UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa

In the Matter of	:	
	:	
ROSE WAY, INC.,	:	Case No. 89-1273-C H
DOUBLE-D LEASING, INC.,	:	89-1274-C H
DOUBLE-D, INC.,	:	89-1275-C H
	:	
Debtors.	:	Chapter 11
	:	

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ORDER--APPLICATIONS FOR ALLOWANCE OF ATTORNEYS FEES AND EXPENSES

On October 3, 1989, a hearing was held on the application for allowance of attorneys' fees and expenses. The following attorneys appeared on behalf of their respective clients: T. J. McDonough and Dennis W. Johnson for Brick, Seckington, Bowers, Schwartz and Gentry, P.C. (hereinafter "Brick, Seckington"); Donald F. Neiman for Exchange National Bank of Chicago (hereinafter "Exchange"); John Waters for U.S. Trustee; and Russell E. Dougherty, pro se. At the conclusion of said hearing, the Court took the matter under advisement. The Court considers the matter fully submitted.

This is a core proceeding pursuant to 28 U.S.C. §157(b)(2)(A). The Court, upon review of the application, responses thereto, evidence admitted and arguments of counsel, now enters its findings and conclusions pursuant to Fed.R.Bankr.P. 7052.

FINDINGS OF FACT

1. On June 8, 1989, Rose Way, Inc., Double-D Leasing, Inc., and Double-D, Inc. (hereinafter "Rose Way") filed its

voluntary Chapter 11 petitions.

2. On June 8, 1989, Rose Way filed its application to employ Brick, Seckington as counsel for Rose Way. The application was signed by David C. Rosenberger, Chairman of the Board of Rose Way. The application stated that Brick, Seckington held “no connection with any of [Rose Way’s] creditors or with any other party in interest or their respective attorneys which would be detrimental to the interests of the estate or creditors or other claimants against the Debtor.”

3. On June 8, 1989, an affidavit was filed with the Court by attorney T. J. McDonough as required by §329 and Fed.R.Bankr.P. 2014 in which T. J. McDonough asserted that "I and the firm which I am associated (Brick, Seckington) represent no interest adverse to Rose Way, Inc., as debtor in possession, or its estate in the matters upon which we are to be engaged."

4. On June 8, 1989, Rose Way filed with its Chapter 11 Petition a list of 10 largest unsecured creditors as required by Fed.R.Bankr.P. 1007(d) and Local Administrative Order X-1(d). The list indicated that Brick, Seckington held an unsecured claim of $76,087.49, the second largest unsecured claim listed by Rose Way.

5. On June 9 and June 12, 1989, the Court conducted emergency telephonic hearings on the use of cash collateral.

At these hearing, Exchange and the U.S. Trustee raised concerns to the Court as to the apparent conflict of interest in Brick, Seckington representing Rose Way. Brick, Seckington responded that no substantial conflict existed on account of Brick, Seckington's pre-petition representation of Rose Way. Brick, Seckington also responded that Brick, Seckington's representation of David Rosenberger and his wife, Doris, the sole equity security holders of Rose Way, did not constitute a conflict.

6. David and/or Doris Rosenberger have personally guaranteed a substantial amount of the Rose Way debt, including debt to NCNB, Ford Leasing, GECC, FBS Leasing and Signal Capital Corporation. Certain real estate owned by David and Doris Rosenberger secures, in part, the claim of Exchange. On Schedule B-2 of Rose Way's schedules filed July 7, 1989, Rose Way lists a David Rosenberger account receivable of $637,123.69.

7. On June 8, 1989, the date Rose Way filed its Chapter 11 petitions, application to employ attorney and affidavit of T.J McDonough, Larry Seckington, a member of Brick, Seckington, served as a director of Rose Way.

8. In response to the concerns raised by Exchange and the U.S. Trustee, the Court ordered Rose Way to give notice of the application to employ to all parties in interest and to provide notice of a bar date for objections to the application

to employ.

9. On June 19, 1989, Rose Way served notice of the application to employ counsel upon all interested parties and set forth therein that any objections to the application were to be filed no later than July 6, 1989.

10. On June 19, 1989, Brick, Seckington filed a motion to withdraw as counsel.

11. On June 20, 1989, the Court entered an order allowing the withdrawal of Brick, Seckington as counsel for Rose Way.

12. At no time did the Court enter an order approving Rose Way's retention of Brick, Seckington as counsel for Rose Way.

13. On June 19, 1989, the Court entered an order authorizing Rose Way to employ Frederickson and Byron and Ahlers, Cooney, Dorweiler, Haynie, Smith and Albee, P.C. as counsel for Rose Way.

14. On July 26, 1989, Brick, Seckington filed an application for allowance of attorneys' fees and expenses requesting that the Court direct that Rose Way pay to Brick, Seckington $17,962.79 ($19,462.79 less a $1,500.00 pre-petition retainer) for fees and expenses owing as a result of the services provided to Rose Way.

DISCUSSION

A. Conflict of Interest

Section 327(a) provides in pertinent part:

> (a) Except as otherwise provided in this section, the trustee, with the court's approval, may employ one or more attorneys ... that do not hold or represent an interest adverse to the estate, and that are disinterested persons, to represent or assist the trustee in carrying out the trustee's duties under this Title.

