

**CURRENT DEVELOPMENTS – PROFESSIONAL ETHICS
IN BANKRUPTCY CASES AND PROFESSIONAL COMPENSATION**

**44th Annual Southeastern Bankruptcy Law Institute
March 22-24, 2018**

**Susan M. Freeman
Lewis Roca Rothgerber Christie LLP
SFreeman@LRRC.com**

I. Bankruptcy Professional Ethics Update

Disqualification

In re Blue Jet, Inc., 2017 WL 785606 (Bankr. D.N.M. Feb. 28, 2017).

A Chapter 11 debtor sought to retain its prepetition lawyers as general bankruptcy counsel. The prepetition retention agreement authorized an attorney's charging lien to collect unpaid fees. In response to a U.S. Trustee objection that the lawyer thereby became a secured creditor, the lawyer represented he would only seek to enforce a charging lien if the case converted to Chapter 7. But the lien would encumber the debtor's postpetition cash and accounts receivable.

The court noted that most courts have held that DIP counsel may obtain a prepetition retainer and remain disinterested, with the retainer disclosed and court approval required before it can be used. Other collateral is reviewed more skeptically, on a case-by-case basis. *In re Martin*, 817 F.2d 175 (1st Cir. 1987). The court found that most *Martin* factors weigh against approval of a charging lien for work in the main case. It also noted that accounts receivable and cash generated during a bankruptcy estate do not constitute a fund generated by the attorney's efforts to which a lien could attach. But the court held that if the lawyer sought to file an adversary proceeding or contested matter to collect funds for the estate, especially if pursued on a contingent fee basis, a charging lien against such funds may be reasonable. It held that the employment application would be approved only if the charging lien proposal was waived, provided that a separate application for specific litigation work would be addressed separately, if ever filed.

In re WM Distribution, Inc., 571 B.R. 866 (D.N.M. 2017).

The court refused to approve the employment of a law firm as Chapter 11 DIP counsel because it was already DIP counsel for another entity owned by the estranged spouse of the DIP's owner. The two companies' businesses were deeply intertwined with extensive inter-company claims including one owing over \$500,000 to the other and owning the trademark on its most valuable product. Both were managed by the divorcing couple's daughter. Because the adversity was so central to the reorganization of the debtors, appointment of conflicts counsel was held not to be a viable solution.

In re Lightning Dock Geothermal Hi-01, LLC, 2017 Bankr. LEXIS 1574 (Bankr. D.N.M. June 8, 2017).

A law firm proposed as special counsel for the Chapter 11 debtors did not have a conflict of interest despite its representation of the debtors' corporate parent which provided DIP financing and would acquire all of the equity under the debtor's plan since special counsel's representation was limited to specific matters.

In re Roper and Twardowsky, LLC, 566 B.R. 734 (Bankr. D.N.J. 2017).

A Chapter 7 trustee was not allowed to retain as special counsel attorneys who were principals in the debtor law firm. The bankruptcy case involved disputes over the rights of multiple law firms and lawyers to litigation settlement proceeds. The lawyers would be witnesses in adversary proceedings, are creditors asserting secured and unsecured claims, are defendants in fraudulent transfer actions, and have other adverse connections to the bankruptcy estate. The lawyers committed to provide their services, objecting to other creditors' claims, free of charge. Their interests were allegedly aligned with the estate because their claim recoveries would increase if other claims were disallowed.

The court discussed applicable state professional responsibility rules and noted that the lawyers could not represent the estate without being materially limited by their own personal financial stakes in their proposed litigation and their competing roles in the case. It held that the lawyers would flagrantly violate RPC 1.7 by representing parties on opposite sides of litigation, representing the estate while also seeking to collect their claims from it. They have a personal stake in recovering money for themselves and ensuring the trustee does not pursue them for any causes of action the estate may have. The court held that retention of the lawyers would violate RPC 3.7, due to their likely witness status.

The court held that the application did not meet the criteria of § 327(e) because the lawyers would represent the trustee in every major legal action affecting the liquidation and distribution of the bankruptcy estate. It also found that the proposed duties would overlap those of the trustee and his general bankruptcy counsel. And while the lawyers would work without charge and were intimately familiar with the facts, the court described a case record replete with complaints about their lack of cooperation with creditors and the trustee and disregard of deadlines. And the lawyers had offered excuses of health problems and a heavy workload for other clients. Thus, their employment was not in the best interest of the estate. They were not disinterested or lacking in any adverse interest as required for § 327(a) employment.

In re Moore, 2017 Bankr. LEXIS 3459 (Bankr. E.D. Mich. July 14, 2017).

A Chapter 7 trustee's proposed special counsel was disqualified because he represented a creditor prepetition engaged in lengthy litigation where the debtor's appeal of claims against the creditor remained pending, and he continued to represent the creditor during the case, including in an adversary proceeding contesting exemptions. The remedies under the creditor's § 523 action and the estate's § 727 action are inherently contradictory, and the lawyer's billing to the estate would be murky in that services for the creditor and the trustee would overlap. The creditor objecting to special counsel also raised inter-creditor conflicts incapable of resolution without a court order, and the court recognized the value of a neutral attorney for the estate.

In re Corwin Place, LLC, 562 B.R. 663 (Bankr. N.D.W.Va. 2016)

The court refused to grant a debtor's request to disqualify a creditor's law firm. While the debtor had sought representation from the firm to sue the creditor on lender liability grounds, the court found that the debtor was merely a prospective client and that no significantly harmful information was provided by the debtor to the firm. The debtor's principal spoke with a paralegal once, and with attorneys only to schedule a meeting that did not occur. The attorneys' communications noted that the firm had not accepted any engagement. The debtor provided copies of loan documentation and email communications between the debtor and creditor. The court applied professional conduct rule 1.18 regarding prospective clients.

In re Olympia Office LLC, 562 B.R. 8 (Bankr. E.D.N.Y. 2017).

Debtor's counsel was disinterested and did not have an interest adverse to the estate on account of a law firm partner being first cousin of the majority owners of the debtor's equity. The owners had transferred the complaining creditor's collateral without the lender's consent to new entities shortly before bankruptcy. The court analyzed the meaning of Code § 101(45), defining "relative" to mean "an individual related...within the third degree as determined by common law." While other courts have held that a first cousin meets this definition, New York law holds otherwise, and counsel was allowed to continue representing the debtor.

In re Pilgrim Medical Center, 2017 WL 3311227 (Bankr. D. N.J. July 27, 2017).

While the application to employ committee counsel was pending, the committee was disbanded by the U.S. Trustee when the debtor recharacterized the members as secured. The firm moved to reinstate the committee, but that motion was adjourned while the parties discussed and finally agreed upon a settlement incorporated into a plan. Although not officially employed, committee counsel made several substantive contributions to the case, including reversal of fraudulent conveyances and obtaining a subordination agreement with an insider. The court approved the firm's retention *nunc pro tunc* under the extraordinary circumstances of the case. It held the firm to be disinterested even though it represented an unsecured creditor in connection with the case and secured creditors on unrelated matters. The debtors' specific objections to fees were overruled, except for time spent on conflicts checking and establishing disinterestedness.

In re Grimmatt, 2017 WL 2437231 (Bankr. D. Idaho June 5, 2017)

The Chapter 7 debtor's law firm undertook such efforts to ensure it was paid in full that it potentially impaired its client's ability to obtain effective relief through the bankruptcy filing and violated bankruptcy laws and ethical rules. A fee agreement was signed by the debtor a month before the bare-bones petition filing, accompanied by a request to pay the filing fee in installments (promptly granted) and payment of \$500 prepetition to the lawyer. The engagement agreement included a form allowing the lawyer to draft funds from the debtor's debit card without further notice or consent and provided that the debtor consented to a billing company collecting fees from the debtor pursuant to a factoring loan agreement. The lawyer threatened the client with dire consequences of nonpayment when she fell behind in installments, and the U.S. Trustee sought disgorgement of all fees. The lawyer claimed his collection tactics were not abusive and that his fee agreement was permissible under *In re Hines*, 147 F.3d 1185 (9th Cir. 1998).

The court found that the engagement agreement committed the lawyer to perform almost all of the services the debtor needed to obtain effective bankruptcy relief, but it also granted counsel the contractual right to withdraw if she failed to pay. The court questioned whether the particular unbundling agreement was reasonable and whether the client gave truly informed consent as required by applicable ethics regulations, but ruled the agreement impermissible just as a matter of bankruptcy law. The agreement was held improper because the lawyer was not obligated to perform critical services such as appearing at the 341 meeting if the client failed to pay, and certain services such as helping with reaffirmation agreements and stay relief motions would be separately billed. And, because the entire agreement was executed prepetition, the debtor's payment obligation was discharged, and the lawyer could only seek fees for postpetition work on *quantum meruit* grounds.

Further, the lawyer likely violated the automatic stay by his collection efforts. He had a conflict of interest in collecting without informing the client of the discharged fees and implying that he could withdraw the fees without advising that the court would have to approve it. The court therefore deemed compensation excessive under § 329(b), and also found that Rule 2014 disclosures were inaccurate, both grounds for denial of compensation. The lawyer's payment coercion efforts also violated the installment fee order, which required full payment of the filing fee before any further payments were made to counsel. And he used computer software for client signatures instead of obtaining wet signatures, another ground for fee disgorgement.

In re Fish & Fisher, Inc., 574 B.R. 608 (Bankr. S.D. Miss. 2017).

The court followed *In re Crivello*, 134 F.3d 831 (7th Cir. 1998) to hold that the court has discretion to award fees to a professional whose employment order was vacated on grounds of lack of disinterestedness.

In re Kretchmar, 2017 Bankr. LEXIS 3429 (Bankr. W.D. Okla. Oct. 4, 2017).

