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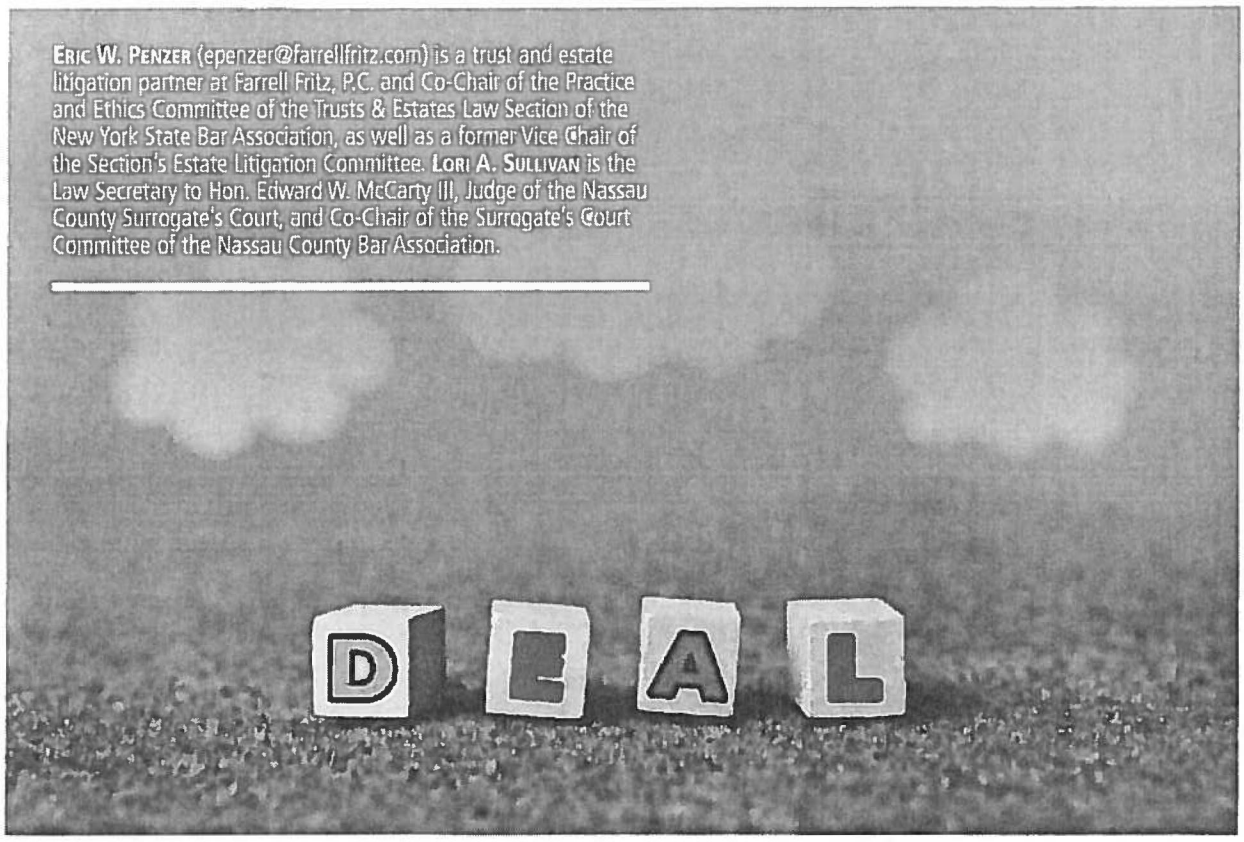

Enforceability of a "Personal Guaranty" Clause

Attorney Fee Agreements in the Surrogate's Courts

By Eric W. Penzer and Lori A. Sullivan

A potential client is the nominated executor under the will of his deceased friend. He would like you to represent him in probating the decedent's purported will. He explains to you that a will contest is likely, as the will treats the decedent's children unequally. He further advises you that the family is very litigious and, specifically, he is concerned that the decedent's children might assert claims against him personally concerning his administration of the estate. Accordingly, the potential client wants the best representation, not only to ensure that his friend's testamentary wishes are carried out, but also to protect himself from liability.

