SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK PART 61

Alan M. Goldston, as Assignee of Goldston & Scwab, LLP,

Plaintiff,

– against–

Bandwidth Technology Corp., and Bandwidth Holdings Corp.,

Defendants.

DECISION/ORDER

Index No. 112098/04

Seq. No. 1

Present:

Hon. Rolando T. Acosta
Supreme Court Justice

The Court previously denied defendants' motions for summary judgment dismissing the complaint and plaintiff's cross-motion for summary judgment dismissing the first, second and sixth affirmative defenses alleged in the answer and informed the parties that a more detailed decision would follow. The Court now sets forth its reasons for denying the motions and hereby vacates and supersedes the August 21, 2005 short-form order. The following documents were considered in reviewing the motions:

Papers	**Numbered**
Notice of Motion, Affidavit, Affirmation & Memorandum of Law	**1-4 (Exhibits A-FF)**
Notice of Cross-Motion & Affidavit & Memorandum of Law	**5-7 (Exhibits 1-9)**
Affirmation and Affidavits in Opposition to Cross-Motion & in Reply	**8-10 (Exhibits A-C)**

Background

Defendant Bandwidth Technology Corp. ("Bandwidth") is the successor in interest to Webface, Inc. ("Webface"). At the time of all the relevant events at issue in this action, Bandwidth was a closely held corporation with three shareholder/ directors – John Leroy Silvers,[1] Erwhin Romer and Jonathan Star – each who owning an equal one-third interest and Star serving as the president. Star, in his capacity as president of this start up business with limited resources, entered into an agreement with Milroy Capital Corp. ("Milroy") to serve as the company's agent for purposes of, inter alia, engaging legal counsel. In May 1998, Milroy brought in Goldston & Schwab, LLP ("G&S") to serve as Bandwidth's legal counsel; plaintiff Goldston was one of two partners in the firm. Milroy was to be compensated with 10% of the company stock and would be responsible for G&S' fees out of this 10%. Within a month, it was decided that G&S's engagement should be directly with Bandwidth and not through Milroy. Accordingly, Goldston and Star began discussing proposed retainer agreements with Bandwidth. See Defendant's Exhibits G-L.

Star rejected G&S's request to serve as general counsel to avoid a potential

---

1. According to Goldston, "[a]lthough Silvers was a shareholder and a director, due to the pendency of a litigation between him and the company, he was excluded from its management" until February 1999.

conflict of interest inasmuch as G&S also represented Milroy. See Defendant's Exhibit I. Star also told G&S that "we shall be seeking your advice on most matters, but we will also be retaining counsel in Upstate NY who will represent our interest alone, and who has no relationship with Milroy. . . ." Id. Star and Goldston on behalf of G&S ultimately entered into a retainer agreement on September 11, 1998. See Defendant's Exhibit L. That agreement states in relevant part:

> We have been engaged to perform various legal services for Bandwidth, Inc. and two successor entities, including:
>
> a) the review of corporate documentation and structure and, as needed, facilitating the correction or adjustment thereof;
>
> b) preparation of settlement agreements and documentation as requested;
>
> c) advice as to general corporate matters as requested;
>
> d) preparation of contracts as requested, except contracts requiring specialty counsel, as to which our engagement will be to select, supervise and coordinate specialty counsel; specifically, we are to prepare non-circumvent and confidentiality agreements; settlement agreements; licensing agreements; service agreements, joint-venture agreements, purchase agreements, sales agreements, employee and agent agreements, agreements relating to the engagement of another company's services, and all agreements not requiring specialization;
>
> e) attendance at and documentation of Directors and/or Shareholders Meetings, as requested;
>
> f) counseling and guidance through the private placement process, as requested; selection, supervision and coordination of litigation,

intellectual property, regulatory and other specialty counsel whose services you may require from time to time;

g) preparation of pre-litigation documents, and carrying out other actions as would precede any possible litigation. Advice on litigation and strategy.

This engagement will not include the preparation of SEC materials in connection with an initial public offering, but may, if requested, include the preparation of such materials as may be required in connection with an initial private placement of securities.

We will perform the above-mentioned legal services, and represent the Company, as requested. We understand that we are not acting as "general counsel" for the Company, and that some of the above-mentioned services will be performed by other counsel engaged by the company. Our firm will be representing the Company, along with other firms, and we understand that we will have no authority to represent the Company in any capacity not requested by the Company.