Section 328 (c) provides in pertinent part:

> (c) Except as provided in ... §1107(b) of this Title, the court may deny allowance of compensation for services and reimbursement of expenses of a professional person employed under §327 or 1103 of this Title if, at any time during such professional person's employment under §327 or 1103 of this Title, such professional person is not a disinterested person, or represents or holds an interest adverse to the interest of the estate with respect to the matter on which such professional person is employed.

Section 1107(b) provides in pertinent part:

> (b) Notwithstanding § 327(a) of this title, a person is not disqualified for employment under § 327 of this Title by a debtor-in-possession solely because of such person's employment by or representation of the debtor before the commencement of the case.

Section 101(13) provides in pertinent part:

> (13) "Disinterested person" means person
>
> that— -
>
> (A) is not a creditor, an equity security holder, or an insider . . .
>
> (D) is not and was not, within two

> years before the date of filing of the petition, a director . . . of the debtor.

If a professional is a creditor of the debtor, then that professional is not disinterested under §101(13) and is subject to disqualification under §327(a). In re Pierce, 809 F.2d 1356, 1362 (8th Cir. 1987). A bankruptcy court has the authority to deny a professional's post-petition fees pursuant to §328(c) when the professional fails to meet the definition of a disinterested person under §101(13). Pierce, 809 F.2d at 1362.

An attorney who represents debtor-in-possession, and also represents an individual who is a potential debtor of the debtor-in-possession, represents an interest adverse to the estate. Roger J. Au & son, Inc. v. Aetna Insurance Co., (In re Roger J. Au & Son, Inc.), 64 B.R. 600, 605 (N.D. Ohio 1986). Although representation of the debtor and principals of the debtor may not always be grounds for disqualification, disqualification is certainly required where the principals and the debtor hold interests which are directly adverse. In re Star Broadcasting, Inc., 81 B.R. 835 (Bankr. D.N.J. 1988).

In the matter ***sub judice***, Brick, Seckington listed itself as the second largest unsecured creditor on the list of 10 largest unsecured creditors filed June 8, 1989. Further, Larry Seckington, a member of Brick, Seckington, served on the Rose Way board of directors. Finally, Brick, Seckington

represented David and Doris Rosenberger, who have a scheduled account receivable due to Rose Way of $637,123.69; are the sole equity security holders of Rose Way; and the guarantors of a substantial amount of Rose Way's debt. Therefore, while performing the services listed on Brick, Seckington's fee application, Brick, Seckington was not disinterested under §101(13) and represented an interest adverse to the Rose Way estate. The Court thus denies Brick, Seckington's fee application under §328(c).

Brick, Seckington asserts that the court should adopt an expansive interpretation of §1107(b), citing In re Best Western Heritage & Partnership, 79 B.R. 736 (Bankr. E.D. Tenn. 1987) and In re Viking Ranches, 89 B.R. 113 (Bankr. C.D. Calif. 1988). However, it is clear that the Eighth Circuit has not adopted this expansive interpretation. See Pierce, 809 F.2d at 1362, n. 18. The Court follows the Eighth Circuit position outlined in Pierce and does not deny Brick, Seckington's fee application solely because Brick, Seckington represented Rose Way pre-petition. Rather, the Court denies Brick, Seckington's fee application because Brick, Seckington is not disinterested and represented an interest adverse to the Rose Way estate.

B. Nondisclosure

Bankruptcy Rule Procedure 2014(a) provides in pertinent part:

> (a) An order approving the employment of attorneys ... pursuant to § 327 or 1103 of the Code shall be made only on application of the trustee ... stating the specific facts showing the necessity for the employment, the name of the person to be employed, the reasons for the selection, the professional services to be rendered, any proposed arrangement for compensation, and, to the best of applicant's knowledge, all of the person's connection with the debtor, creditors, or any other party in interest, the respective attorneys and accountants. The application shall be accompanied by a verified statement of the person to be employed setting forth the person's connections with the debtor, creditors, or any other party in interest, their respective attorneys and accountants.

Nondisclosure of an attorney's connections with the debtor is a violation of the disclosure requirements of §328(a) and B.R. 2014(a), and constitutes a separate independent ground for denying attorney's fees. Pierce, 809 F.2d at 1363. Many courts have denied compensation to professionals where, in addition to other factors, the professional fails to previously disclose a relationship with the debtor that could have presented a potential area of conflict. See e.g. In re Gray, 64 B.R. 505, 508 (Bankr. E.D. Mich. 1986); In re Roberts, 46 B.R. 815, 850 (Bankr. D. Utah 1985); In re Patterson, 53 B.R. 366, 373 (Bankr. D. Neb. 1985); In re Guy Apple Masonry Contractor, Inc., 45 B.R. 160, 162 (Bankr. D. Ariz. 1984). Neither the bankruptcy court nor

the trustee have the responsibility of culling through the often voluminous material filed with the bankruptcy court in order to ascertain every possible conflict of interest in a particular case, especially when a professional's potential conflicts are required to be disclosed in the professional's application. Pierce, 809 F.2d at 1363, n. 20.

