IN THE UNITED STATES BANKRUPTCY COURT FOR THE EASTERN DISTRICT OF TENNESSEE

In re

Case No. 03-31932

MEDEX REGIONAL LABORATORIES, LLC

Debtor

CHARLES McRAE SHARPE,
CHAPTER 11 TRUSTEE

Plaintiff

v. Adv. Proc. No. 03-3208

PERSHING, YOAKLEY & ASSOCIATES, P.C.

Defendant

NOTICE OF APPEAL FILED:	August 23, 2004
DISTRICT COURT NO.:	3:04-cv-438
DISPOSITION:	On July 20, 2005, U.S. District Court Judge Leon Jordan reversed the bankruptcy court's August 19, 2004 order.

MEMORANDUM OPINION

August 19, 2004

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF TENNESSEE
NORTHERN DIVISION

IN RE:	:	
	:	
MEDEX REGIONAL	:	Case No. 03-31932
LABORATORIES, LLC	:	Chapter 11
	:	
Debtor	:	
	:	
CHARLES McRAE SHARPE,	:	
CHAPTER 11 TRUSTEE	:	
	:	
Plaintiff	:	
	:	
v.	:	Adv. Proc. No. 03-3208
	:	
PERSHING, YOAKLEY &	:	
ASSOCIATES, P.C.	:	
	:	
Defendant	:	

BEFORE THE HONORABLE RICHARD STAIR, JR.
UNITED STATES BANKRUPTCY JUDGE

APPEARANCES:

FOR THE PLAINTIFF:

DEAN B. FARMER, ESQ.
KEITH L. EDMISTON, ESQ.
Post Office Box 869
Knoxville, Tennessee 37901

APPEARANCES (Continued):

FOR THE DEFENDANT:

MARTIN B. BAILEY, ESQ.
Post Office Box 1308
Knoxville, Tennessee 37901-1308

THE COURT: As has proved typical in this extremely contentious adversary proceeding, the court is once again confronted with numerous objections and motions filed by the parties. Specifically before me this afternoon are the Objection to Plaintiff's Rule 26(a)(3) Disclosure and Defendant's Brief in Limine Pursuant to Paragraph 6(g) of the Scheduling Order filed by the Defendant on July 23, 2004; the Petition for Writ of Habeas Corpus ad Testificandum filed by the Plaintiff on July 26, 2004; the Renewed Motion by the Plaintiff to Continue Trial Date and Modify the Scheduling Order or, in the Alternative, for a Voluntary Dismissal Without Prejudice Under Fed. R. Civ. P. 41(b) [sic], and Motion by Keith L. Edmiston, Dean B. Farmer, and Hodges, Doughty & Carson, PLLC to Withdraw as Counsel filed jointly by the Plaintiff and his attorneys, Hodges, Doughty & Carson, PLLC, on July 28, 2004; the Plaintiff's Objection to Defendant's Rule 26(a)(3) Disclosure filed by the Plaintiff on August 2, 2004; the Motion in Limine to Exclude the Testimony and Report of Bradford Eldridge filed by the Plaintiff on August 2, 2004; and the Motion in Limine Regarding the Testimony of John A. Lucas filed by the Plaintiff August 3, 2004. Supporting briefs have been filed with almost every motion, as have responses and briefs in opposition to each objection and motion.

After reviewing the present objections and motions, the history of this adversary proceeding, and considering the conflict of interest that has developed between the Plaintiff and his attorneys, I have decided to focus solely on the Plaintiff's request for a voluntary dismissal filed July 28, 2004. First, let me say that the caption to this Motion refers to a voluntary dismissal "under Fed. R. Civ. P. 41(b)." Rule 41(b) deals with involuntary dismissals and what the Plaintiff clearly requests is a voluntary dismissal pursuant to Rule 41(a)(2) of the Federal Rules of Civil Procedure.

Briefly, the history of this adversary proceeding is as follows. The Complaint was filed by the Debtor-in-Possession, MEDex Regional Laboratories, L.L.C., on December 23, 2003, and amended on May 27, 2004. The Plaintiff alleges that the Defendant breached an employment engagement contract between the Debtor and the Defendant, under which the Defendant recruited and recommended for employment the Debtor's former Chief Financial Officer, Mike Ladd. The Plaintiff contends that this breach of contract was a proximate cause of the Debtor's bankruptcy filing and seeks damages of, at a minimum, $7,410,000.00, plus reasonable costs and expenses.