Although our fees for professional services are usually based on actual time spent, billed at hourly rates, you and we have agreed, in light of the current and projected negative cash-flow and start-up condition of the Company, that for the initial period June 1, 1998 through May 31, 1999, or until Bandwidth Technology Corp. accomplishes an initial private placement of securities whichever shall first occur, our total compensation for the services described above, shall be the issuance to our firm or our designee of four (4) shares, representing 2% of the authorized and outstanding shares, of Bandwidth Technology Corp. These shares will be deemed earned, and shall be issued to our designee(s), immediately upon your acceptance of this agreement, and will cover all services which we have performed heretofore and all the services within the scope described above which may be performed for the Company during that initial period.

Any work which you ask us to undertake which is not subsumed within the share compensation will be billed approximately monthly. Our invoices will contain detail records of each task performed, who performed it, and how long it took.

Star signed the agreement on behalf of Bandwidth. When asked at a deposition whether he ever presented it to the board for signature, he stated "[t]he quorum of the board was present at the time of the signing of the agreement." "I didn't need Erwhin [Romer] to sign the agreement at that moment. The board approval was already in place. It was implicit." Star Dep. at 278-79. He also testified that Goldston advised him that his signature was sufficient. Id. When asked whether he had obtained written board approval, he said no but they had a vote: "Yes, me and Romer represented 62 percent of the shareholders, we agreed on the agreement; we had a quorum of shareholders and directors on the agreement, yes." Id. at 163-65. Defendants note, however, that although Star testified that the agreement was signed in Goldston's office with Romer present, documentary evidence shows that it was in fact signed by Star in Upstate New York and returned to Goldston by facsimile. See Defendants' Exhibit L.

Although Goldston stated that board approval was not required because Bandwidth was a "small, closely held company, which often acted informally," Defendants' Exhibit M at 15, defendants note that Goldston had advised Bandwidth in mid September 1998 that formal board approval was required to sell 1% of its stock to Phillip Wong, an interested investor. Defendants' Exhibits N and O.

In late September 1998, Schwab withdrew as a member of the firm and on

October 1, 1998, Goldston, as the sole remaining member and liquidator of the firm, assigned to himself the uncollected receivables from clients that he was servicing (including uncollected receivables from Bandwidth), subject to "any duty Goldston may have to account to Andrew L. Schwab for collections therefrom in respect of receivables to the Firm arising from services rendered or expenses incurred prior to the withdrawal of Schwab from the firm." Defendants' Exhibit O. On February 19, 1999, Bandwidth officially discharge G&S and on March 1, 1999, it retained Schwab to provide "general and other legal services" through December 31, 2003, in consideration for 2% equity interest in Bandwidth.

In his complaint, Plaintiff alleges three causes of action: specific performance; damages in an amount representing the decline in value of the shares from their highest point of value from September 1998 to the date of judgment; and, present value (estimated at approximately $1,000,000.00) in lieu of specific performance. Defendants raised eight affirmative defenses. Three of the eight affirmative defenses are relevant for disposition of this motion. Namely, the first (retainer is void because Star had no authority to enter into the agreement), second (retainer is void as against public policy) and sixth (plaintiff entitled to damages in *quantum meruit,* if any).

Analysis

Bandwidth's Motion for Summary Judgment Dismissing the Complaint

The burden is on Bandwidth to establish its entitlement to summary judgment. Zuckerman v. City of New York, 49 N.Y.2d 557, 562 (1980). Specifically, it has to establish with admissible evidence that Star did not have the authority to execute the retainer agreement with Goldston and/or that the retainer agreement is unenforceable as a non-refundable special retainer. Assuming that it could do so, plaintiff can defeat the motion by demonstrating the existence of triable issues of fact. Here, not only has Bandwidth failed to meet its burden, there are many triable issues of fact precluding summary judgment.

With respect to whether Star had the authority to enter into the agreement with G&S, Bandwidth argues that neither the by-laws or the certificate of incorporation authorized Star to issue stock to G&S. It also posits that paragraph "FIFTH" of the certificate of incorporation expressly reserves the right to the board to "issue shares" and "fix" the price thereof. There is evidence, however, that two of the three board members were present when the retainer was signed, and the third (Silvers), due to pending litigation between Silvers and Bandwidth, was excluded from management affairs. Moreover, as plaintiff argues, in a close corporation, where informal action has been the norm, the corporation may act without going through the formality of a

board meeting:

> A formal board meeting may not be necessary for valid corporate action where informal action has been customary, particularly in the case of a close corporation, and the directors of such corporation, when few in number and in frequent contact with each other, may act effectively without going through the formality as convening as a board. In other words, where informality has become customary, and the directors of small or close corporation may transact corporate business by conversation and without formal votes at conferences, and in such a case, the action taken is binding on the corporation.