The Chapter 7 trustee sought to employ counsel for an under-secured creditor as special estate counsel to pursue recovery of assets for the estate. The lawyer sought, as counsel for both the trustee and the creditor, substantive consolidation of the debtor's estate with those of the debtor's parents. Upon objection by the defendants, the court held that the lawyer had no conflict because both the trustee and the creditor with a substantial deficiency claim sought to enlarge the pot of funds for payment to unsecured creditors. The court warned that if the creditor sought to assert a security interest in recovered or consolidated property, the lawyer would be disqualified *sua sponte*.

In re Shelnut, 2017 Bankr. LEXIS 3404 (Bankr. S.D. Ga. Oct. 4, 2017).

The potential dispute of whether the law firm's undisclosed postpetition payments by third parties are unauthorized avoidable transfers creates an adverse interest in the lawyer engaged as special counsel because the bankruptcy estate has a potential cause of action against the recipients and against the law firm. In such circumstances, the law firm would not be able to independently evaluate the merits of pursuing the cause of action.

In re Stone Res. Inc., 2017 Bankr. LEXIS 1241 (Bankr. E.D. Pa. May 4, 2017).

Chapter 11 DIP counsel represented the debtor's principal and sole shareholder in the district court contempt proceedings for violating a non-compete agreement. The district court found that a contempt ruling would have resulted in effect in a judgment against the debtor in

violation of the automatic stay. This disclosed representation was held not to cause a disqualifying conflict. DIP counsel argued that the conflict was merely potential and the interests of the company and shareholder were aligned. A consent decree was ultimately entered in the district court case. The bankruptcy case was converted to Chapter 7, and the issue affected former DIP counsel's entitlement to compensation.

Disclosure Deficiencies

In re Digerati Technologies, Inc., 2018 WL 501384 (5th Cir. Jan. 19, 2018).

The Fifth Circuit affirmed an opinion reported at 524 B.R. 666 (Bankr. S.D. Tex. 2015), sanctioning an investment banker by denial of all fees for failure to disclose that the firm was represented by DIP counsel in an appeal of an adverse fee determination in a different Chapter 11 case. DIP counsel's fee award also was reduced for that disclosure violation. 537 B.R. 317 (Bankr. S.D. Tex. 2015). That professional-client relationship must be disclosed and is sufficient grounds to deny compensation. The bankruptcy court also found that both professionals billed for services that did not benefit the estate.

In re Berjac of Oregon, 2017 WL 2984113 (Bankr. D. Or. June 14, 2017).

DIP general bankruptcy counsel, who also served as counsel for the Chapter 7 trustee upon conversion, did not represent any interest adverse to the estate, but a major creditor bank was the law firm's lender. After initially pursuing an adversary proceeding against the bank and others, the firm made a business decision to withdraw and substitute other counsel (who ultimately settled the litigation).

The firm's management marketed itself toward the bank as a possible source of referrals and one of its board members was a long-time friend of a bank executive. The firm did not disclose its connections with the bank in its Rule 2014 statement, which the court held it should have done even though such commercial banking relationships generally are not disclosed. It did not make a supplemental disclosure after the firm decided to withdraw, or for 1 1/2 years thereafter until the court suggested this should be done. The court found that the firm did not intentionally conceal the connection and provided valuable services unrelated to estate claims against the bank. It approved a fee reduction of \$300,000 that the firm negotiated in a mediated settlement with the Chapter 11 trustee (over the objection of the U.S. Trustee and certain creditors).

In re Memory Lane Assisted Living Facility of Bowdon, LLC, 2017 WL 3475663 (Bankr. N.D. Ga. Aug. 11, 2017).

DIP counsel's employment applications failed to mention that the firm represented the sole member of the debtors in non-bankruptcy litigation and that it was seeking employment in four cases involving affiliated debtors who had intermingled their funds. The court did not find this to be a deliberate attempt to circumvent the requirements of the Code. But the firm's compliance with Rule 2014 was careless, even cavalier. The firm had already reduced its requested compensation and expenses by approximately 60%, but the court reduced it further (for a total of \$8,000) as a sanction.

The court found that the conflicts were potential conflicts, not rising to the level of actual conflict sufficient to deny the employment applications. It decided that if actual conflicts arose, the firm must withdraw at that point or face disqualification.

In re Private Asset Group, Inc., 2017 WL 5035075 (Bankr. C.D. Cal. Nov. 1, 2017).

A Chapter 7 trustee obtained approval of a contingency fee lawyer to pursue a malpractice action against the debtor's former accountants for misrepresentations relating to a Ponzi scheme. The firm brought in \$2.1 million to the estate in a settlement and was awarded over \$900,000 fees. An objection to the claim of the debtor's prepetition contingency fee lawyer led to a dispute between the Chapter 7 trustee and estate contingency fee lawyer. During discovery in that dispute, the lawyer brought out his two previous personal loans to the Chapter 7 trustee, long-since paid in full, without realizing he should have disclosed them at the outset in his Rule 2014 disclosure. The Chapter 7 trustee resigned and was replaced, and the court addressed factors bearing on the amount by which the lawyer should be sanctioned for the disclosure violation. The court found that he did not know, but should have known, that disclosure was required. And it found that the loans did not influence the trustee's or lawyer's actions. The lawyer was sanctioned by a \$35,000 fee reduction.

In re THR & Associates, Inc., 2018 WL 279741 (Bankr. C.D. Ill. Jan. 3, 2018).

An auctioneer charged a "buyer's premium" from a Chapter 7 asset buyer, disclosed only in the report of sale, in addition to the 5% commission plus transportation fees disclosed in the employment application and charged to the estate. The court questioned the wisdom of doubling or tripling auction charges and the validity of assertions that buyer's premiums have no impact on net sales proceeds payable to bankruptcy estates. It said that trustees, as fiduciaries, have a continuing duty to review such practices as they sell estate assets. But the court also held that any such proposed premium must be disclosed in the employment application and be approved by the court. Without full disclosure, the court cannot police the requirement of no interests adverse to the estate.

Rule 2014 requires disclosure of "any proposed arrangement for compensation" with no limitation on the source or application of payments. Rule 6005 requires that the order approving an auctioneer or appraiser "fix the amount or rate of compensation." The court held that amounts collected as a buyer's premium are proceeds of estate property and thus themselves estate property, and therefore must be approved by the court under Rule 2016. The court cannot determine fee reasonableness without such information.

In re Howard Ave. Station, LLC, 568 B.R. 146 (Bankr. M.D. Fla. 2017).

Special counsel for litigation was approved on the basis that fees would be paid by the debtor's principal. He waived any administrative expense claim, but the approval order required fee allowance upon proper application under §§ 330 and 331. Monthly operating reports showed that he was paid \$39,750 by a third party on behalf of the DIP, but he filed no fee applications until the U.S. Trustee objected. Special counsel thereafter cooperated with the U.S. Trustee to make full disclosures and applied for fee approval.

The court held that the attorney's failure to comply with its obligation to disclose fee agreement details was grounds for the court to deny all fees and costs and order disgorgement of amounts already received. But the court exercised its discretion to require only a minimal fee refund. The lawyer was primarily a creditors' lawyer in bankruptcy cases, with little experience in representing a fiduciary or the obligation to disclose payments when received. The court found the lawyer was not willful or reckless and gave significant weight to his cooperation with

the U.S. Trustee and commitment to fully and accurately and timely comply with his duties under Code § 329 and Rule 2016(b).

In re Roman, 574 B.R. 430 (Bankr. D.P.R. 2017)

The court imposed sanctions under Code § 329 and Rule 2016 where debtor's attorney failed to comply with fee disclosure requirements and collected prepetition attorneys' fees from estate funds after the Chapter 7 petition was filed and also before the installment filing fees were fully paid, contrary to Rule 1006(b)(3), and failed to return them. It could not impose sanctions under Rule 9011 because the U.S. Trustee failed to comply with the safe harbor provisions of that rule. The court ordered full disgorgement of fees.

In re Frye, 570 B.R. 21 (Bankr. D. Vt. 2017).

In response to a U.S. Trustee disgorgement motion in a Chapter 13 case, the debtor's counsel argued that Code § 329 was unconstitutionally vague, overbroad, and violated free speech rights. The court held that argument was meritless and that the fees were not excessive. The attorney violated a local rule requiring an application and explanation for any fees sought in excess of the presumed reasonable fee, but met his burden of proving fee reasonableness in the disgorgement hearing. However, the court also held that the attorney's failure to timely and fully disclose all fees violated the Bankruptcy Code and Rule 2016 because fees were in fact in connection with or in contemplation of the bankruptcy, and fees paid by third parties must be disclosed along with payments by the debtor. It held that an appropriate sanction was to require disgorgement of half of all fees paid under the facts of this case, which included the attorney's devotion of substantial time and effort in spite of charging a below-market rate and the debtor's inability to pay for all services, which in turn had a significant financial and emotional impact on his personal life, because the debtors could find no other counsel.

Fee Sharing and Disclosure

In re Harris-Nutall, 572 B.R. 184 (Bankr. N.D. Tex. 2017).

Chapter 13 debtors' counsel entered into a co-counsel arrangement with special litigation counsel to pursue causes of action related to the debtors' mortgages. The agreements provided for sharing of any court award or settlement to incentivize debtors' counsel to pursue such claims and special counsel to do the work. The court held the arrangement prohibited under Code § 504, even though litigation recoveries were the source of fee payments. The concerns warranting § 504 apply in such cases too.

The court also found that the Rule 2014 disclosure affidavits improperly failed to disclose the fee sharing arrangements. These provisions were in the attached engagement agreements, but the court held that was insufficient. It held that the fee sharing agreements in other cases were also a connection that should have been disclosed. The court sanctioned special counsel by a 25% fee reduction and sanctioned bankruptcy counsel by cancelling the agreed entitlement to 25% of special counsel's fees.