On March 5, 2004, the court held a scheduling conference, and pursuant thereto, entered a Scheduling Order on March 8, 2004. The Scheduling Order set forth deadlines for disclosures, discovery, the filing of motions *in limine*, and set a three-day jury trial commencing on September 20, 2004. The dates and deadlines set forth in the Scheduling Order were agreed upon by the parties at the scheduling conference. Among the agreed upon deadlines were a March 31, 2004 cutoff for making disclosures pursuant to Federal Rule of Civil Procedure 26(a)(1), the Plaintiff's April 23, 2004 deadline for disclosure of any expert witnesses, followed by a May 14, 2004 deadline for the Defendant to disclose any expert witnesses, and a final discovery deadline of May 31, 2004. The Scheduling Order was amended pursuant to the court's May 21, 2004 Order, extending the Defendant's time to designate expert witnesses to June 30, 2004, and making July 31, 2004 the deadline for the completion of all discovery, including depositions "for evidence." Additionally, the May 21, 2004 Order allowed the Plaintiff through May 27, 2004 to supplement his Rule 26(a)(1) disclosures regarding damages.

On March 18, 2004, the court approved the appointment of a Chapter 11

Trustee in the underlying bankruptcy case, and Charles McRae Sharpe was duly appointed by an Order entered on March 26, 2004. On May 21, 2004, the court entered an Order substituting Mr. Sharpe, in his capacity as Chapter 11 Trustee, as the Plaintiff in this adversary proceeding.

On July 12, 2004, the court entered an Order that did two things: (1) it denied the Plaintiff's Motion seeking to modify the March 8, 2004 Scheduling Order to allow the designation of an expert witness to testify as to damages; and (2) it denied the Plaintiff's Motion requesting a continuance of the September 20, 2004 trial date. The basis behind the July 12, 2004 ruling is set forth in the Memorandum on Plaintiff's Motion to Identify Expert and Motion to Continue Trial Date and Modify Scheduling Order that was filed with the Order.

Now before me is the Plaintiff's Renewed Motion again requesting a continuance of the trial and modification of the Scheduling Order to extend the expert disclosure and discovery deadlines. Alternatively, the Plaintiff moves that he be allowed to voluntarily dismiss the Complaint without prejudice. The Renewed Motion is joined with a Motion by the Plaintiff's attorneys that they be allowed to withdraw as counsel. Hodges, Doughty & Carson, PLLC, the Plaintiff's attorneys, ground their withdrawal motion, in part, upon a conflict of interest that has arisen with the Plaintiff. That conflict is grounded upon facts set forth in paragraphs 8 through 20 of the July 28, 2004 Motion, which reads as follows:

> 8. The Attorneys have been relying on the testimony of Richard F. Ray, MEDex's CFO, to prove damages, and assert that Mr. Ray may render opinions on the damage issue under Fed. R. Evid. 701.
>
> 9. The deposition of Mr. Ray took place on June 24,

2004, after the hearings on May 20, 2004 and June 17, 2004 where the Attorneys stated that they would not be calling an expert to testify at trial.

10. Shortly after Mr. Ray's deposition on June 24, 2004, the Attorneys filed a motion to continue the trial and modify the scheduling order, which motions were denied by order entered by this Court on July 12, 2004.

11. On July 22, 2004, Michael H. Fitzpatrick . . . the attorney for the Trustee, met with the Attorneys and advised the Attorneys that the Trustee alleges, as a result of this Court's opinion of July 12, 2004, that the Attorneys' failure to designate an outside expert on the issue of damages constitutes legal malpractice and that prosecution of the case without an expert is not in the best interests of the Estate due to a perceived impairment of the ability to prove damages.

12. Although the Trustee has not as of the time of the filing of this motion terminated the Attorneys with respect to this adversary proceeding, the Trustee has terminated his engagement of the Attorneys with respect to all other matters related to the bankruptcy of MEDex.

13. After meeting with Fitzpatrick, the Attorneys immediately consulted with Carl Pierce, a professor of law in the area of professional responsibility, and discussed the existence of a conflict of interest.

14. The Attorneys have requested an informal opinion

from Lance Bracy, chief disciplinary counsel of the Board of Professional Responsibility, regarding whether the circumstances set forth hereinabove create a non-waivable conflict of interest.

15. As of the date of the filing of this motion, the Attorneys have not received the opinion of Mr. Bracy, but the Attorneys expect the opinion will be received prior to a hearing on this motion.

16. The Attorneys believe that the circumstances regarding the allegation of legal malpractice by their client, the Trustee, creates a conflict of interest that may be materially adverse to the Trustee pursuant to Tenn. Sup. Ct. R. 8, RPC 1.7(b).