You explain to the client that, as the fiduciary, he will be entitled to pay your legal fees from the estate "on account." Ultimately, however, it will be up to the Surrogate to fix the amount of legal fees payable from the estate, and the Surrogate is not required to honor your retainer letter. You present the client with a retainer letter providing that if the Surrogate fixes the legal fee payable from the estate in an amount lower than the fee contractually agreed upon, the client will be personally responsible, in his individual capacity, for the difference. The client signs the retainer, agreeing to be bound by the "personal guaranty" clause. The question, however, is whether the personal guaranty is enforceable.

The current debate over these types of personal guaranty clauses reflects the inherent tension between a Surrogate's broad discretion in approving legal fees to be paid from an estate and a fiduciary's right to enter into a fee agreement with counsel in his or her individual capacity. In theory, such personal guaranty clauses should not be subject to the same judicial review applicable to agreements concerning fees payable from an estate.[1] These clauses implicate the "valued right" of a party to be rep-

resented by counsel of his or her choice[2] because, absent an enforceable personal guaranty, attorneys, aware that their fees might be disallowed in whole or in part, might well decide not to undertake representation of fiduciaries in Surrogate's Court proceedings.

Those who argue against the enforceability of personal guaranty clauses contend that the Surrogate's award represents the "reasonable" fee for counsel's services. Thus, to enforce a provision allowing counsel to receive a fee over and above that fixed by the Surrogate would, essentially, permit counsel to receive an "unreasonable" fee for the services provided.

On the other hand, proponents of these types of clauses, in addition to asserting the personal right to contract, argue that the Surrogate's "reasonableness" determination is based upon various factors, including the size of the estate, that are immaterial, or at least less significant, when the fiduciary is paying the fee personally. Moreover, the fiduciary's potential for personal liability weighs in favor of the enforceability of personal guaranty clauses. In an estate or trust accounting, damages can be awarded against a fiduciary individually, in the form of a surcharge, if an objectant establishes that the fiduciary was negligent or caused the estate to suffer a loss. It is hardly surprising, therefore, that a fiduciary desiring representation by counsel of his or her own choosing might elect to personally guarantee the payment of that professional's fee.[3]

The Surrogate's Discretion in Fixing Legal Fees

The debate regarding the enforceability of personal guaranty clauses must begin with an analysis of N.Y. Surrogate's Court Procedure Act 2110 (SCPA) and a Surrogate's broad discretion in fixing fees. Section 2110(1) provides:

> At any time during the administration of an estate and irrespective of the pendency of a particular proceeding, the court is authorized to fix and determine the compensation of an attorney for services rendered to a fiduciary or to a devisee, legatee, distributee or any person interested or of an attorney who has rendered legal services in connection with the performance of his duties as a fiduciary or in proceedings to compel the delivery of papers or funds in the hands of an attorney.

The Surrogate bears the ultimate responsibility for approving legal fees that are charged to an estate and has broad discretion in determining what constitutes reasonable compensation for legal services rendered.[4] This discretion is grounded in the proposition that the Surrogate is in the best position to assess and consider the necessary factors in determining compensation. In evaluating the reasonableness of compensation, the court may consider a number of nonexclusive factors, often referred to as the *Freeman-Potts* factors after the seminal cases of *In re Freeman*[5] and *In re Potts*.[6] These factors include: the time spent;[7] the complexity of the questions involved;[8] the nature of the services provided;[9] the amount of litigation required;[10] the amounts involved and the benefit resulting from the execution of such services;[11] the lawyer's experience and reputation;[12] and the customary fee charged by the Bar for similar services.[13]

This discretion in fixing fees is so broad that the Surrogate's Court may inquire into the reasonableness of attorney fees even absent an objection – that is, even if the executor and beneficiaries consent to the legal fees charged.[14] In addition, this is not subject to arbitration. Part 137 of the Rules of the Chief Administrator[15] provides for the arbitration and mediation of certain fee disputes between attorneys and clients. However, excepted from Part 137 are fees awarded by a court order. Thus, if the Surrogate's Court issues an order determining the attorney's fee, the client cannot dispute that fee in mediation or arbitration. On the other hand, if the fee is arbitrated, the Surrogate could nevertheless inquire into the reasonableness of the fee, which it could do, presumably, in connection with a motion to confirm or vacate the arbitrator's award.