In re Wright, 2017 WL 6001685 (Bankr. S.D. Tex. Dec. 1, 2017).

A Chapter 13 debtor – through her bankruptcy counsel – entered into a postpetition fee-sharing agreement with special counsel pursuing litigation on a contingency basis along with her bankruptcy attorney that was not disclosed in the special counsel employment application. The

arrangement was discovered when funds not specifically awarded by the court were not turned over to the Chapter 13 trustee. The funds were estate property and the disclosure omissions violated Code § 327 (which the court found applied to Chapter 13 debtors, not just trustees), § 329, Bankruptcy Rule 2014, Bankruptcy Local Rule 2014-1. The fee sharing violated Code § 504 and fee collection efforts and general counsel's transfer of estate funds to special counsel and their retention of such funds were intentional violations of Code § 362. The court noted ample credible evidence of numerous potential ethical violations, which it left to the State Bar of Texas to address.

Delayed Employment Approval

In re Mussi Realty, LLC, 2017 WL 746219 (Bankr. M.D. Pa. Feb. 24, 2017).

Special counsel engaged to sell restaurant assets failed to seek an order approving employment for several months, then did not obtain *nunc pro tunc* approval. The court rejected the excuses of unfamiliarity with bankruptcy requirements, time constraints and misunderstanding of whether bankruptcy counsel or special counsel was responsible for the application. The court only approved fees incurred post-application from the estate without prejudice to the lawyer seeking compensation from the non-debtor owner of a share of the restaurant.

Breach of Professional Duties to the Client

Brown Media Corp. v. K&L Gates, LLP, 854 F.3d 150 (2d Cir. 2017).

The Second Circuit reversed the district court's dismissal of a lawsuit against DIP counsel alleging breach of fiduciary duty, tortious interference and common law fraud. The plaintiffs were the debtor's principals, who allegedly had retained the firm to advise them about how to retain control over their closely-held corporation in light of impending financing defaults. The firm advised about strategies, including a bankruptcy sale to a stalking-horse formed by the principals, and filed a Chapter 11 case for the debtor. They did not obtain a conflict waiver from the principals, but arranged for a former partner to represent them. The firm did not disclose the representation of the principals in its employment approval application.

During the bankruptcy case, the law firm helped to engineer a sale of the debtor's assets to a competing bidder with which it also had a relationship instead of to the principals. Sale delays and bankruptcy proceedings dragged on, allegedly due to the firm helping a creditor that was also its client. The stalking-horse lost its financing for the purchase and did not bid at or object to the sale. The sale was approved and closed, and a liquidation plan was confirmed. Then the principals sued the law firm and two partners. The district court held that the sale order and confirmation order barred the suit on *res judicata* grounds.

The Second Circuit held that the causes of action were different, noting a standard in bankruptcy of whether an independent judgment in the separate proceeding would impair or invalidate the plan and whether they could have presented their causes of action during the bankruptcy proceedings. It was not persuaded that the bankruptcy court would have structured a different disposition of the case. And it reasoned that if the plaintiffs had alerted the court to DIP counsel's conflicts and other mischief, the court may have acted, but that still would not have been a forum to litigate fully all of their causes of action.

In re Radnor Holdings, Inc., 564 B.R. 467 (D.Del. 2017), *aff'd*, 2017 WL 5900560 (3d Cir. 2017).

Six years after an order approving the sale of Chapter 11 estate assets to the largest secured creditor, the founder, chairman and primary shareholder of the debtor moved to set aside the sale order, objected to the final fee application of DIP counsel Skadden Arps, and filed a complaint to rescind the asset sale, all on the grounds of a conspiracy by the creditor and Skadden to hide conflicts of interest and ensure that an asset sale prevailed over other restructuring options he preferred. The bankruptcy court found that the firm did not fail to make disclosure or act improperly. The district court and Third Circuit affirmed. Then the shareholder appealed from the order dismissing the rescission complaint.

The firm's connections with the creditor had been fully disclosed and explored in an evidentiary hearing when the U.S. Trustee contested its disinterestedness, and the court had found no conflict. Special counsel who had not represented the creditor investigated its claims and potential causes of action against it. Special counsel objected to the creditor's claims and the creditors committee filed an adversary proceeding against it, but the court ruled in favor of the creditor. The committee's appeal was dismissed, and that litigation resolved the issue of a conspiracy to sell the assets to the creditor. The sale order included a finding that a restructuring instead of a sale was precluded by the debtor's circumstances, not by improper conduct on the part of Skadden or the creditor. The sale order was not appealed. Nor was the plan confirmation order appealed.

The district court held that the claims were either time-barred, precluded by prior court orders, or asserted by a party without proper standing, i.e. a shareholder with only derivative claims. The Third Circuit affirmed again.

In re McIntosh, 697 Fed. Appx. 569 (9th Cir. 2017).

The bankruptcy court properly dismissed a Chapter 13 case and declined to award fees to the debtor's attorney because the attorney breached his duty of loyalty. The attorney first argued that a lien was not preserved for the estate and that the equity created by removing the lien would go towards the debtor's homestead exemption. Then after a dispute arose between lawyer and client and the engagement ended, the lawyer argued that the lien was preserved under 11 U.S.C.S. § 551 and that the lien assets should be available to pay unsecured creditors, including the attorney. The duty of loyalty requires that an attorney not injure his former client in a matter arising out of the engagement and survives termination of the attorney-client relationship.

In re Haimil Realty Corp., 2017 WL 6311681 (Bankr. S.D.N.Y. Dec. 8, 2017)

The court refused to reduce DIP counsel's fees on account of nondisclosure allegations made by the equity owner who would obtain free legal services due to such a sanction, given plan provisions for full payment of creditors. But the court also analyzed DIP counsel's unrealistic advice that the DIP had a strong litigation case against its primary secured creditor and absurd "worst case" scenario, its breach of a professional duty to recommend against litigation when the likely cost exceeds the likely litigation value, and the resulting excessive payment obligations to the creditor. It also analyzed the equity owner's knowledge of the strategy and desire to defeat the creditor. The court concluded that a fee reduction was appropriate because counsel's job is to give good advice, even sobering or unwelcome advice,

when the circumstances call for it instead of making zealous arguments that feed a client's desire to do battle. The court also reduced fees because DIP counsel failed to pursue a plan or refinancing of the secured creditor's debt until after the court decided the litigation, resulting in crippling interest accruals, even though the DIP was glad to hold the secured creditor at bay while the litigation proceeded.

In re Swisher, 2017 WL 5634594 (Bankr. C.D. Ill. Nov. 22, 2017).

The court denied a consumer debtor's discharge due to inaccurate disclosures on her Schedules so that she could use cash for rent and moving expenses. It also explained that her attorney could not have fully investigated the debtor's financial affairs as required by § 707(b)(4)(C) and made such errors on the Schedules. If the attorney had recognized the inconsistencies in disclosures of tax refund money and cash on hand and explained the consequences of inaccurate disclosures, the debtor might have waited to file her case until securing and moving into the apartment she needed. The court pointed out that an attorney who overlooks the propriety of timing a filing to maximize the benefits of bankruptcy does not provide competent representation to the client.

In re Bird, 577 B.R. 365 (10th Cir. BAP 2017).

In the context of determining that the fees incurred by a Chapter 7 trustee and his counsel (his own law firm) were unreasonable, the BAP addressed the trustee's duties to the estate and debtor, and competing policies of a debtor's fresh start and payment of unsecured creditors. The debtors' homesteads were subject to liens exceeding their value. But rather than abandoning the property, the trustee entered into stipulations with lienholder the IRS to carve out \$10,000 from the proceeds of any sale otherwise payable to it and moved to sell the property for only a small amount more than the liens. The sale proceeds would be subject to the trustee's and his counsel's fees and broker and closing costs. Effectively, the sale would eliminate the debtors' homesteads, leave them with nondischargeable tax claims, and transfer funds to the trustee and his counsel for unnecessary fees without a meaningful distribution to unsecured creditors.

The proposed sale was circumvented by conversion to Chapter 13, but the trustee and his counsel sought a fee award for their efforts, which the bankruptcy court denied. The BAP noted the trustee's fiduciary duties to the estate, and that the duty to liquidate assets for creditor distributions is limited. When liquidation would result in little to no payment to unsecured creditors, the proper course of action is to abandon the property. It held the bankruptcy court did not err in concluding the services rendered were not reasonably likely to benefit the estates, or in denying the fee applications in their entirety.

Sanctionable Conduct

In re Bressman, 874 F.3d 142 (3d Cir. 2017).

The court affirmed a bankruptcy court vacatur of its default judgment in an adversary proceeding against the debtor alleging securities fraud. The victims' lawyer failed to disclose to the bankruptcy court that he had settled with other wrongdoers in the securities fraud for millions of dollars. The default judgment did not take into account the partial reduction in damages and was improperly excessive even before trebling. The court upheld the bankruptcy court's finding that this was an intentional fraud on the bankruptcy court by the victims' lawyer. It rejected his excuse that the settlement confidentiality order prohibited him from disclosing the existence of

the settlement. The court noted that especially in the *ex parte* context of a default proceeding, the court depends on the integrity of appearing counsel to obtain the full scope of relevant, material information of which he was aware. The lawyer's failure to do that sufficiently undermined the judicial process that it constituted fraud on the court.

In re Keating, 2016 U.S. Dist. LEXIS 186067 (W.D. La. Nov. 16, 2016), rejected in part by *In re Keating*, 2017 U.S. Dist. LEXIS 61196 (W.D. La., Apr. 20, 2017).

A district court magistrate judge recommended upholding bankruptcy court monetary and 90-day suspension sanctions against a lawyer who made material misrepresentations in pleadings and during oral argument, then violated his suspension order by performing work for a client in another case and by misrepresenting the extent of that work in sworn testimony.