17. The Attorneys believe that withdrawal may be mandatory under Tenn. Sup. Ct. R. 8, RPC 1.16(a), and the Attorneys are in the process of attempting to obtain an informal opinion in this regard.

18. The Attorneys believe that, based on the perceived conflict of interest and the existence of sufficient ambiguity in the Rules of Professional Responsibility as to whether withdrawal under these circumstances is mandatory and non-waivable, it is prudent to seek withdrawal, at least conditionally at this time.

19. Due to the circumstances which have arisen regarding the Trustee's assertion of legal malpractice by the Attorneys, the Attorneys and the plaintiff additionally request

that this Court continue the trial date and modify the scheduling order to extend the discovery and expert disclosure deadlines so as to prevent any prejudice to the parties and to the estate.

20. In the alternative, the plaintiff and the Attorneys seek an order allowing the plaintiff to voluntarily dismiss this action without prejudice.

Rule 41 of the Federal Rules of Civil Procedure, made applicable to this adversary proceeding by Rule 7041 of the Federal Rules of Bankruptcy Procedure, states, in material part:

> (a) Voluntary Dismissal: Effect Thereof.
>
> (1) By Plaintiff; By Stipulation. . . . . Unless otherwise stated in the notice of dismissal or stipulation, the dismissal is without prejudice, except that a notice of dismissal operates as an adjudication upon the merits when filed by a plaintiff who has once dismissed in any court of the United States or of any state an action based on or including the same claim.
>
> (2) By Order of Court. Except as provided in paragraph (1) of this subdivision of this rule, an action shall not be dismissed at the plaintiff's instance save upon order of the court and upon such terms and conditions as the court deems proper. . . . . Unless otherwise specified in the order, a dismissal under this paragraph is without prejudice.
>
> . . . .
>
> (d) Costs of Previously-Dismissed Action. If a plaintiff who has once dismissed an action in any court commences an action based

> upon or including the same claim against the same defendant, the court may make such order for the payment of costs of the action previously dismissed as it may deem proper and may stay the proceedings in the action until the plaintiff has complied with the order.

FED. R. CIV. P. 41.

The decision to grant a motion to dismiss under Rule 41(a)(2) is within the sound discretion of the court, which may dismiss either with or without prejudice, and/or may condition the dismissal upon certain requirements, or "terms and conditions," to be met by the plaintiff. *See, e.g., Knafel v. Pepsi Cola Bottlers of Akron, Inc.*, No. C83-3534-A, 1987 U.S. Dist. LEXIS 16918 (N.D. Ohio February 4, 1987); *B & J Manufacturing Company v. D.A. Frost Industries, Inc.*, 106 F.R.D. 351, 352 (N.D. Ohio 1985). "The plaintiff's reasons for desiring to dismiss are immaterial." *B & J Manufacturing Company*, 106 F.R.D. at 352 (quoting *Home Owners' Loan Corporation v. Huffman*, 134 F.2d 314, 318 (8th Cir. 1943)). Instead, the court's essential inquiry is whether the defendant will be unduly prejudiced by dismissal. *B & J Manufacturing Company*, 106 F.R.D. at 352. Legal prejudice is defined as follows:

> What suffices to require a court to exercise its discretion to deny the motion, or to dismiss with prejudice, has been variously described as harm manifestly prejudicial to the defendant, substantial legal prejudice to defendant, and the loss of any substantial right. The question is whether the granting of plaintiff's motion infringes the legal or equitable rights of the defendant as shown by the circumstances and facts conceded or

> undisputed. When considering a dismissal without prejudice, the court should keep in mind the interests of the defendant, for it is his position which should be protected. The task for the Court then is to determine how the defendants in this action would be affected by a dismissal without prejudice.

B & J Manufacturing Company, 106 F.R.D. at 352 (quoting *Spencer v. Moore Business Forms, Inc.*, 87 F.R.D. 118, 119-20 (N.D. Ga. 1980)).

