

IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF UTAH

CENTRAL DIVISION

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IN RE: UNPUBLISHED OPINION

WASATCH FACTORING, INC.,) Bankruptcy No. 83A-00134
Debtor.)

UNPUBLISHED OPINION

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MEMORANDUM DECISION AND ORDER
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Michael Deamer, who was appointed attorney for Wasatch Factoring, Inc., a corporate debtor, by order of this Court dated January 21, 1983, has made application for approval of attorney's fees for services rendered to the debtor in this Chapter 11 proceeding. His affidavit, filed in support of the application, shows that he has represented that debtor since January 14, 1983. The record before the Court further shows that Mr. Deamer commenced the representation of certain principals of the debtor on March 21, 1983.

At the hearing on the application, held at the same time as the hearing on the application for approval of attorney's fees for the attorney for the creditor's committee, no objections to the allowance of Mr. Deamer's fees were made, and there have been no objections made as to the quality of the services he performed for the debtor. However, because of the significance of the legal problems raised by an attorney representing both the

corporate debtor and the principals of that debtor, the Court took the application for approval of attorney's fees under advisement, and now renders this opinion.

11 U.S.C. §1101(1) defines a "debtor-in-possession" as including the "debtor" under Chapter 11. There is no distinction between the two roles. Matter of Triangle Chemicals, Inc., 687 F2d 1286, 1290 (5th Cir., 1983). Under §1107(a) a debtor-in-possession has all the rights and powers of a trustee, and must perform all the functions and duties of a trustee. Under §327(a) the trustee, with the Court's approval, may employ one or more attorneys that do not hold or represent an adverse interest to the estate, and that are disinterested persons, to represent or assist the trustee in carrying out the trustee's duties. The term "disinterested person" is defined in §101(13), and for the purposes of this opinion, is a person as described in §101(13)(E) that does not have an interest materially adverse to the interest of the estate or of any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor. Section 327(a) is a mandate and must be rigidly applied, and cannot be waived because of the integrity or ability of the attorney. See In re Philadelphia Athletic Group, 20 B.R. 328 (E.D. Pa., 1982). Evidence of the significance that the drafters put on being disinterested or representing adverse interests is §328(c), which

provides that the Court may deny allowance of compensation for services and reimbursement of expenses of a professional person if such professional person is not a disinterested person, or represents or holds an interest adverse to the interest of the estate with respect to the matter on which such professional person is employed.

One of the more troubling problems for a debtor's attorney is where the attorney is consulted by principals (officers, directors, etc.) of the corporation and requested to represent them personally in connection with the difficulties arising out of the financial problems of the debtor, or in other matters. There is a distinction between the problems of a corporation and the problems of the individual principals. These problems may not always be the same. In fact, the solution to these problems may create conflicts of interest, especially in a bankruptcy situation. For example, if a transfer to a principal has occurred, the validity thereof should be examined by the debtor-in-possession. If an attorney represents the debtor-in-possession, as well as the principal, the attorney cannot give unbiased advice to one party or the other. One of the two clients will suffer the consequences of the action or lack of action advised by the attorney. Thus, if the attorney represents the debtor, as well as a principal, the attorney is not a disinterested person, and does represent an interest adverse to the estate.

The theory underlying the requirement of being disinterested is that the attorney for the debtor should exercise a measure of independent judgment, because of the multiple duties of the client owed to large bodies of creditors and shareholders. In Bohach Corp. v. Gulf & Western Industries, Inc., 607 F.2d 258 (2nd Cir., 1979) the Court went so far as to rule that the fact that an attorney had close ties to the debtor's chairman was sufficient to create a disqualifying conflict, even though the attorney would not be ineligible under the literal language of the governing statute. This concept is consistent with Canon 5 of the American Bar Association Code of Professional Responsibility, which deals with the exercise, by a lawyer, of independent professional judgment on behalf of a client. Ethical consideration 5-1 states that "[t]he professional judgment of a lawyer should be exercised . . . solely for the benefit of his client and free of compromising influences."

In addition to the conflict which was created by operation of law, when Mr. Deamer began to represent both the debtor and some of its principals, the record in the case reflects a divided loyalty. The Disclosure Statement on the Debtor's First Amended Plan, signed by Mr. Deamer as counsel, shows that the debtor and its officers are currently involved as defendants in litigation, and that the officers are requesting indemnification from the

debtor. At the hearing on the adequacy of the Disclosure Statement, counsel for the Unsecured Creditor's Committee argued against such indemnification, while Mr. Deamer argued for it. Mr. Deamer, therefore, has a conflict of interest in fact and by operation of law.

In ruling on entitlement to fees, where an actual conflict exists, there is no need to make other findings, such as fraud, mismanagement, or negligence. Woods v. City National Bank and Trust Co., 321 U.S. 262 (1941). The mere appearance of a conflict has been held to be sufficient, as a matter of policy, to deny compensation. See Mossert v. Darrow, 341 U.S. 267 (1951).

Standards for denial of compensation for representing adverse interests have previously been decided by this Court. In re Penoyer Farms, No. 81M-03621; In re Cottontree Inn, No. 82C-02016, and In re Arden Howard Spencer, No. 82C-02016. These standards and rulings are incorporated herein by reference. Copies of these rulings are attached.

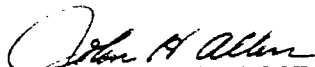
An order was signed by this Court on August 17, 1983, approving interim payment of attorney's fees to Deamer in the amount of \$20,235.00 for services and \$468.55 for costs. The application covered the time period from January 14, 1983,

through July 31, 1983. The Courts view interim allowances as "sustaining allowances," subject to final adjustment. In re Callister, 673 F.2d 305 (10th Cir. 1983). See New England Carpet Company, 28 B.R. 766 (Vt., 1983); Matter of Pennsylvania Tire & Rubber Company of Mississippi, 19 B.R. 124 (Ohio, 1980); Matter of Mansfield Tire & Rubber Company, 19 B.R. 12 (N.D., Ohio, 1981); In re Vermont Real Estate Trust, 26 B.R. 905 (Vt., 1983); In re International Horizons, Inc., 10 B.R. 895 (N.D., Ga., 1981). In light of its determination that Mr. Deamer has a disqualifying affiliation with the debtor and its principals and is, therefore, not a "disinterested person", the Court has reconsidered its previous allowance of compensation.

IT IS THEREFORE ORDERED:

1. That the pending application for compensation is denied.
2. That any order by this Court allowing compensation for services rendered subsequent to March 21, 1983, is set aside.

DATED this 28 day of September, 1984.



JOHN H. ALLEN

UNITED STATES BANKRUPTCY JUDGE