary under Article 9. There is no evidence that the parties even contemplated that the circumstances of the payment of the client's fee from the Valujet settlement would route McDonald's portion through Gary. Even though Core specifically identified an account receivable from the fees owed by the tort client as the security for its loan to McDonald, Core now insists that the assignment pertains to the obligation of co-counsel under the fee agreement. Thus, since Article 9 prohibits the assignment of contingent fees paid from the recovery of a tort client, Core simply declares that Gary is the obligated account debtor. As previously discussed, however, the distribution of the fee by Gary represents property of the client which is paid to McDonald from the tort recovery for services rendered. It is not a separate debt owed by Gary on its own account. Therefore, routing the client's fee through an attorney intermediary does not escape Article 9's prohibition against assignments of any proceeds from a tort claim.

REPLY TO CORE'S STATEMENT REGARDING PUBLIC POLICY

Core set forth its global view on these matters at the end of its arguments on the propositions of law. Core sees itself within the mainstream of the lending and financing industry which provides business capital to attorneys secured by accounts receivable. Core obliquely refers to Gary's descriptions of its business practices as "irrelevant information" and makes pointed references to specific law firms which have engaged in traditional loan transactions. Core warns that the adoption of Appellants' propositions of law will cause great harm and disruption in this industry.

Core's warning is misplaced. Core's own web site provides a revealing picture of its position in the industry with its promise of "CASH NOW" and disquieting offer to pay attorneys a "referral fee" for steering their personal injury clients to Core to cash out their structured settlements. (See Reply Brief Appendix, at pages 1 and 2.) Dress it up how you will, but shorn of its adornments Core's business model looks like this - Core finds a lawyer who has managed to sign up a client with a large tort claim under a contingent fee contract and is willing to pay an exorbitant interest rate (typically 24% or better) to borrow money for a short term. After finding a lawyer to borrow money from it, Core's chief problem then becomes getting the lawyer to pay back the money - hence its eagerness to use the UCC to force third parties to take responsibility for the lawyer's payment or be held liable themselves.

Another central difference between the mainstream financing engaged in by law firms where there is a loan or line of credit secured by the assets of the firm, including accounts receivables, and the type of lending business operated by Core is that Core's transactions involve the outright sale of the contingent fee expected from an expressly identified tort case. (See, Offer to Purchase/Purchase Contract, Appellant's Supplement to the Merit Brief, at p. 13.)

This is where Core's business model falters. Whether Core is in the mainstream of the traditional financial industry or not, its attempt to use the UCC to enforce the repayment of its loans secured by specific tort actions is improper. McDonald assigned the right to funds due to her for attorney services rendered to a client in a tort case. Since Core knows that it cannot make the tort client an account debtor under Article 9, it claims that it is merely taking an assignment of McDonald's right to a distribution of the fee from her co-counsel. Core's practice is violative of both the spirit and the actual terms of Article 9. If a debtor cannot assign an account receivable when the proceeds derive from payment of a tort claim, then McDonald certainly cannot assign an interest in a portion of those funds just because co-counsel collected and held the money for her in trust.

Finally, Core has also complained that it is inappropriate for this Court to issue a ruling governing lawyers from Georgia and Florida. In making that argument, Core overlooks that it initiated this action in an Ohio court and that the contracts it drafted provide that Ohio shall provide the governing law and venue for any disputes arising under the contract. (See, Offer to Purchase/Purchase Contract, Appellant's Supplement to the Merit Brief, at p. 11.) Only Core knows how many of these transactions have taken place across the country, with each and every one carrying with it the potential to come back to Ohio in the form of litigation. For that reason alone, the legal and financing communities would welcome a ruling on the validity of Core's application of Article 9. Most importantly, however, this case provides the Court with an opportunity to disallow attempts between creditors and debtors to improperly utilize the UCC to assign interests in a bodily injury tort claim.

CONCLUSION

Appellants, by and through undersigned counsel, respectfully request this Court's adoption of the proposed propositions of law for the reasons stated above.

Respectfully submitted,

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PROOF OF SERVICE

I certify that a true copy of this Reply Brief was sent by ordinary U.S. Mail to counsel for appellees, Jack J. Brady and Patricia J. Kleeberger, 4052 Holland-Sylvania Road, Toledo, Ohio 43623, and Jeffrey W. Morris, One Dayton Centre, Suite 1600, One South Main Street, Dayton, Ohio 45402, and pro se defendants, Diana McDonald, 2633 Winzley Place, Suite C, Duluth, Georgia 30097, and Diana McDonald, P.C., 2800 Peachtree Industrial Blvd., Suite C, Duluth, Georgia 30097, on November 16th, 2006.

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