14A N.Y. Jur. 2d Business Relationships § 590; see, also., Leslie, Semple & Gerrison, Inc. v. Gavit & Co., Inc., 81 A.D.2d 950 (3rd Dept. 1981).[2]

Given that Bandwidth was a start-up corporation with only three board members, and evidence exists that informal action had been customary, there are issues of fact as to whether Star had either actual, implied or apparent authority to enter into the retainer agreement with G&S. 14A N.Y. Jur. 2d Business Relationships § 590.

The next issue before this Court is whether the retainer agreement is enforceable as a general retainer, which allows plaintiff to seek contractual damages, or unenforceable as a non-refundable special retainer, which limits plaintiff's compensation to *quantum meruit* only. A "general" retainer is defined as:

---

2. Although Leslie, Semple & Gerrison, Inc. v. Gavit & Co., Inc., 81 A.D.2d 950 (3rd Dept. 1981), states that all board member must be in agreement, Silvers was not involved in management decision given his litigation with the company.

> an agreement between attorney and client in which the client agrees to pay a fixed sum to the attorney in exchange for the attorney's promise to be available to perform, at an agreed price, any legal services (which may be of any kind or of a specified kind) that arise during a specified period. Because the general retainer fee is given in exchange for availability, it is a charge separate from fees incurred for services actually rendered. In other words, such fees are "earned when paid" because the payment is made for availability.[3]

Brickman & Cunningham, Nonrefundable Retainers Revisited, 72 N.C.L. Rev. 1, 6 (1993); In Re Cooperman, 83 N.Y.2d 465, 476 (1993)(implicitly adopting Brickman & Cunningham's definition of general retainer); Levisohn, Lerner, Berger, & Langsman v. Medical Taping Systems, Inc., 20 F. Supp. 2d 645, 653(S.D.N.Y. 1998). An attorney discharged under general retainer is entitled to full contract price. Greenberg v. Jerome H. Remick & Co., 230 N.Y. 70 (1920); Levisohn, Lerner,

---

3. As Brickman and Cunningham state:

> Availability is the essence of a general retainer. A general retainer is an agreement by a lawyer, for value, to forego her right to refuse to perform services for the client even if the need for specific services arises at a time of great inconvenience to the lawyer. It is a commitment to be available to represent the client in matters where the services may or may not need to be rendered in matters that may yet be unknown and undefined. The client paying a general retainer is therefore getting something for the payment: a contractual commitment that the lawyer will be on call to handle the client's legal matters, if and when the client needs her. The arrangement is, in essence, an option contract, under which the client has the right at any time during the "exercise period" to call upon the lawyer and direct her to render services. . . . [T]he reason general retainers do not impair the client discharge right is precisely that general retainers involve a fee that is earned when paid.

Brickman & Cunningham at 23 (emphasis added).

Berger, & Langsman v. Medical Taping Systems, Inc., supra, 20 F. Supp. 2d at 652(citing Brickman & Cunningham at 9, court reasoned that "[a]n attorney discharged under a general retainer may . . . recover the contract price because the general retainer fee was "earned when paid" and therefore not a penalty or loss to the client. . . . This "earned when paid" theory is based on the fact that a general retainer fee (in its pure sense) is paid solely in exchange for the attorney's availability-i.e. at the time of accepting a retainer agreement, the attorney must forgo other employment opportunities in order to remain personally available to the client throughout the term of the agreement").

A special retainer, on the other hand, is "an agreement between attorney and client in which the client agrees to pay the attorney a specified fee in exchange for specified services to be rendered. The fee may be calculated on an hourly, percentage, or other basis and may be payable either in advance or as billed." Brickman & Cunningham at 6. Non-refundable special agreements, "arrangements . . . marked by the payment of a nonrefundable fee for specific services, in advance and irrespective of whether any professional services are actually rendered," are unenforceable and may subject an attorney to professional discipline. In Re Cooperman, supra, 83 N.Y.2d at 469, 471 ("special nonrefundable retainer fee agreements clash with public policy and transgress provisions of the Code of Professional Responsibility *(see,* DR

2-110 [A] [3]; [B] [4]; 2-106 [A]), essentially because these fee agreements compromise the client's absolute right to terminate the unique fiduciary attorney-client relationship"). Although non-refundable special retainers are void as a matter of law, counsel may recover payment in *quantum meruit* for reasonable value of services actually rendered. Id. at 472-73; Wong v. Kennedy, 853 F. Supp 73, 81 (E.D.N.Y. 1994).