Although the bankruptcy court did not specifically find "bad faith," as required for inherent power sanctions, the record was replete with findings tantamount to bad faith that were patent from the record, and that was sufficient. Failure to correct misrepresentations, once discovered, meets the criteria for bad faith. The magistrate also held that authority to sanction extends to actions outside the bankruptcy judge's courtroom, in connection with cases filed or to be filed in bankruptcy court. The magistrate considered the ABA's Standards for Imposing Lawyer Sanctions and extended the bankruptcy court's suspension order for an additional year because the 90-day sanctions did not deter the lawyer from additional misconduct, as he insisted upon parsing court orders relating to transitioning his work to other lawyers as narrowly and as self-beneficially as possible, indicating a willful resistance to the judiciary's authority. And he continued to dispute that much of his conduct was wrongful or intentional, and made outright misrepresentations to the court. At the conclusion of the sanctions period, the lawyer would have to apply for reinstatement, with evidence of ethics CLE. The district court accepted the findings as correct, but allowed the lawyer to apply for reinstatement immediately, one year and two months after the bankruptcy court's sanctions order.

In re Griffin, 563 B.R. 171 (Bankr. M.D.N.C. 2017).

The court entered a show cause order for why the debtor's attorney should not be sanctioned for violating Rule 9011 by filing a declaration in connection with a reaffirmation agreement with inaccurate facts and without personal knowledge of its content. The opinion discusses the critical role of attorneys with respect to reaffirmation agreements, including exercising independent judgment in determining whether the agreement imposes an undue hardship, verifying the creditor's security interests and confirming that liens are unavoidable, as well as advising the debtor of other available options.

In re Sharif, 549 B.R. 485 (Bankr. N.D. Ill. 2016).

The court imposed Rule 9011 sanctions for seven years of attempts to claim trust assets held to belong to a bankruptcy estate, despite repeated rulings rejecting those claims, including at the Seventh Circuit. The court held that the plaintiffs had repeatedly misrepresented facts and law and shown a complete disregard for the judicial system and blatant attempts to circumvent it. The court entered an order to show cause why the litigants and their counsel should not be sanctioned for violating Rule 9011.

In re Dickson, 2017 WL 5634598 (Bankr. E.D. Ky. Nov. 22, 2017).

An elderly debtor filed Chapter 11 on the advice of counsel to obtain the benefit of a stay in lieu of a supersedeas bond in an appeal of a judgment in favor of her daughter. The court dismissed the case as a two-party dispute bad faith filing. The daughter declined to seek Rule 9011 sanctions against DIP counsel who advised the filing, but sought them against the debtor who relied on advice of counsel, underscoring the emotional nature of the family conflict. The court noted cases holding that the standards for a bad faith filing under § 1112(b) are different than for imposing Rule 9011 sanctions and that the likelihood of a repeat occurrence is remote. But the debtor filed a Chapter 11 petition that lacked a legitimate bankruptcy purpose, the creditors incurred significant expense as a result, and litigants are held accountable for the acts and omissions of their counsel. The court ordered that the debtor pay the creditors \$5,000 for the Rule 9011 violation.

In re David Wroblewski & Assoc. Law Ctr., P.C., 2017 Bankr. LEXIS 1247 (Bankr. D. Az. May 2, 2017).

The decision recounts a lengthy investigation of a consumer mill law firm's mishandling of client matters and disobeying court orders, including state bar disciplinary action. The lead attorney owner ultimately was held in contempt for disobeying orders not to distribute client trust account funds, appropriating some of the funds for his own use, and failing to adequately explain his withdrawal of over \$100,000 of client trust funds.

In re Lynch, 2017 WL 416782 (Bankr. N.D. Okla. Jan. 17, 2017).

The debtor's counsel not only displayed incompetence, but also overreached and took advantage of her desperate and vulnerable client, pressing litigation instead of resolving it, advising the debtor that the judge, trustee and others were corrupt and conspiring against him, hiring supporting professionals through Craigslist, pursuing many unsupportable motions, suits and appeals including a complaint against the bankruptcy judge. She embarked on an unreasonable "scorched earth" strategy detrimental to her client and did not even keep competent billing records. The court required that all fees other than fees incurred in state court litigation be disgorged; it held it could not review work unrelated to the bankruptcy case under *In re Hargis*, 895 F.2d 1025 (5th Cir. 1990). The court also blamed the debtor client for not being more diligent and indirectly authorizing and approving of his lawyer's strategy, but placed primary blame on the lawyer.

In re George, 2017 Bankr. LEXIS 1415 (Bankr. E.D. Pa. May 24, 2017).

The court imposed sanctions under its inherent powers and Code § 105 when a lawyer showed a pattern of filing multiple bankruptcy cases solely to stop state court litigation and foreclosure sales and then abandoning his clients, engaging in bad faith, making misrepresentations, and repeatedly failing to file required documents and attend hearings. All fees were ordered disgorged due to failure to file Rule 2016 disclosures or attend fee hearings. In light of the burden on the court and trustees caused by the lawyer's bad faith misbehavior, sanctions were also imposed for vexatious litigation under 28 U.S.C. § 1927.

In re Henry, 2017 Bankr. LEXIS 1877 (Bankr. D. Ak. July 5, 2017).

Rule 9011 sanctions were imposed against an attorney who waited 19 months after being hired to file a Chapter 7 bankruptcy, then filing it in Alaska even though the debtor had moved to

Oregon, deceiving her into believing she was still eligible to file in Alaska and filing incomplete and obsolete forms. Counsel was suspended from representing debtors in Alaska for one year and required to complete CLE in representing consumer debtors and ethics. The court considered and was guided by American Bar Association Standards for Imposing Lawyer Sanctions.

In re Howrey, LLP, 698 Fed. Appx. 881 (9th Cir. June 27, 2017).

The bankruptcy court did not abuse its discretion in partially disallowing the fees sought by committee counsel. He simultaneously represented the committee and individual creditors, without disclosing the individual representations to the committee and improperly disclosing confidential information about the committee's deliberations and strategy. The attorney's excuse of a lack of privilege between joint clients was held inapplicable because the committee did not know of or consent to the representation of individual creditors. The court also upheld the finding that the attorney violated his duty of loyalty to the committee by attempting to pursue alter ego claims against former Howrey partners that the committee had considered and rejected when he was committee counsel, and by opposing a settlement agreement the committee negotiated with the estate.

In re Husain, 866 F.3d 832 (7th Cir. 2017).

Bankruptcy court disbarment and an order to refund fees to 18 clients were upheld as to an attorney who routinely filed bankruptcy petitions and other documents without his clients' wet-ink signatures that the clients had never reviewed. The forged or copied signatures were used on, among other filings, schedules not revealing all assets that the debtors would not have signed if they had seen the documents before filing. The lawyer lied on the witness stand and gave testimony that was not credible. The circuit court also held that a contempt order entered when he failed to comply with the refund should have been heard by a single judge on appeal under 28 U.S.C. § 158(a) instead of the district court's executive committee for disciplinary proceedings. The contempt appeal was remanded for that reason.

In re Nielsen, 2017 WL 57260 (D. Colo. Jan. 4, 2017).

The district court upheld bankruptcy court sanctions including attorneys' fees and punitive damages under 11 U.S.C. § 362(k) against the lawyers who filed the most consumer cases in that district. They marketed and used a "zero down" bankruptcy filing program where a client could hire the firm without paying any up-front fees. Instead, a client would sign an agreement to make payments through regular automatic bank or debit card withdrawals in a total amount the bankruptcy court said was significantly higher than the going rate in that district, \$2,500 for a Chapter 7 case. The client was required to sign a promissory note for the full fee and begin making payments at or soon after the initial consultation. The client was advised that nonpayment would result in a collection action. And the client also signed an agreement to reaffirm the debt after the petition was filed. It informed the client that reaffirmation was voluntary but also explained that lawyers were only willing to provide post-petition services provided that the client reaffirmed the debt.

Bankruptcy courts began denying the reaffirmations, but the law firm kept deducting fees from bank accounts. After lengthy proceedings, the bankruptcy court found intentional stay violations. It determined minimal actual damages, awarded \$2,000 punitive damages, but

declined to award all fees billed by the debtors' replacement counsel who litigated against the firm because they excessively billed on a crusade to shut down their competitor and duplicated work of the U.S. Trustee. The district court affirmed, and the state supreme court suspended the lawyers' licenses.

In re Hanawahine, 2017 WL 4221096 (Bankr. D.Haw. Sept. 21, 2017).

This is an internet law firm case, where the Chapter 7 debtor client was ill-advised by the national firm located online and the local lawyer who started representing her, then ceased when he had a falling-out with the national firm. The national firm and local lawyer were ordered to pay treble damages as a civil penalty under Code § 526, with the underlying damages consisting of the debtor's wages that were garnished when her bankruptcy case was not timely filed, as promised. *See also In re Elrod*, 2017 Bankr. LEXIS 3911 (Bankr. E.D. Tenn. Nov. 14, 2017), where a national internet firm attorney's motion to dismiss a complaint alleging unauthorized practice of law and negligence per se was denied, where a Tennessee debtor was incompetently advised to file a Chapter 13 case instead of using the minimal funds needed to reinstate his mortgage debt by a lawyer not admitted in that state, then his bankruptcy case was mishandled by the designated local attorney.

Matter of Carroll, 850 F.3d 811 (5th Cir. 2017).

The court affirmed the bankruptcy court's sanction against pro per litigants for vexatious litigation of an injunction against future filings and a fine of nearly \$50,000 for opposing counsel's attorneys' fees. The bankruptcy court made detailed findings of facts supporting the conclusion of bad faith action for the purpose of harassing the Chapter 7 trustee and delaying the administration of the bankruptcy estate. The court was empowered to award such sanctions under its inherent power, 28 U.S.C. § 1651 (the All Writs Act) and Code § 105.