"In determining whether a defendant will suffer plain legal prejudice, a court should consider such factors as the defendant's effort and expense of preparation for trial, excessive delay and lack of diligence on the part of the plaintiff in prosecuting the action, insufficient explanation for the need to take a dismissal, and whether a motion for summary judgment has been filed by the defendant." *Grover by Grover v. Eli Lily & Company*, 33 F.3d 716, 718 (6th Cir. 1994) (citing *Kovalic v. DEC International, Inc.*, 855 F.2d 471, 474 (7th Cir. 1988)); *see also Smith v. VW Credit, Inc. (In re Smith)*, 227 B.R. 667, 672 (Bankr. N.D. Ill. 1998) (quoting *Clark v. Tansy*, 13 F.3d 1407, 1411 (10th Cir. 1993)). "'Plain legal prejudice' does not result simply because the defendant faces the prospect of defending a second lawsuit, nor does it result simply because the plaintiff may gain some tactical advantage in a future lawsuit." *Johnson v. Pharmacia & Upjohn Company*, 192 F.R.D. 226, 228 (W.D. Mich. 1999); *see also Grover*, 33 F.3d at 718; *Smith*, 227 B.R. at 672. Additionally, "the advanced state of the litigation and the legal and other expenses incurred . . . do not mandate a denial of plaintiff's motion . . . ." *B & J Manufacturing Company*, 106 F.R.D. at 353 (quoting *Louis v. Bache Group, Inc.*, 92 F.R.D. 459, 461 (S.D.N.Y. 1981)). "[The] presence of all factors listed in the foregoing precedent is by no means necessary. Rather, the factors are 'simply a guide for the trial judge, in

whom the discretion ultimately rests.'" *Smith*, 227 B.R. at 673 (quoting *Kovalic*, 855 F.2d at 474).

As for what "terms and conditions" are imposed, the Sixth Circuit generally allows for the imposition of attorney's fees and costs if the case is dismissed without prejudice. *See, e.g., Johnson*, 192 F.R.D. at 229 ("In this circuit, a court may award attorneys fees against the dismissing party when a dismissal is without prejudice for the purpose of 'compensating the defendant for expenses in preparing for trial in the light of the fact that a new action may be brought in another forum.'") (quoting *Smoot v. Fox*, 353 F.2d 830, 833 (6th Cir. 1965)). "However, because the purpose of the award is to ensure that a defendant does not have to defend the case twice, only those fees representing work that could not be used in subsequent litigation on the same claims should be awarded." *Johnson*, 192 F.R.D. at 229.

Specifically, in *Duffy v. Ford Motor Co., Inc.*, 218 F.3d 623 (6th Cir. 2000), the Sixth Circuit set forth some requirements concerning imposition of "terms and conditions." In *Duffy*, the plaintiffs moved to voluntarily dismiss on the third day of trial, following the district court's exclusion of two "key" witnesses. The court granted the motion, with the caveats that the plaintiffs must pay the defendant's costs and attorney's fees that could not be recouped in a subsequent lawsuit, the amount of which would be determined if and when the plaintiffs refiled, and that all evidentiary rulings, including a partial summary judgment, would be applied to any subsequently refiled case. After the plaintiffs refiled, the court determined the amount of costs that must be paid, and when the plaintiffs were unable to pay them, the court dismissed the second lawsuit, in essence with prejudice. The Sixth Circuit found the court's "involuntary" dismissal was an abuse of discretion.

First, the court held that "it was an abuse of discretion for the court not to

consider the Duffys' responsibility for Ford's wasted costs in assessing costs against the Duffys rather than their counsel." *Duffy*, 218 F.3d at 630. Again focusing on the desire for a plaintiff to "have his day in court," the Sixth Circuit found that the district court should have analyzed whether the plaintiffs' attorneys were at fault, and if so, they should bear the costs. *Duffy*, 218 F.3d at 630. Next, the court held that the trial court abused its discretion by failing "to give the Duffys notice of the approximate amount of costs for which they would be responsible upon refiling and to afford them an opportunity to withdraw their motion" prior to entering the dismissal order. *Duffy*, 218 F.3d at 630. "At the time that [a plaintiff] move[s] voluntarily to dismiss the action, they should [be] informed of the specific conditions that [will] be placed on their dismissal and given the opportunity to withdraw the motion if they [find] those conditions to be too onerous." *Duffy*, 218 F.3d at 631. Nonetheless, the Sixth Circuit found that "[a]lthough the district court's failure to give the Duffys proper notice was an abuse of discretion, we find that it was reasonable to condition the voluntary dismissal upon the payment of Ford's costs." *Duffy*, 218 F.3d at 632.