Talbot

The court's discretion extends to contractually agreed-upon contingency fee agreements. In *In re Talbot*,[16] the Second Department affirmed the Surrogate's decree approving counsel's fees. The attorney agreed to represent the proponent of the will in a contested probate proceeding pursuant to a contingent-fee arrangement. The agreement provided for an initial retainer of $5,000 plus 33% of any proceeds he would recover on her behalf, by settlement or trial, up to a maximum fee of $600,000. The attorney negotiated a settlement admitting the propounded will to probate in exchange for a minimal payment to objectants. Two years later, the client brought a proceeding to fix his counsel's fees. The Surrogate granted the attorney's motion for summary judgment, enforcing the contingency fee agreement, and dismissed the petition. The client appealed and the Appellate Division reversed the order, remanding the matter to the Surrogate's Court for consideration of the *Freeman-Potts* factors and to evaluate the reasonableness of the retainer agreement. Thereafter, the Surrogate's Court found that the fee was reasonable and was supported by the evidence, a determination ultimately affirmed by the Appellate Division.

Werper

Similarly, another recent case, *In re Werper*,[17] evidences the Surrogate's Court's broad authority in fixing fees. In *Werper*, the attorney's efforts resulted in the recovery of $62,455.04, the balance owed to the estate on two promissory notes. The attorney sought approval of a fee of $53,064.38. The court focused on two factors in its determining what constituted a reasonable fee: (1) the difficulty of the questions involved and (2) the benefit resulting from such services. As to the first, the court concluded that the issue was "quite simple in nature." Moreover,

based upon the result achieved, the court found that the fee request was unreasonably high. The court adopted a novel approach and relied upon the standard applied by the lower courts in cases involving the enforcement of promissory notes, resulting in fees as high as 20% of the notes' face value. The court, in an exercise of discretion, applied the same approach and set the reasonable attorney's fees at 20% of the notes' face value.

While a Surrogate generally will not interfere with a retainer agreement absent proof of fraud, mistake or overreaching,[18] the Surrogate nevertheless bears the ultimate responsibility of deciding what constitutes reasonable compensation. Regardless of the retainer agreement, an estate is not bound to pay more than a reasonable amount in legal fees.[19] Where a personal guaranty clause is at issue, however, the question becomes whether the fiduciary, in his or her individual capacity, may agree to pay an amount over and above the amount the Surrogate determines is properly payable from the estate.

Jurisdictional Issues

The Surrogate's Court's jurisdiction concerning disputes involving personal guaranty clauses is less than clear, as such disputes could well be characterized as disputes "between living persons."[20] A determination regarding the Surrogate's Court's jurisdiction over such fee disputes will require an analysis of the underlying facts.

Levine

In *In re Levine*,[21] for example, the court held that where an attorney was hired by a client who was both a cofiduciary and legatee of an estate, and performed services that benefited both the estate and the individual interests of the client, the Surrogate's Court had jurisdiction

> to parse the two types of services, and make an award against the client personally for the services that furthered only the client's interests as either a legatee or as a challenged cofiduciary whose conduct was found to be against the interests of the estate and resulted in his removal.[22]

Dicosimo

Likewise, in *In re Dicosimo*,[23] the court held that it lacked jurisdiction over a request that it order the objectant law firm to refund to the estate that portion of legal fees, paid by a nonfiduciary beneficiary for services rendered to that beneficiary, determined to be excessive. The retainer agreement was between the objectant and the beneficiary, individually; the invoices were submitted directly to the beneficiary, who paid for all of the services in full from his own funds. The court noted that the beneficiary might be held responsible for the entire fee even though the objectant might not have been able to recover the entire fee from estate funds had the agreement been with the fiduciary of the estate; and most of the services were rendered in another court involving a dispute between decedent's siblings.