In re Greene, 2017 WL 1628870 (Bankr. E.D.N.C. Apr. 28, 2017).

A Chapter 13 debtor satisfied mortgage arrearages under a 2010 plan, the court so found and the debtor was discharged. Then the mortgage was transferred to a new servicer who contended it was delinquent by \$2,000. The debtor repeatedly explained the history to at least 11 servicer representatives and sent them documentation, but they did not correct the record. The servicer started a foreclosure; the debtor lost his job and filed another Chapter 13 case. At a discharge violation hearing which the creditor chose not to attend, the court imposed sanctions of \$10,000 payable to the Chapter 13 debtor, \$10,000 payable to the debtor's law firm, and \$10,000 payable to the clerk of court.

In re Bavelis, 563 B.R. 672 (Bankr. S.D. Ohio 2017)

A secured creditor demonstrated a long-time pattern of deception designed to conceal its postpetition assignment of its interest in the note and security agreement on which its claim was based to an unrelated third party. The claimant and his counsel made false representations during discovery and intentionally withheld relevant documents, then participated in a 4-day hearing in which they attempted to establish the secured claim without mentioning the previous assignment. The creditor's lawyer represented the assignee as well as the assignor in the bankruptcy case post-assignment, but hid the arrangement to avoid disclosure of the purchase price for the secured note. He represented clients with conflicting interests because the assignee sought to collect the maximum amount on the note, and the assignor had no standing or rights to collect

anything in the bankruptcy case. He also represented other clients defending against collection actions by the bankruptcy estate and took other positions detrimental to the interests of actual estate creditors like the assignee. And, he had a “breathtaking disregard for the truth.”

The court imposed sanctions under its inherent power, Code § 105 and 28 U.S.C. § 1927 (vexatious litigation). It rejected the defendants’ argument that they could not be held liable for their actions because the debtor did not seek discovery sanctions under Bankruptcy Rule 7037. The rule did not displace the court’s other authority, and Rule 7037 was deemed “not up to the task” in a situation where the party being sanctioned not only failed to produce a document, but also made misrepresentations both to opposing counsel and the Court that were designed to conceal its existence. The court sanctioned the parties by awarding attorneys’ fees and expenses jointly and severally payable by the assignors and attorney, plus the attorney paying the debtor’s excess costs and fees reasonably incurred, plus punitive damages in an amount to be determined for abuse of process and fraud on the court.

In re Vizconde, 2017 WL 5770034 (9th Cir. Nov. 29, 2017).

The Ninth Circuit upheld *sua sponte* sanctions, agreeing with the BAP that the court’s findings supported the sanctions under the higher “akin to contempt” standard applicable when sanctions are not sought by a party. Monetary sanctions were held to be moderate and appropriately ordered payable to the court, and counsel received sufficient notice through an order to show cause hearing.

Limitations on Sanctions

In re Jemsek Clinic, P.A., 850 F.3d 150 (4th Cir. 2017).

The court held that a bankruptcy court did not err in imposing sanctions against a creditor insurer, but vacated the order because the sanctions were excessive – dismissal with prejudice of claims exceeding \$10 million and payment of \$1.29 million debtor attorneys’ fees. Creditor Blue Cross Blue Shield was named a defendant in a Florida class action claiming improper business practices to deny, delay and reduce payments for medical treatment. It sued a North Carolina doctor three years later for alleged unnecessary or excessively expensive treatments. The doctor filed Chapter 11, removed the litigation to bankruptcy court, and filed counterclaims alleging similar misconduct to the class action complaint. The class action settled, and BCBS and its affiliates were released. The debtor was a putative member of the class, with his counterclaims barred by the settlement release and injunction against such litigation. But although he received notice of the settlement, he did not opt out. When BCBS’ North Carolina counsel raised the release and injunction 10 months later, it was held applicable and upheld on appeal.

The bankruptcy court sanctioned BCBS NC for purposefully avoiding informing the court and debtor about the settlement, by not mentioning it in disclosures and discovery. The Fourth Circuit ruled that BCBS did not violate the class action settlement, but could sanction BCBS NC for delaying and continuing litigation the class action court had resolved and not making disclosures until after the opt-out deadline, even though it had no duty to remind the debtor about the opt-out deadline. But the appellate court ruled that the sanctions were disproportionate to the severity of the misconduct. The debtor was responsible for not opting out and losing his counterclaims, not BCBS NC.

Blixseth v. Yellowstone Mountain Club, LLC, 854 F.3d 626 (9th Cir. 2017).

The co-founder of the Chapter 11 debtor moved to recuse the bankruptcy judge as biased and appealed the denial of his motion to the district court and then Ninth Circuit. Both affirmed the bankruptcy judge. The Court of Appeals further determined that sanctions against the co-founder and his primary attorney were warranted for a frivolous appeal and ordered them to pay the attorneys' fees of multiple opposing counsel under FRAP 38, also ordering the attorney to pay under 28 U.S.C. § 1927.

The court held that fees incurred in seeking or opposing sanctions under the court's inherent power or under FRAP 38 cannot be awarded, only the "direct" fees and costs of opposing the offending pleading or motion. But it held that § 1927 is a fee-shifting statute, and the costs of obtaining sanctions may be included in a sanctions award under that statute. The entire financial burden of an action's defense, including attorneys' fees, may be shifted if the proceedings were unwarranted and should not have been pursued.

In re Blasingame, 2018 WL 286116 (6th Cir. 2018).

The bankruptcy court erred in imposing Rule 9011 sanctions against a lawyer who participated in advising a client that trust assets need not be disclosed on bankruptcy schedules because the complaining creditor failed to comply with the 21-day safe harbor provision of Rule 9011. The rule's exception when the conduct alleged is the filing of a petition was inapplicable because another lawyer handled and took responsibility for the filing.

In re Taylor, 2017 WL 3429029 (9th Cir. BAP Aug. 9, 2017).

Plaintiffs' delay in requesting voluntary dismissal of their adversary proceeding was not sanctionable under the court's inherent power as a matter of law because there was no statute, Rule, Civil Rule, Local Rule, ethical rule or court order requiring more expeditious action. Nor was litigation misconduct in the form of repeated presentation of the same poor quality, rejected arguments the plaintiffs raised in their sanctions defense. Isolated instances of delay to increase the defendants' litigation costs may have been grounds for Rule 9011 relief, but they did not seek such relief or comply with the rule's safe harbor provisions.

In re Roessler-Lobert, 567 B.R. 560 (9th Cir. BAP 2017).

The bankruptcy court erred in sanctioning a creditor in a pro per Chapter 7 case by dismissing a dischargeability complaint at the initial status and scheduling conference. The creditor's lawyer had failed to serve the debtor on a timely basis, so that she received documents 15 days after her response deadline, and telephoned the debtor to say that meet-and-confer requirements were met without actually complying with them. He failed to file a proof of service of the summons or status report. And he sent other lawyers to the initial hearing and hearing on a motion for reconsideration of dismissal (in which he misrepresented facts). The BAP held the sanction to be unduly harsh, while not condoning the lawyer's misrepresentations or negligence. The opinion discusses the standards for sanctions on grounds of failure to prosecute, violation of the scheduling conference order, and failure to comply with local rules.

In re Tukhi, 568 B.R. 107 (9th Cir. BAP 2017).

In the similar context of dismissal of a dischargeability complaint as a sanction for a creditor's counsel's failure to comply with local bankruptcy rules, the BAP again found the

sanction too harsh. It summarized the holding in *Roessler-Lobert*: Dismissal sanctions based on local rule violations must be supported by finding a degree of culpability higher than mere negligence or fault, such as willfulness, bad faith, recklessness, or gross negligence or a repeated disregard of court rules. The sanction must be proportionate to the violation, and the court must consider the public's interest in expeditious resolution of litigation, the court's need to manage its docket, the risk of prejudice to defendants, the public policy favoring disposition of cases on their merits, and the availability of less drastic sanctions.

In re Brizinova, 565 B.R. 488 (Bankr. E.D.N.Y. 2017).

The Chapter 7 trustee sought contempt and sanctions against debtor's counsel pursuant to §105(a), the court's inherent authority, and Bankruptcy Rules 9014 and 9020 on grounds that the attorney violated a stipulated order in another case, a mediation order in another case, and state Rules of Professional Conduct. The court denied the relief without prejudice to a request for such relief in the case where those orders were entered.

The court also refused to sanction counsel for strident and emotion-laden language in a motion to dismiss an adversary proceeding. It held that the trustee failed to show that sanctions were warranted under 11 U.S.C. § 105 and the court's inherent authority, as he did not show that counsel acted in bad faith, or that his conduct was entirely meritless and undertaken for improper purposes.

In re Black, 2017 WL 3034848 (W.D. La. July 18, 2017).

In adversary litigation between a creditor and Chapter 11 individual debtor, the court excluded certain evidence and allowed the debtor to make a proffer for the appellate record only after the judge left the courtroom. The debtor nevertheless referred to the evidence in post-trial memoranda. He removed the references after the creditor moved to strike it. The bankruptcy court found DIP counsel's conduct to be "very serious" and sanctioned him \$3,000 for violating the court's order under his inherent powers.

The creditor's motion to strike had included a request for Rule 9011 sanctions (which the rule requires to be made separately) and was made without presentation to DIP counsel 21 days prior to filing. Under Fifth Circuit law, failure to comply with Rule 9011's safe harbor provisions precludes imposition of sanctions on the opposing party's motion, but not on the court's own initiative. *In re Pratt*, 524 F.3d 580, 586 (5th Cir. 2008). Here, the court had relied on its inherent authority. And while it didn't make a specific finding of bad faith, the district court concluded that was patent from the record and inferred the bad faith finding from the bankruptcy court's statement about counsel's misconduct being a very serious matter.