The following cases give other examples of contingencies imposed upon plaintiffs by the courts in dismissing under Rule 41(a)(2). *See Pontenberg v. Boston Scientific Corporation*, 252 F.3d 1253, 1256 (11th Cir. 2001) (holding that the district court did not abuse its discretion in granting the plaintiff's motion for voluntary dismissal, conditioned upon payment of the defendant's costs, despite the fact that "the discovery period had expired and after her expert reports had been excluded from the record as a result of her attorney's failure to timely comply with the expert disclosure requirements of Rule 26[]" because "[n]either the fact that the litigation has proceeded to the summary judgment stage nor the fact that the plaintiff's attorney has been negligent in prosecuting the case, alone or together, conclusively or per se

establishes plain legal prejudice requiring the denial of a motion to dismiss."); *Bentz v. Reed Elsevier, Inc.*, No. C-3-00-350, 2000 U.S. Dist. LEXIS 203070 (S.D. Ohio Dec. 5, 2000) (requiring any refiling be filed in the same court).

Here, Mr. Sharpe was appointed Chapter 11 Trustee several months after the bankruptcy case and this adversary proceeding were filed. As might be expected, he retained the Debtor's counsel, who had familiarity with the lawsuit, to proceed in his behalf. At the point of his substitution as Plaintiff on May 21, 2004, the Scheduling Order had been in place for almost three months, the Plaintiff's April 23, 2004 expert disclosure deadline had already expired, and the other amended discovery deadlines, pursuant to the May 21, 2004 Order, were approaching. Under these circumstances, it is difficult to hold Mr. Sharpe accountable for actions that had taken place prior to his involvement in the adversary proceeding.

In summary, I am going to grant the Plaintiff's July 28, 2004 Motion to the extent a voluntary dismissal is requested. The dismissal will be without prejudice; however, the Defendant, Pershing, Yoakley & Associates, P.C., will be entitled to recover its costs expended in defending the action prior to its dismissal. These costs will not include attorney fees. It would be extremely difficult, if not impossible, to determine those attorney fees that would not be recurring expenses in future litigation involving these parties. Furthermore, costs will not be taxed to the Plaintiff or to the bankruptcy estate of MEDex Regional Laboratories, L.L.C., but will be charged in their entirety to the Plaintiff's attorneys, Hodges, Doughty & Carson, PLLC. Finally, the court will condition the Plaintiff's refiling of his action against Pershing, Yoakley & Associates, PLLC, based on the facts of the present action on the payment of the costs taxed herein.

I will not ask the court reporter to transcribe my opinion. If she does so, it

will be submitted to me for such corrections as I deem necessary, at which time the Memorandum will then be filed and, of course, served on counsel for all parties in interest. An appropriate Order will be entered.

FILED: August 20, 2004

/s/ Richard Stair, Jr.
RICHARD STAIR, JR.
U.S. BANKRUPTCY JUDGE

IN THE UNITED STATES BANKRUPTCY COURT FOR THE EASTERN DISTRICT OF TENNESSEE

In re

Case No. 03-31932

MEDEX REGIONAL LABORATORIES, LLC

Debtor

CHARLES McRAE SHARPE,
CHAPTER 11 TRUSTEE

Plaintiff

v. Adv. Proc. No. 03-3208

PERSHING, YOAKLEY & ASSOCIATES, P.C.

Defendant

O R D E R

For the reasons set forth in the memorandum opinion dictated from the bench on August 19, 2004, the court directs the following:

1. The Renewed Motion by the Plaintiff to Continue Trial Date and Modify the Scheduling Order or, in the Alternative, for a Voluntary Dismissal Without Prejudice Under Fed. R. Civ. P. 41(b) [sic] filed by the Plaintiff on July 28, 2004, jointly with the Motion by Keith L. Edmiston, Dean B. Farmer, and Hodges, Doughty & Carson, PLLC to Withdraw as Counsel filed by the Plaintiff's attorneys, Hodges, Doughty & Carson, PLLC, is, to the extent of the requested alternative relief of voluntary dismissal, GRANTED.

2. The Complaint filed by the Plaintiff on December 23, 2003, as amended on May 27, 2004, is DISMISSED, without prejudice.

3. Pursuant to Rule 41(a)(2) of the Federal Rules of Civil Procedure, made applicable to this adversary proceeding by Rule 7041 of the Federal Rules of Bankruptcy Procedure, as a "term and condition" of dismissal, the Defendant shall recover its costs in defending this action, excluding attorneys' fees, from the Plaintiff's attorneys, Hodges, Doughty & Carson, PLLC.

4. The Plaintiff shall not be entitled to refile his action against the Defendant until the costs of the present action have been paid.

SO ORDERED.

ENTER: August 19, 2004

BY THE COURT

/s/ Richard Stair, Jr.

RICHARD STAIR, JR.
UNITED STATES BANKRUPTCY JUDGE