Weiss

In addition, in *In re Weiss*,[24] the Surrogate refused the executor's request to review legal fees chargeable to the estate where the executor was the sole residuary beneficiary. The court held that it did not have jurisdiction because the dispute as to legal fees was one between living persons that did not affect the administration of the estate.

Warsaski

However, in *In re Warsaski*,[25] the attorney for unsuccessful objectants in a probate proceeding sought an order permitting her withdrawal as counsel of record and fixing her legal fees. The objectants opposed the fee request, arguing that the court lacked jurisdiction as the dispute was between living persons.[26] The court disagreed, noting that the dispute "arises out of services rendered in a probate contest tried before this court. Thus, 'the Surrogate's Court is in a unique position to determine the amount of fees owed to a plaintiff in light of the extensive litigation that has taken place in that court.'"[27]

Lohausen

Similarly, in *In re Lohausen*,[28] the court addressed the issue of its jurisdiction to fix and determine legal fees in a proceeding by the decedent's daughter, the sole distributee, a residuary beneficiary, and executor of his estate. Counsel was retained by letter agreement to "probate the estate." In addition, counsel agreed to prepare an inventory of assets, appear in court, marshal assets, obtain a tax identification number and review the assets for estate tax purposes. The fee was set at 5% of the gross taxable estate. Counsel billed the daughter $103,000, which she paid in part from her personal funds and in part from estate funds. In support of the SCPA 2110 proceeding, the daughter alleged that counsel took advantage of her in connection with the fee arrangement and that the reasonable value of his services did not exceed $10,000. Counsel moved to dismiss on the basis that the estate had been fully administered and the fees had been paid in accordance with the retainer. Accordingly, he argued the court no longer had jurisdiction. Counsel also argued that because the petitioner executed the retainer in her individual capacity, the matter was a contractual dispute between living persons.

Surrogate Kelly concluded that there was no time limitation on the court's jurisdiction to fix counsel's fee. Most important, the court held that, in any event, it had the inherent authority to supervise the conduct of counsel and the legal fees charged for services rendered, as well as the jurisdiction to do so pursuant to the New York State Constitution with respect to the issue of the retainer. As to counsel's argument that petitioner individually retained and paid counsel, therefore she was bound by the retainer and the court could not modify its terms, the court disagreed. It held that an attorney bears the burden of establishing that the

retainer's terms were fairly presented and understood by the client, and that the fee is fair and reasonable. The court further held that an agreed-upon fee may be disallowed if the amount of the fee is so large as to become out of proportion to the value of the professional services rendered.

Enforceability of Personal Guaranty Agreements

The validity and enforceability of personal guaranty attorney fee agreements is supported by the history behind the Surrogate's authority to fix fees. Originally, the executor of an estate was required to pay from personal funds the fee of the attorney for the estate. Upon the settlement of the executor's account, the executor had a right of reimbursement from the estate to the extent the payment was deemed reasonable and necessary. In 1914, the Legislature enacted former Code of Civil Procedure 2692, authorizing a fiduciary to pay attorney fees from the funds of the estate. However, notwithstanding § 2692, if a fiduciary disputed the fees, the attorney could bring an action at law against the fiduciary in his or her individual capacity. In 1916, the Second Department held in *In re Rabell*[29] that if a fiduciary refused to pay the full amount, the Surrogate's Court had jurisdiction to fix the amount of the fee and direct its payment from the estate in a special proceeding. Finally, in 1923, the Legislature enacted former Surrogate Court Act § 231-a, the predecessor to SCPA 2110, which broadened the Surrogate's jurisdiction by also giving the court jurisdiction over disputes between an attorney and a nonfiduciary of the estate, such as a devisee, legatee or other person interested in the estate.