In re Waldrop, 2017 WL 4857425 (Bankr. W.D. Okla. Oct. 25, 2017).

A Rule 9011 sanctions motion should be filed as soon as practicable after discovery of the violation, not after the entry of summary judgment when the matter is essentially concluded. Such delay turns Rule 9011 from a tool for the deterrence of abusive litigation practices into a mere fee shifting statute.

Klein v. Weidner, 2017 WL 2834260 (E.D. Pa. June 3, 2017).

A Chapter 7 trustee filed an adversary proceeding against the pre-bankruptcy receiver for mismanagement of the estate. The bankruptcy court noted that the trustee had violated the

Barton doctrine by not obtaining pre-complaint permission to sue. But if the complaint were to be dismissed, the limitations period would have run, so the judge submitted proposed findings and recommendations to the district court. It dismissed the case when the trustee declined to proceed. The receiver later sought sanctions. The district court held that it could not award sanctions for vexatious litigation under 28 U.S.C. § 1927 because the allegedly vexatious litigation was in another court, the bankruptcy court. It rejected inherent power sanctions because of the trustee's unreasonable 22-month delay in requesting such relief.

Mar-Bow Value Partners v. McKinsey RTS, 2017 U.S. Dist. LEXIS 163214 (E.D. Va. Sept. 30, 2017).

The district court held that a creditor lacks standing to challenge another professional's inadequate disclosures under Rule 2014 or fee award when reversal will not affect the appealing creditor's treatment under the confirmed plan, such that the creditor is not an "aggrieved party."

In re Grabanski, 2017 Bankr. LEXIS 3692 (Bankr. N.D. Oct. 24, 2017).

The bankruptcy court has ancillary jurisdiction under § 329 to order fee disgorgement even after dismissal of the case with prejudice. Creditors in the dismissed case are interested parties with standing to seek disgorgement on grounds that the attorney failed to disclose compensation received from the debtors or entities they controlled because any disgorgement would go to the bankruptcy estate and they would get a share, as creditors. Moreover, even if they did not have standing, the court may explore the issue *sua sponte* because it has an independent duty to review fee applications. A state court judgment awarding fees lacks res judicata or Rooker-Feldman effect to prevent disgorgement because it did not address § 329 excessive payment or disclosure issues under the Bankruptcy Code.

Goldsmith v. U.S. Trustee, 2017 U.S. Dist. LEXIS 168618 (D. Nev. Oct. 11, 2017).

The Chapter 11 debtors' first counsel inexcusably failed to diligently or adequately represent the debtors, and the case was closed without plan confirmation. New counsel filed a new case, and the initial one was reopened at the trustee's request to seek compensation disgorgement from the first attorney. The bankruptcy court ordered disgorgement and denied any further fees. On appeal, the district court rejected the attorney's argument that the bankruptcy court should not have decided without an evidentiary hearing or allowing him to conduct discovery because the attorney had declined his opportunity for oral argument and said he had nothing to add to his briefs. The district court further held that the lawyer's Fifth Amendment rights were not violated by retainer disgorgement because the retainer was not his property and the record supported findings that his services provided no value.

Trustee Misconduct

In re Escarcega, 573 B.R. 219 (9th Cir. BAP 2017).

The Ninth Circuit held that if a creditor objects to a plan under § 1325(b)(1)(B), a Chapter 13 debtor must commit to a fixed plan term. *In re Flores*, 735 F.3d 855 (9th Cir. 2013). But debtors in one district sought to modify their plans for an indeterminate duration so they could be completed without modification and the debtor discharged as soon as all priority and secured debt was paid, with unsecured creditors receiving nothing. The Chapter 13 trustee colluded in the work-around of *Flores* by providing debtors' attorneys with a "draft objection" so they could make required amendments outside the court proceeding.

The BAP chastised the Chapter 13 trustee, but held that she did not owe all traditional fiduciary duties of a common law trustee. Nor is the Chapter 13 trustee's primary duty to serve unsecured creditors. Rather, the BAP evaluated the Code duties imposed on Chapter 13 trustees and case law holding that they have a duty to appear and be heard at any confirmation hearing. It held they have a duty to object to plans whenever all requirements are not met, even if no creditor objects. Even though there is no absolute requirement of a fixed-duration plan, the procedure used in these cases skirted the specific procedure for plan modifications.

Creditor Misconduct

In re Freeman-Clay, 2017 WL 3841739 (Bankr. W.D. Mo. Sept. 1, 2017).

A national lender filed proofs of claim with the electronic signature of a person who did not personally review each of them. The lender contended that the signer was familiar with the process of preparing proofs of claim and authorized the use of her signature, and the people who authorized the filing were authorized to do so, and this was sufficient. The court held that the lender violated Rule 3001. But it held that in the absence of bad faith, sanctions would be inappropriate. The lender had ceased the robo-signing practice. It continued to file time-barred claims, but the court held that there were still rights to payment, and the practice was not sanctionable under *Midland Funding L.L.C. v. Johnson*, 137 S.Ct. 1407, 1412 (2017). The lender also had a practice of not attaching necessary copies of documents to its proofs of claim as required by Rule 3001. The court held that the remedy was to strip such proofs of claim of their prima facie validity, not to disallow the claim or impose other sanctions – that would be judicial legislation.

Judicial Estoppel

BPP Illinois, LLC v. Royal Bank of Scotland, 859 F.3d 188 (2d Cir. 2016).

The court upheld dismissal of a reorganized Chapter 11 debtor's complaint on judicial estoppel grounds. The debtor had failed to list a cause of action against a bank for LIBOR-fraud in its schedules before confirmation of its plan. Publicity about the possibility of such a fraud claim had been reported in major publications, and the bank's SEC Form 6-K disclosed that regulators were investigating LIBOR manipulation and the bank was cooperating. Further, the bank had been sued by others before the plan was confirmed.

Slater v. U.S. Steel Corp., 871 F.3d 1174 (11th Cir. 2017).

The district court dismissed a sex and race discrimination lawsuit because the plaintiff did not list it in her Chapter 7 bankruptcy schedules. The Eleventh Circuit initially held that the judicial estoppel doctrine barred the lawsuit. But on en banc review, it held that the district court had to evaluate all relevant facts to determine whether omission of the claim in the bankruptcy schedules was intended to make a mockery of the judicial system. These factors include the plaintiff's level of sophistication, explanation for the omission, whether she subsequently corrected the disclosures, and any action taken by the bankruptcy court concerning the nondisclosure. The court noted a split among the circuits, siding with three. And it expressly noted that the court is not required to accept the debtor's testimony about her intentions.

In this case, the debtor testified that she understood the question in the bankruptcy schedules about lawsuits to ask only about suits filed against her, she amended her filing the day after it was brought to her attention by a defendant's motion to dismiss the litigation, and the

bankruptcy trustee sought to employ the debtor's lawyers to pursue the claims on behalf of the estate. The debtor then converted to Chapter 13, where she could control the lawsuit and terms of any settlement.

II. Professional Fees Update

Fee Reasonableness

In re CWS Enterprises, Inc., 870 F.3d 1106 (9th Cir. 2017).

In this intense family feud case, the fee agreements at issue provided for contingent fees for two law firms for the explicit reason that the client was “without funds to pay hourly fees,” with provisions for arbitration of any dispute relating to the fee agreement. The attorneys succeeded in obtaining a \$30.5 million litigation recovery. An arbitrator heard extensive evidence about fee reasonableness, then decided the fee agreement should be enforced as written, finding it not unconscionable. After a state court judgment confirming the \$2.5 million arbitration award, the client filed Chapter 11. The bankruptcy court took a fresh look at fee reasonableness under § 502(b)(4) and found that the fees should have been only \$440,250.

The district court reversed, and the Ninth Circuit agreed with the district court that § 504(b)(4) does not permit the bankruptcy court to determine the reasonableness of attorney's fee in the first instance, as it must give full faith and credit to the state court's fee approval. Instead, the statute only provides a “reasonableness” cap on the allowance of claims for prepetition services by the debtor's insider or attorney. It held the arbitrator's award, as confirmed by the state court, was entitled to issue preclusive effect.

In re Sundquist, 576 B.R. 858 (Bankr. E.D. Cal. 2017).

The bankruptcy court initially imposed significant sanctions against the debtor's home mortgage lender for willful violations of the automatic stay. *Sundquist v. Bank of America, N.A.*, 566 B.R. 563 (Bankr. E.D. Cal. 2017). It held that the litigating attorney's contingency fee agreement could not be used to determine the fee component of § 363(k) damages, and that the agreement was doctored and back-dated and the contingency fee amount would exceed the reasonable value of services rendered. It awarded \$70,000 in fees, somewhat higher than counsel's lodestar method analysis that she stated would be acceptable. But the attorney then sought to collect more from her client's damages as additional fees and threatened further litigation against the bank.

This opinion explains, with regret, the attorney's lack of competence and resulting burden on the judge to fairly decide the merits, as well as her § 329/Rule 2016 disclosure violations. It also holds that the bankruptcy court has jurisdiction over fee determinations despite closure of the bankruptcy case and is not required to, and should not, abstain to let a state court decide such fees. Nor is counsel entitled to fees on a *quantum meruit* basis. The court held that the attorney was attempting to sabotage a settlement achieved by her former clients through her improper fee collection efforts. *See* 2018 WL 494630 (Bankr. E.D. Ca. Jan. 18, 2018) (ruling on settlement issues). It did not reduce the initial \$70,000 fee award because counsel undertook representation that other lawyers declined and provided a “barely adequate” presentation to enable the court to discern the just result.

In re Fansteel, Inc., 2017 WL 1929489 (Bankr. S.D. Iowa May 9, 2017).