The Cooperman decision is significant because the Court of Appeals made very clear that by its holding it "intend[ed] no effect or disturbance with respect to other types of appropriate and ethical fee agreements (See Brickman & Cunningham, Nonrefundable Retainers Revisited, 72 N.C.L. Rev. 1, 6 [1993]). [G]eneral retainers that provide for fees, not laden with the nonrefundability impediment irrespective of any services, will continue to be valid and not subject in and of themselves to professional discipline." In Re Cooperman, supra, 83 N.Y.2d at 476.;

Here, there are triable issues of fact as to whether the retainer agreement signed on September 11, 1998, was a general retainer. It provided for Bandwidth to pay a fix sum of money (2% of the outstanding stock) in exchange for G&S to be available for a specified period (one year). Although the retainer did not use the word "available," the terms of the agreement provided for G&S to indeed be available as "requested." In fact, when listing the various legal services that G&S would provide

during the length of the contract, the parties agreed that G&S would "advice as to general corporate matters as requested."[4] It also provided that G&S would be responsible for preparation of pre-litigation documents, and carrying out other actions as would precede any possible litigation. (emphasis added). This latter section sounds like "a commitment to be available to represent [Bandwidth] . . . in matters where the services may or may not need to be rendered in matters that may yet be unknown and undefined," which Brickman & Cunningham at 23, cite as a characteristic of "availability."

Thus, unlike the special retainers in Wong v. Kennedy, 853 F. Supp. 73 (E.D.N.Y. 1994), where the retainer provided for the attorney to represent Wong in a specific case under indictment or Levisohn, Lerner, Berger, & Langsman v. Medical Taping Systems, Inc., 20 F. Supp. 2d 645, 653(S.D.N.Y. 1998),[5] where the firm agreed to provide a start-up company with intellectual property legal services and to

---

4. The parole evidence rule will not be violated by the introduction of extrinsic evidence because the evidence would not be admitted to change the terms of the retainer agreement, but merely to explain the meaning of the terms of the retainer. Shepard v. Seril, 118 A.D.2d 422(1st Dept. 1986).

5. The Levisohn, Lerner, Berger, & Langsman court made much about the fact that the retainer in that case made no reference to a separate fee in exchange for availability, separate and apart from the fee charged for services. In this case, however, a reference to a separate fee for availability was not warranted given the general and broad nature of the agreement, where G&S agreed to represent Bandwidth in essentially any matter they requested.

defend the company against a competitor, here G&S agreed to represent Bandwidth in essentially any matter that Bandwidth requested. That the agreement stated that G&S was not acting as general counsel is of no moment inasmuch as what distinguishes a general retainer from a special retainer is the element of "availability" rather than whether a firm was hired as general counsel or not. Additionally, the retainer was "not laden with the nonrefundability impediment irrespective of any services," language that the Cooperman Court found offensive, In Re Cooperman, supra, 83 N.Y.2d at 476, and clearly provided that the shares would be "deemed earned immediately." Brickman and Cunningham at 23 ([T]he reason general retainers do not impair the client discharge right is precisely that general retainers involve a fee that is earned when paid).

Nor does this Court find that the agreement necessarily violates DR 2-106, which prohibits a lawyer from charging or collecting an excessive fee. New York City Ethics Opinion 2000-3, 2000 WL 33769162 (N.Y.C. Assn. B. Comm. Prof.Jud. Eth.)(Ethics Opinion) cited by defendants does not prohibit attorneys from accepting securities as compensation. On the contrary, recognizing that:

> [a]s high technology and internet companies have continued to spawn throughout the country from Silicon Valley, California to Silicon Alley, New York, the legal profession has been prompted to examine and adopt alternatives to the conventional hourly billing rate arrangement that has been traditionally applied to more mature companies. In response to the attitudes and concerns of the "new age" entrepreneurs who are often strapped for cash,

> normally risk-averse attorneys increasingly are accepting securities, including options or equity stakes, in startup companies, instead of their customary cash retainers and monthly payments for legal services[,]

it specifically states that "an attorney may, in certain circumstances, ethically accept securities in a client company in exchange for legal services to be performed." Ethics Opinion at 1.[6]