Ganea

Other relevant authority also supports the validity of such fee arrangements. One of the first cases on the subject, *Seth Rubenstein, P.C. v. Ganea*,[30] was not a Surrogate's Court proceeding at all; rather, it was an Article 81 guardianship proceeding. There, the principal issue was whether an attorney who failed to obtain a written retainer agreement or letter of engagement with a client, in violation of applicable rules, could nevertheless recover the reasonable value of professional services rendered in *quantum meruit*. The court answered that question in the affirmative. A secondary issue was whether an attorney awarded fees in a guardianship proceeding could seek to recover additional fees from the client who sought the appointment of the guardian. The court answered that question in the affirmative as well.

It is "possible for a court to find that an attorney entered into a reasonable fee agreement with the petitioner in a guardianship proceeding, but to also conclude that the amount to be paid as 'reasonable compensation' by the AIP is less than the overall amount the petitioner agreed to pay,"[31] saying that, "[u]nder such circumstances, attorneys may recover additional fees from the petitioner pursuant to the attorney-client fee arrangement." The court relied on cases decided in the context of matrimonial proceedings, standing for the proposition that "an award of attorneys' fees to a spouse pursuant to [the Domestic Relations Law] does not preclude attorneys from seeking, from their own client, the balance of fees earned if the retainer agreement permits it."[32]

> The Surrogate has broad discretion in determining what constitutes reasonable compensation for legal services rendered.

The "Code of Professional Responsibility provides that attorneys must reach 'a clear agreement . . . with the client as to the basis of the fee charges to be made,'"[33] and attorneys consulted by clients anticipating the commencement of Article 81 proceedings should, therefore, "make clear beyond question that any fee arrangement agreed upon is wholly independent of and not controlled by the determination of the guardianship court as to what may constitute reasonable compensation to the attorney."[34] The attorney "bears the burden of establishing that he reached a clear agreement with [the client] that she would be responsible for fees incurred in the guardianship proceeding, including the amount that the fair value of legal services exceeds the amount awarded by the guardianship court."[35] While the absence of a retainer letter is not dispositive on the issue of the existence of such an agreement, "[a]ny misunderstanding or lack of clarity arising from [the attorney's] failure to provide a letter of engagement or enter into a signed retainer agreement shall be resolved in favor of the client."[36]

Coudert Brothers

Appellate Division authority supports the enforceability of similar fee agreements in Surrogate's Court proceedings. In *Coudert Brothers v. de Cuevas*,[37] the First Department affirmed a grant of summary judgment in an action to recover unpaid legal fees, determining, *inter alia*, that

> [t]he Surrogate's disallowance of a portion of plaintiff's legal services, on the ground that such did not benefit the estate directly, was not binding or determinative of plaintiff's claims herein in view of the retainer agreement wherein defendant agreed to be individually liable for services rendered "in connection with the administration of the . . . estate, and various litigations involving the estate."

Yet, agreements by which fiduciaries assume personal liability for legal fees have not met with universal approval by the Surrogate's Courts.

Valk

In re Valk[38] was a proceeding brought to establish a supplemental needs trust. Before the court was a motion, *inter alia*, to reargue a portion of a prior decision in which the court fixed counsel's fees and directed that "'to the extent that the guardian/trustees have paid counsel more than this amount [$8,500.00], the excess should be refunded by counsel.'"[39] The attorney argued that the court "overlooked or misapprehended pertinent case law" – specifically, *Ganea*, among others – supporting the proposition that the petitioner may assume personal liability for legal fees beyond those the court awards from the guardianship estate.

The court noted that even assuming *Ganea* was applicable to matters other than Article 81 proceedings – the court noted, *in dicta*, that it was not – "the cases are clearly distinguishable from this court's prior decision in this case" because, the court, in its prior decision, determined that the fees requested by counsel were "'significantly higher than those customarily charged for work of this nature.'"[40] Unlike in *Ganea*,

> where the attorney was given leave to seek an additional fee equal to the amount by which the "fair value of legal services exceeds the amount awarded by the . . . court," here the court has already determined the fair value of the legal services provided and awarded a fee in that amount. There is, therefore, no amount by which the fair value of counsel's services in this case exceeds the amount awarded because the amount awarded is the fair value of the legal services provided.