The court reduced the fees charged postpetition by an oversecured creditor whose loan documents provided for payment of the lender's fees and costs, on grounds of unreasonableness. The secured creditor was represented by Weil, Gotshal & Manges plus local counsel and a financial advisor. For the first half-month of the case, the Weil firm charged over \$1 million in fees and costs. The court noted that § 506(b) is "critical to 'policing the urge of an oversecured creditor to release the full force and fury of its advocates against a debtor's efforts to reorganize,'" quoting *In re Latshaw Drilling, LLC*, 481 B.R. 765, 799 (Bankr. N.D. Okla. 2012). The court defined "reasonable" as "fair, proper, or moderate under the circumstances; sensible," quoting BLACK'S LAW DICTIONARY (10th ed. 2014).

Weil did not submit evidence of reasonableness beyond its own lawyers' opinions, and the court found the description of the case as exceedingly complex and "national" in scope to be overstated. The court criticized the firm's internal handling of the case, such as multiple attorneys monitoring audio-recorded hearings telephonically and lawyers doing ministerial tasks, with hourly rates ranging from \$510 to \$1,350. It found the fees "staggering...by any measure," and reduced the fees by approximately half and denied most disbursements without prejudice to submitting additional supporting documentation.

In re United Plastic Recycling, 2017 WL 4404780 (Bankr. M.D. Ala. Sept. 29, 2017).

The owner of a struggling business committed suicide on the eve of the Chapter 11 petition filing, leaving the company with \$6 million in life insurance proceeds. It appeared to the court that the professionals were far less efficient and effective than they should have been, potentially churning their bills, in light of that. The unsecured creditors probably would have been better off with conversion of the case to Chapter 7, as the business sold for just \$80,000 more than its secured debt and significant operating losses were incurred during the marketing period. During this time, DIP counsel spent nearly 1,700 hours working on the case, and special counsel spent substantial time on due diligence unnecessary in a bankruptcy sale context and work duplicative of general bankruptcy counsel's work. Committee counsel spent exorbitant hours monitoring the case and doing nothing to inhibit the demands of the secured creditor. The court reduced all the professionals' fees, with the largest hit to committee counsel's fees. After their 10% voluntary reduction, the court cut their fees by another 40%.

In re ABQ Manufacturing, Inc., 2017 WL 2304226 (Bankr. D.N.M. May 25, 2017).

Even though DIP counsel voluntarily reduced his requested fees by 66%, the court reduced the remaining amount by another 33%. The attorney had repeatedly shown the client's approval on filed documents that the client had not seen, missed court deadlines, submitted documents riddled with errors, and missed the § 1121(e)(2) deadline for filing a small business plan of reorganization. The debtor was forced to retain new counsel, who salvaged the case with the help of a significant creditor.

In re Pursley, 2017 WL 4480235 (Bankr. E.D. Tenn. Oct. 6, 2017).

The Chapter 13 trustee objected to the debtor's attorney's fee of \$3,250 (under the "no look" \$3,750 because of no secured creditors) as excessive because it would represent 51.58% of the total plan payments of \$6,300, providing unsecured creditors with a 30% dividend. The Chapter 13 trustee wanted the fee reduced to \$2,000, bringing the unsecured creditors' dividend

to 44%. The debtor was entitled to a Chapter 7 discharge, and the standard Chapter 7 fee for the debtor's counsel in such a case would have been \$1,750.

The court discussed how a Chapter 13 could be more beneficial to the debtor's attorney than to the debtor and said counsel should be prepared to explain what benefits the longer and more expensive Chapter 13 provides to the client – which could be non-economic, such as the debtor's wish to protect a family member who cosigned a note. The court presented a thorough analysis of the facts in the case and overruled the objections on those facts.

In re Terrill Mfg. Co., 2018 Bankr. LEXIS 65 (Bankr. N.D. Tex. Jan. 11, 2018).

DIP counsel's retainer source disclosure was inaccurate, and he handled the Chapter 11 case incompetently, including using cash collateral without consent. Reorganization was hopeless from the inception of the case, which DIP counsel should have known when the court denied his efforts to recover funds seized by the lender shortly after the filing. Yet he continued to oppose conversion with nothing more than a vague possibility of future financing, driving up administrative expenses. The court held that fees for services provided in the early days of the case should have been allowed, but upheld the bankruptcy court's ruling as to the rest of the fee request being unreasonable.

Fee Collection

In re Wallace, 2017 WL 4773106 (Bankr. D.N.M. Oct. 19, 2017).

The bankruptcy court has jurisdiction to reopen a case to consider the reasonableness of a fee application not filed before case dismissal. Fees must be approved by the court to be an enforceable obligation of the debtor, before or after dismissal.

In re Delta Produce, 845 F.3d 609 (5th Cir. 2016).

Special counsel was engaged to preserve, collect and distribute PACA trust assets under an employment order providing for payment from funds collected. No appeal was taken by anyone from the employment order, but a PACA beneficiary did appeal fee approval orders entered by the bankruptcy court. The Fifth Circuit held that it lacked jurisdiction over interim fee approval orders, and even the district court lacked jurisdiction because its ruling on the merits of the interlocutory appeals was not deemed the grant of a motion for leave to appeal. The court held it had jurisdiction over the final order, but only as to the PACA funds of the appealing PACA claimant that did not consent to special counsel's fee award, because the appellant was only aggrieved to that extent.

While a majority of courts allow PACA producers to recover attorneys' fees related to collection efforts from the PACA trust if entitlement to those fees is included in the sales contract, the court distinguished this from bankruptcy counsel employed under § 327. It held that the lawyer could not be paid until the objecting PACA claimant was paid in full under PACA's unequivocal language requiring that a PACA trustee may not be paid from trust assets "until full payment of the sums owing" is paid to all claimants. 7 U.S.C. § 499e(c)(2).

In re Sweports, Ltd., 565 B.R. 129 (Bankr. N.D. Ill. 2017).

Counsel for a creditors committee supported case dismissal, in the best interest of committee constituents, before it could apply for and obtain approval of fees. The Seventh

Circuit held that the bankruptcy court had jurisdiction to approve fees despite the dismissal. *In re Sweports, Ltd.*, 777 F.3d 364 (7th Cir. 2015). But after the bankruptcy court approved the fee applications on remand, the lawyers had difficulty collecting, including in state court actions. The court held that under the appellate mandate, it had ancillary jurisdiction to tie up loose ends by approving fee applications, but not to order payment. Hence, it lacked jurisdiction to enforce the fee awards through writs of execution.

In re Paris, 568 B.R. 810 (Bankr. C.D. Ca. 2017).

A Chapter 7 trustee's special litigation counsel for personal injury litigation on a contingency stipulated with the state bar to his suspension from practice (following criminal convictions). The trustee found replacement counsel who negotiated a settlement. The court did not allow the suspended lawyer to claim an attorneys' lien on the proceeds. Under state law, he forfeited any lien and entitlement to a share of the litigation settlement because his own acts caused his inability to continue representing the trustee. And he violated his obligations under Code § 329 and Bankruptcy Rule 2014 by not disclosing his asserted attorneys' lien in his employment application, warranting fee denial and disgorgement. Indeed, his application affidavit affirmatively represented under penalty of perjury that he did not hold and would not assert a lien in any recovery realized by the trustee, which the court deemed a judicial admission.

The Binding Effect of a Fee Agreement and Approval Order

Weinberg v. Scott E. Kaplan, LLC, 2017 WL 3588277 (3d Cir. Sept. 14, 2017).

The court upheld dismissal of a malpractice action against DIP counsel for incidents during representation in the Chapter 11 case because the confirmed plan listed an allowed administrative claim for fees and provided for a right to payment on the effective date of the plan. The court held that the fee approval request prior to the plan obligated the bankruptcy court to inquire into the quality of the lawyers' services – which included the disputed incident – and triggered a contested matter although no objection was filed. The court held that the bankruptcy court impliedly found the services rendered were at least acceptable. The debtors should have raised their claim then. And the plan confirmation proceedings provided additional opportunities to challenge the previous fee order or object to confirmation of the payment part of the plan, disclose their intent to file a malpractice action (which was property of the estate), or otherwise advise the court of their discontent. The court also noted that the bankruptcy court, in a unique position to judge the law firm's alleged malpractice, should have been the one to do so. It was unreasonable not to have brought the malpractice claim at the same time in the same bankruptcy forum.

The Aftermath of *Baker Botts*

In re Horne, 876 F.3d 1076 (11th Cir. 2017)

The bankruptcy court awarded damages for an automatic stay violation under § 362(k), including attorneys' fees incurred in litigating the dispute. The district court affirmed and awarded additional fees incurred on appeal, later expanded to include fees in connection with the defendant's efforts to recuse the bankruptcy judge and fees incurred at the circuit level and in resisting a Supreme Court certiorari petition.

The Eleventh Circuit held that § 362(k) authorizes courts to award fees not just through the end of a stay violation, but also fees incurred in pursuing a damages award and defending the

award on appeal, as did the Ninth Circuit in *In re Schwartz-Tallard*, 803 F.3d 1095, 1101 (9th Cir. 2015) (en banc). The court held that § 362(k) is a statutory fee-shifting authorization, such that the *Baker Botts* holding is inapplicable.

In re Nortel Networks, Inc., 2017 WL 932947 (Bankr. D. Del. March 8, 2017).

The Nortel plan provided for payment of \$4.25 million of indenture trustee professional fees, with the balance payable out of the \$150 million distribution to bondholders, which satisfied the claim without postpetition interest. The bankruptcy court in Delaware rejected in substantial part a bondholder request to disallow more than half of their indenture trustee's \$8 million fee claim.

The court limited allowance of fees for matters affecting unsecured creditors generally, such as attendance at creditors committee meetings. But it held the indenture trustee's counsel acted appropriately as a fiduciary when its counsel took a more active role to protect the noteholders' rights in contested proceedings that might have significantly and adversely affected the noteholders' recoveries, instead of relying on committee counsel (even though committee counsel was largely responsible for ultimately resolving the disputes in a global settlement).