This Court is cognizant of the fact that in late 1998, 2% of the stock was valued at approximately one million dollars, which out of context may seem excessive for a one year agreement to be available. Placed in its proper context, however, the Court does not find the value of the stock to be excessive compensation. The three Bandwidth owners were not naive as to their possible predicament; indeed, their venture was based on the development of intellectual property, a tenuous enterprise

---

6. Inasmuch as the fee in a general retainer is "earned when paid," the section of NYC Eth. Op. 2000-3, 2000 WL 33769162 (N.Y.C. Assn. B. Comm. Prof.Jud. Eth.) cited by defendants is relevant only if the retainer is ultimately determined to be a special retainer:

> a lawyer who accepts securities in whole or in part as a substitute for cash fees is bound in the event of his or her premature discharge or withdrawal to receive no more in value than the work to the date of discharge or withdrawal justifies. To the extent the work has not been completed, it is clear that receipt of the entire fee contemplated to be charged at the outset would be excessive and must be credited or refunded to the client. N.Y. State 599 (1988). See In re Cooperman, 83 N.Y.2d 465, 633 N.E.2d 1069, 611 N.Y.S.2d 465 (1994). That principle is equally applicable to an arrangement whereby securities are given by the client in payment for legal services to be rendered.

Opinion at 12.

at best. It is also clear that they had no cash flow and needed the services of a an experience attorney to help it "accomplish[] an initial private placement of securities." For that, Milroy hired G&S presumably because Goldston had extensive corporate law experience and had served as branch chief in the Securities and Exchange Commission (SEC) and had led the SEC Unit in the US Department of Justice Organize Crime Strike Force for the Southern District of New York. Significantly, when they retained G&S, the stock was only of speculative value. The company could just as easily have gone "belly up" and the stock would have been worthless. G&S simply chose to assume the risk. It should also be noted that not only did Bandwidth pay with stock for other services, such as to retain Milroy, but after they discharged G&S, they retained Schwab for 2% of their stock. Thus it appears very disingenuous for Bandwidth to complain at this juncture, when, at least partially due to Goldston's efforts, the stock value is considerable.

There are also issues of fact as to whether plaintiff is entitled to specific performance since Schwab left G&S and therefore it was impossible for G&S to perform as required under the agreement.[7] It should be noted, however, that Schwab

---

7. See Haddock Motors v. Metzger, 92A.D.2d ,5(4th Dept. 1983)("A party who seeks specific performance must prove that he has substantially performed his contractual obligations or tendered performance within the time specified in the agreement or within a reasonable time thereafter; that he is ready, willing and able to perform those contractual obligations not yet performed and not waived by the defendant; and that, except where the contract is one for the sale of real property, he

left the firm in late September 1998, a few weeks after the agreement was signed with Golston on behalf of G&S, and yet, Bandwidth did not discharge G&S until February 19, 1999, approximately four and a half months after Schwab left. It appears to this Court that at least during those four and a half months, Bandwidth had waived any objections to have Goldston represent their concerns as a solo practitioner. Indeed, all the pre-retainer correspondence between the parties seems to suggest that Bandwidth was being serviced by Goldston.

Last, the Court also rejects Bandwidth's argument that Goldston has no standing to pursue this litigation. Although Goldston is bound by his fiduciary duties to Schwab, he had to wind down affairs and collect any outstanding receivables owed to G&S. Partnership Law § 64. How the retainer fee is divided between Goldson and his former partner is between them and not relevant to this litigation.

Plaintiff's Motion for Summary Judgment Dismissing the First, Second and Sixth Affirmative Defenses.

For the reasons stated above, plaintiff's motion for summary judgment dismissing defendants first (retainer is void because Star had no authority to enter into the agreement), second (retainer is void as against public policy) and sixth (plaintiff entitled to damages in *quantum meruit,* if any) affirmative defenses is also denied.

---

has no adequate remedy at law(see, generally, 55 NY Jur, Specific Performance, §§ 4, 25; 4 Pomeroy, Equity Jurisprudence [5th ed], §§ 1401, 1402, 1407")(emphasis added).

Accordingly, defendant's and plaintiff's motions for summary judgment are DENIED.

This constitutes the Decision and Order of the Court.

SO ORDERED

Dated: September 29, 2005

Rolando T. Acosta, J.S.C.

ROLANDO T. ACOSTA
J.S.C.

Jonathon D. Warner, Esq.
Warnet & Scheuerman
6 West 18th Street 10th Floor
New York, NY 10011
Attorneys for Defendants

Neal Schwartzfeld, Esq.
Penn Proefriedt Schwartzfeld & Schwartz
114 West 47th Street
New York, NY 10036