Grassi

In *In re Grassi*,[41] a contested accounting proceeding, the petitioner sought to have the court fix and determine legal fees. The petitioner's retainer agreement with counsel provided that "[i]n the event that there are net sufficient assets in the estate or if any of our legal fees are disallowed by the Surrogate, [petitioner] agree[s] to be personally responsible for all legal fees incurred in this matter."

The court noted that

> [a] review of the time records submitted show that the attorneys spent a significant amount of time performing work for which, under the terms of their retainer agreement, they cannot seek reimbursement, including work for the beneficiaries, with whom there was no retainer agreement; preparing a deed and transfer papers for the beneficiary of specifically devised property; performing work that was administrative in nature; and, preparing their own affidavit of legal services.

It therefore fixed legal fees in an amount less than that sought by the petitioner's attorneys.

The court, *in dicta*, addressed the provision of the retainer agreement pursuant to which the petitioner agreed to be personally liable for the legal fees incurred. Citing *Coudert* and *Dicosimo*, discussed above, the court noted that "such language in a retainer agreement can be enforceable against the individuals entering into the agreement, but not against the estate as a whole" and, thus, "it appears that petitioner, both by the finding of this court and the language contained in her retainer agreement, could be held personally liable for any legal fees not approved by this court."

However, the court noted that enforcement of the personal guaranty clause could be problematic for counsel under the facts of the case, which

> appear to demonstrate that petitioner relied on her attorneys in distributing the assets of the estate prior to seven months, resulting in her liability. . . . Thus, any effort to collect legal fees from petitioner could be problematic since under these circumstances, reliance on holdings such as the Second Department's decision in *Coudert Brothers* (supra) is not necessarily conclusive on the issue of whether collection of legal fees from petitioner personally should be deemed reasonable.[42]

It appears that the enforceability of personal guaranty provisions is an issue unresolved. Yet, should not a fiduciary, subject to potential liability in his or her personal capacity, be entitled to counsel of his or her choice, especially in view of the fact that there is no expense to the estate? If the fiduciary is agreeable to such a fee arrangement, the only inquiry in a fee dispute concerning the personal guaranty provision should be the inquiry applied to retainer agreements generally. The only appellate authority on the issue, the First Department's decision in *Coudert Brothers* and the Second Department's decision in *Ganea*, appear to indicate that this is the correct approach. Moreover, the argument can be made that given that the dispute is between living persons, the Supreme Court is the proper court to determine the enforcement of the personal guaranty clause in the retainer agreement. On an equitable basis, it is troubling that our client in the scenario described above, who voluntarily signed such a retainer agreement, could now refuse to pay counsel the agreed-upon fee, despite receiving the benefit of such representation. ■

1. That is not to say the agreements are not subject to any judicial review. They can be reviewed, like any other attorney fee agreement, to determine whether they are fair, reasonable, and whether the fee agreed upon is unconscionable. The Court of Appeals has noted that "attorney-client fee agreements are a matter of special concern to the courts and are enforceable and affected by lofty principles different from those applicable to commonplace commercial contracts." *In re Cooperman*, 83 N.Y.2d 465, 472 (1994) (citations omitted). "'[C]ourts as a matter of public policy give particular scrutiny to fee arrangements between attorneys and clients, casting the burden on attorneys who have drafted the retainer agreements to show that the contracts are fair, reasonable, and fully known and understood by their clients.'" *King v. Fox*, 7 N.Y.3d 181, 191 (1994).

2. *In re Deans*, 92 A.D.3d 879 (2d Dep't 2012).