The *Nortel* court also allowed the indenture trustee's professional fees incurred in defending the fee objection, distinguishing *Baker Botts LLP v. Asarco LLC*, 135 S. Ct. 2158 (2015) because the indenture contractually obligated the debtor to pay the fees of trustee's counsel and granted the trustee a charging lien on any recovery owed to the noteholders. The court reduced the \$8 million fee claim by \$913,936 and suggested that the noteholders should not have delayed their objections until near the end of the case.

In re Hungry Horse, LLC, 2017 WL 4174359 (Bankr. D.N.M. Sept. 20, 2017)

The court followed the reasoning of *Nortel Networks* and rejected the reasoning of *In re Boomerang Tube, Inc.*, 548 B.R. 69 (Bankr. D. Del. 2016) with respect to *Baker Botts*. It held that an agreement to retain DIP counsel and committee counsel that included such fee commitments could be approved under Section 328. The court suggested sample language that it believed could be acceptable under Section 328:

Fee Defense. The Client agrees to pay all reasonable legal fees and expenses incurred by the Firm, and also by any counsel retained by the unsecured creditors' committee (if one is formed in the Client's bankruptcy case) for successfully defending their respective fee applications. The bankruptcy court must approve all of such fees as reasonable. The Client will have no obligation to pay for any fees or expenses the Firm incurs defending fees that are not allowed.

In re Valence Technology Inc., 2017 WL 4544678 (W.D. Tex. Oct. 10, 2017).

The district court upheld a bankruptcy court's denial of fees incurred in successfully defending through an appeal an attack on an investment banker's success fee by the debtor. The court-approved engagement agreement provided that if the success fee "is not fully paid when due," the debtor agreed "to pay all costs of collection . . . including but not limited to attorney's fees and expenses" The district court reasoned in part that the investment banker's professionals were not themselves approved by the court under Sections 328 or 330. It also interpreted *Baker Botts* as controlling and rejected the investment banker's argument that it was inapplicable because there was a "prevailing-party fee-shifting provision." It was enough for the

court that the banker's attorney's fees and costs, "like those in *ASARCO*, were not incurred for labor performed for, or in service to," the debtor. And the court said the fees were paid when due, because the plan provided for payment upon entry of a final order no longer subject to appeal, and the debtor paid promptly after the Fifth Circuit's decision allowing the fees.

In re Capitol Litho Printing Corp., 573 B.R. 771 (Bankr. D. Ariz. 2017).

A real estate brokerage firm successfully defeated the debtor's challenge to its 4% commission, then sought reimbursement of its attorneys' fees incurred in that effort as provided in its court-approved agreement and an Arizona statute authorizing fee shifting in successful contract litigation. The U.S. Trustee objected on *Baker Botts* grounds. The court declined to follow *Nortel Networks*, noting that the brokerage firm's attorneys were not themselves court-approved, making the case more like *In re Walker Land & Cattle, LLC*, 535 B.R. 348 (Bankr. D. Idaho 2015) and *In re Specialty Plywood, Inc.*, 160 B.R. 627 (9th Cir. BAP 1993), *opinion withdrawn following settlement*, 166 B.R. 153 (9th Cir. BAP 1994). The court also noted that the defense fees were not actual or necessary to the work for which the brokerage firm was specifically employed and did not benefit the estate.

In re Stanton, 569 B.R. 840 (Bankr. N.D. Fla. 2017).

When a Chapter 7 trustee's counsel supplemented his fee application with a more detailed description of his work, as requested by the U.S. Trustee, *Baker Botts* did not preclude the court from allowing fees for the application supplement. It was not a matter of litigating reasonableness, but just providing additional information.

Investment Banker Fees

In re Relativity Fashion, LLC, 2016 WL 8607005 (Bankr. S.D.N.Y. Dec. 16, 2016).

The court rejected challenges by a fee examiner and secured lender to an investment banker's transaction fees. The firm's employment was approved under Code § 328, but with a proviso that the U.S. Trustee retained the rights to object to expenses on all grounds, including reasonableness under § 330 (the "Blackstone Protocol"), with objection rights shared by the creditors committee. The fee examiner objected to the reasonableness of the entire transaction fee for lack of a clear "nexus" between the work performed and the debtors' restructuring. The court held that negotiated transaction fees are an ordinary and important piece of investment bankers' compensation, with a formula approved in advance as part of the retention under § 328, not a discretionary fee enhancement or bonus.

See also In re Digerati Technologies, Inc., 2018 WL 501384 (5th Cir. Jan. 19, 2018), *infra*.

Substantial Contribution Claims

In re Maqsoudi, 566 B.R. 40 (Bankr. C.D. Cal. 2017).

In re Connolly North America LLC, 802 F.3d 810 (6th Cir. 2015) held that a substantial contribution administrative expense claim under § 503(b)(3)(D), which section refers only to Chapters 9 and 11, could be awarded to a creditor in a Chapter 7 case. The creditors in that case had contributed by litigating and causing the removal of a grossly negligent Chapter 7 trustee and recovering substantial funds under a settlement. *Connolly* reasoned that the opening phrase of § 503(b)'s use of "including" renders the following examples non-exclusive. 802 F.3d at 816-

17. And while the U.S. Trustee can generally be expected to protect creditors' interests in Chapter 7 cases, when that does not happen and creditors step in, the court is empowered to reimburse them.

The court followed *Connolly* to approve a substantial contribution claim by a creditor who helped a Chapter 7 trustee recover property that was sold by the trustee and resulted in a surplus estate and creditor distribution. The court rejected the holding of the Ninth Circuit BAP in *In re United Educ. & Software*, 2005 WL 6960237 (9th Cir. BAP 2005) which held that the six examples in § 503(b), which do not use the word "including," are not non-exhaustive. *Id.* at *7. It said that the Ninth Circuit's reasoning in *In re Mark Anthony Constr., Inc.*, 886 F.2d 1101, 1106 (9th Cir. 1989) is consistent with *Connolly*.

In re Sharkey, 2017 WL 5476486 (E.D. Mich. Nov. 15, 2017).

The district court affirmed a bankruptcy court allowance of a substantial contribution claim in a Chapter 13 case. It followed *Connolly*, upholding such claim by a former Chapter 7 trustee (identified as a creditor in the Chapter 13) who challenged the debtor's claimed exemption of annuities during the Chapter 7, with allowance made after conversion to Chapter 13 (when the Chapter 13 trustee did not object to the exemptions but also did not object to the substantial contribution claim). The exemption disallowance enabled all administrative and unsecured creditors to be paid in full with interest. The district court said that, like in *Connolly*, a creditor who steps in when the trustee or U.S. Trustee does not deserves reimbursement as an administrative expense. And it held that *Lamie v. U.S. Tr.*, 540 U.S. 526, 538 (2004) concerned compensation under § 330 and was irrelevant to § 503(b)(3)(D) claims.

In re Community Home Financial Services, Inc., 571 B.R. 714 (Bankr. S.D. Miss. 2017).

The DIP's CEO transferred millions of dollars from the estate to unauthorized accounts in Panama and Costa Rica. A Chapter 11 trustee was appointed, and in due course the CEO was deported to the U.S. and indicted for bank fraud, bankruptcy fraud and wire fraud. The CEO's criminal defense attorney filed a substantial contribution claim for his own work in recovering and turning over some of the funds (for which his CEO client got credit toward his criminal restitution order). The court held that only an "entity" can make a § 503(b)(4) contribution claim, not the attorney employed by the entity; the CEO made no such motion even if he were to qualify as an entity. And the return of stolen funds should be expected of a fiduciary and thus not an activity constituting a substantial contribution. Further, criminal defense counsel fees are presumed noncompensable from estate funds, and the recovery was less than the amount stolen and not a net contribution to the estate.

In re Fontainebleau Las Vegas Holdings, LLC, 2017 WL 3503659 (Bankr. S.D. Fla. Aug. 15, 2017).

After an examiner's counsel was paid in full pursuant to a court order entered after conversion to Chapter 7, an appellate decision in a lien priority dispute ordered disgorgement of previously-paid professional fees pending adjudication of the lien dispute. Thereafter, examiner's counsel incurred additional fees at the district court and court of appeals (where the disgorgement issue settled). The court held that the examiner's counsel could not be paid for such additional fees incurred post-conversion under *Lamie v. U.S. Tr.*, 540 U.S. 526, 538 (2004). And § 503(b)(4), which allows for an administrative expense to counsel for a creditor who has

made a substantial contribution in a case under Chapter 9 or 11, is not applicable in a Chapter 7 case.

Chapter 13 “No-Look” Fees

In re Riley, 2017 WL 4404284 (Bankr. W.D. La. (Sept. 29, 2017)).

The court held that Chapter 13 counsel cannot be reimbursed for advancing filing and credit-counseling fees on top of a “no-look” fee. The district adopted a new rule that did not expressly require that such reimbursement be included in the no-look fee, unlike the previous local rule, and practitioners began adding the amounts to their fee applications. The court noted that “virtually all” Chapter 13 attorneys in the district filed “no-money-down” cases where the lawyer paid the filing fee, the credit-counseling fee, and the fee for a credit report.

The court reasoned that the fees to be reimbursed are not an administrative expense under Section 503(b)(1)(A), because they are “prepetition expenses of the debtor, not the estate.” The reimbursement obligation arises from the pre-petition retention agreement between the debtor and the attorney, not “from a transaction with the debtor’s bankruptcy estate.” And the expenses advanced by the lawyer do “not provide a direct and substantial benefit to the estate.” The cost of filing fees cannot be shifted to the estate unless the debtor obtains an order authorizing the payment of the filing fees in installments.