3. This conclusion is supported, analogously, by cases such as *In re Deans*, 92 A.D.3d 879 (2d Dep't 2012), a proceeding to settle the joint account of the coadministrators of an estate. There, the Appellate Division, Second Department, held that the advocate-witness rule did not warrant the disqualification of an attorney coadministrator. It disagreed with the Surrogate's determination that a fiduciary of an estate does not have the same right to self-representation as he or she otherwise has in an individual capacity, noting that "[a] party's entitlement to be represented by counsel of his or her choice is a valued right which should not be abridged absent a clear showing that disqualification is warranted." *Id.* at 811 (citations omitted). Recognizing the "unique circumstances" of an accounting proceeding where "the sole issue, in effect, is the conduct of the fiduciary," the court held that "a fiduciary's interest in the right of self-representation should prevail over the interests of the beneficiaries of the estate, as there is no prejudice to the estate, which is protected by the potential imposition of a personal surcharge against the fiduciary

in the nature of damages if an objectant establishes that the fiduciary was negligent or caused the estate to suffer a loss." *Id.* (citations omitted).

4. *See In re Piternick*, 38 A.D.3d 780, 781 (2d Dep't 2007); *In re Szkambara*, 53 A.D.3d 502 (2d Dep't 2008).
5. 34 N.Y.2d 1 (1974).
6. 241 N.Y. 593 (1925).
7. *In re Kelly*, 187 A.D.2d 718 (2d Dep't 1992).
8. *In re Coughlin*, 221 A.D.2d 676 (3d Dep't 1995).
9. *In re Von Hofe*, 145 A.D.2d 424 (2d Dep't 1988).
10. *In re Sabatino*, 66 A.D.2d 937 (3d Dep't 1978).
11. *In re Shulman*, 68 A.D.2d 940 (3d Dep't 1979).
12. *In re Brehm*, 37 A.D.2d 95 (4th Dep't 1971).
13. *Potts*, 241 N.Y. 593; *Freeman*, 34 N.Y.2d 1.
14. *Stortecky v. Mazzone*, 85 N.Y.2d 518 (1995).
15. 22 N.Y.C.R.R. pt. 137.
16. 122 A.D.3d 867 (2d Dep't 2014).
17. 44 Misc. 3d 1227(A) (Sur. Ct., Dutchess Co. 2014).
18. *In re Schanzer*, 7 A.D.2d. 275 (1st Dep't 1959), *aff'd*, 8 N.Y.2d 972 (1960).
19. *In re Prettel*, N.Y.L.J., Mar. 24, 1999, p. 32, col. 2 (Sur. Ct., Nassau Co.).
20. *See generally In re Lainez*, 79 A.D.2d 78, 435 N.Y.S.2d 798 (2d Dep't 1981) ("[T]he power of the Surrogate's Court relates to matters affecting estates of decedents and not to independent matters involving controversies between living persons" (citations omitted)).
21. 262 A.D.2d 80 (1st Dep't 1999).
22. *Id.* at 80 (citations omitted).
23. 180 Misc. 2d 89, 92 (Sur. Ct., Bronx Co. 1999).
24. N.Y.L.J., July 13, 2009, p. 30, col. 2 (Sur. Ct., N.Y. Co.).
25. 190 Misc. 2d 553 (Sur. Ct., N.Y. Co. 2002).
26. *See id.* at 556.
27. *Id.* (quoting *Rosenman & Colin v. Winston*, 205 A.D.2d 451 (1st Dep't 1994)).
28. 36 Misc. 3d 1209(A) (Sur. Ct., Queens Co. July 2, 2012).
29. 175 A.D. 345 (2d Dep't 1916).
30. 41 A.D.3d 54 (2d Dep't 2007).
31. *Id.* at 65 (citations omitted)..
32. *Id.*
33. *Id.* (Note that Judge Dillon is quoting the ABA Model Code of Professional Responsibility, which was in effect at that time.)
34. *Id.*
35. *Id.*
36. *Id.* at 65–66 (citations omitted).
37. 247 A.D.2d 266 (1st Dep't 1998).
38. 41 Misc. 3d 1216(A) (Sur. Ct., Nassau Co. Sept. 24, 2013).
39. *Id.* at *1.
40. *Id.* at *2.
41. N.Y.L.J., Oct. 28, 2013, p. 44 (Sur. Ct., Suffolk Co.).
42. *Id.*

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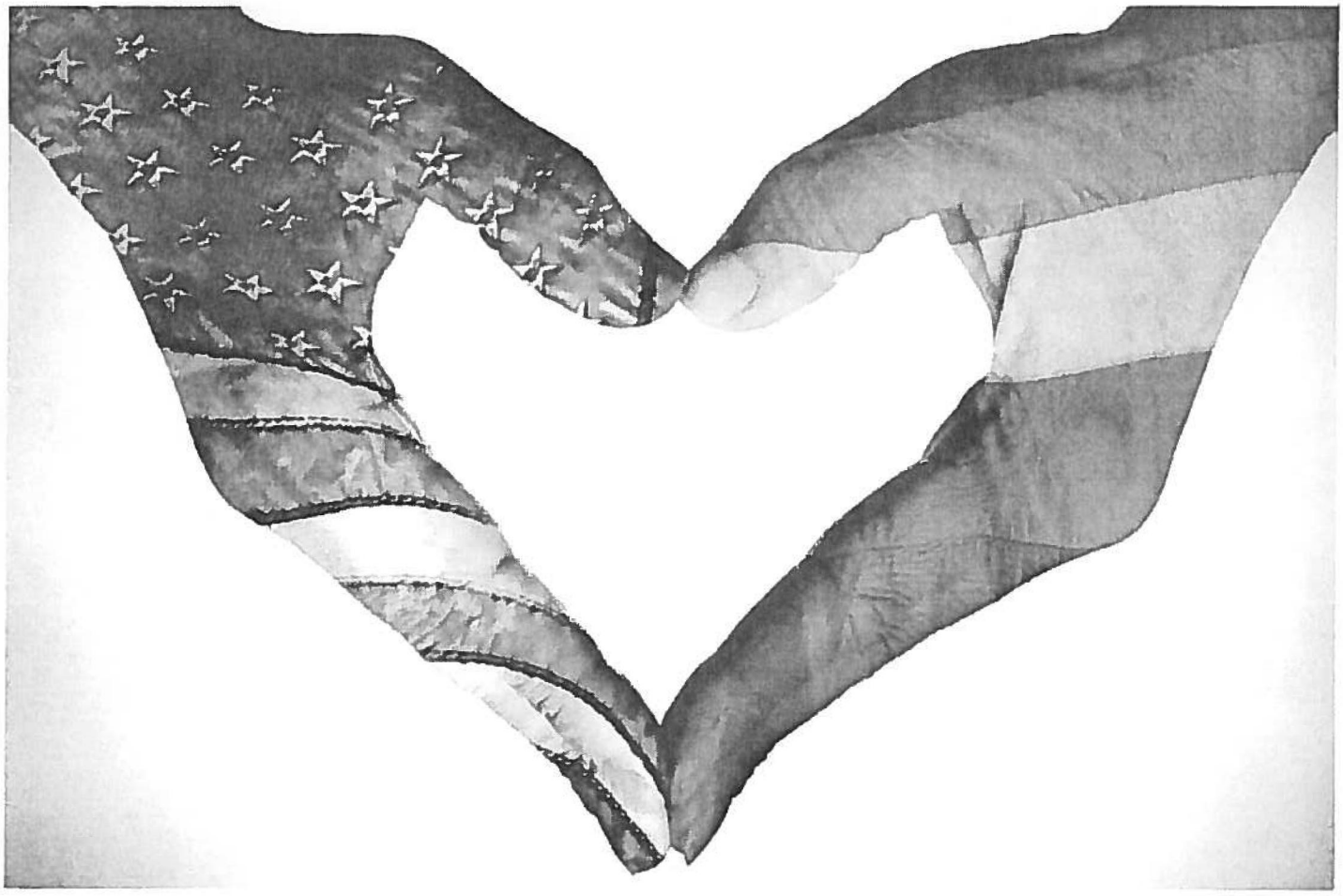

Obergefell v. Hodges

The Effect of the Decision and Estate Planning for LGBT Couples

by Joan M. Burda

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