The application to employ attorney filed by Brick, Seckington as counsel for Rose Way, stated that Brick, Seckington held "no connection with any of [Rose Way's] creditors or with any other party in interest or their respective attorneys which would be detrimental to the interest of the estate or creditors or other claimants against the debtor." In addition, in an affidavit by attorney T.J. McDonough filed with the Court on June 8, 1989, T. J. McDonough asserted that "I and the firm which I am associated represent no interests adverse to Rose Way, Inc., as debtor-in- possession, or its estate in the matters in which we are to be engaged." Neither the application to employ counsel nor the T.J. McDonough affidavit disclosed Brick, Seckington's status as the second largest unsecured creditor, Larry Seckington's position as a director of Rose Way, or the potential conflicts due to Brick, Seckington's representation of Rosenbergers. As stated by the Eighth Circuit Court of Appeals in Pierce, this constitutes a classic violation of the disclosure requirements of the Bankruptcy Code and Bankruptcy

Rules of Procedure, and constitutes an independent ground for denial of fees to Brick, Seckington.

Brick, Seckington asserts that its listing of Brick, Seckington on the list of 10 largest unsecured creditors is sufficient disclosure of the unsecured claim of Brick, Seckington. However, the Eighth Circuit specifically rejected this argument in Pierce, 809 F.2d at 1363, n. 20. Brick, Seckington also asserts that T.J. McDonough, the attorney who filed the application for Brick, Seckington and Rose Way, was unaware of the status of Larry Seckington as a director of Rose Way. However, as a member of Brick, Seckington, T.J. McDonough had a duty to investigate any conflicts which other members of the firm might have. The fact that the failure to disclose may have been unintentional does not constitute an excuse. In re Coastal Equities, 39 B.R. 304, 308 (Bankr. S.D. Calif. 1984). Finally, Brick, Seckington asserts that T. J. McDonough was ignorant of the fact that Brick, Seckington's connections with Rose Way constituted actual conflicts of interest disqualifying Brick, Seckington from employment. However, Brick, Seckington's obligation was to disclose all connections between Brick, Seckington and Rose Way. The disclosure requirement is not limited to those items which create an actual conflict of interest. It is the duty of the attorney to reveal all connections. The disclosure rules do not give the attorney the right to withhold certain

information on that grounds that, in the attorney's opinion, the connection is of no consequence or not adverse. If the duty to disclose is neglected, however innocently, the attorney performs services at his peril. Coastal Equities, 39 B.R. at 308.

C. Nunc Pro Tunc Order

Brick, Seckington seeks a nunc pro tunc order approving its employment and fee application. Entry of a nunc pro tunc order approving employment requires exceptional circumstances. Matter of Independent Sales Corp., 73 B.R. 772 (Bankr. S.D. Iowa 1987); All Iowa Transport Services, Inc., (Bankr. S.D. Iowa), No. 85-364-C unpub. Op. April 7, 1988. As stated supra, Brick, Seckington does not qualify for employment under §327(a). Therefore, Brick Seckington's request for nun pro tunc approval of its employment and fee application is moot. See Pierce, 809 F.2d at 1363. Brick, Seckington is not entitled to nunc pro tunc approval of employment and its fee application.

D. Fees and Costs Subject to Denial

If a professional person is not a disinterested person, represents or holds an interest adverse to the interest of the estate or violates the disclosure requirements, the court may deny the professional fees and costs. See §328(c); In re Pierce, 53 B.R. 826, 829 (Bankr. D. Minn. 1985) aff'd Pierce,

809 F.2d 1356 (8th Cir. 1987). The Court therefore denies Brick, Seckington's fees and costs.

E. Pre-petition Fees and Expenses

Prior court approval under §327(a) is not necessary as to pre-petition services. Kressel v. Kotz, 34 B.R. 388 (D. Minn. 1983), aff'd in Kotz v. Westfall, 746 F.2d 1329 (8th Cir. 1984). However, as indicated by §329 and B.R. 2017, the compensation drawn for such pre-petition services and costs is subject to court scrutiny and must be reasonable. Matter of Independent Sales Corp., 73 B.R. 772, 779 (Bankr. S.D. Iowa 1987); Kressel v. Kotz, 34 B.R. at 392. Further, because prior court approval is not necessary as to the pre-petition services, the fees for pre-petition services are clearly not compensable as an administrative expense under §503(b)(2).[1]

The Court finds that $5,730.50 in fees and $1,500.00 in expenses incurred by Brick, Seckington through June 7, 1989, are reasonable and are unsecured claims of Brick, Seckington. Brick, Seckington must file an application with the Court itemizing the June 8, 1989 services and photocopy, messenger, postage, telephone, telefax, and travel expenses it incurred pre-petition in order to have those fees and expenses considered an unsecured claim of Brick, Seckington. Further, Brick, Seckington must reimburse the Rose Way estate for the

[1] The issue of whether a claim for pre-petition services rendered in the bankruptcy cases is an unsecured claim or an administrative expense was not before the Eighth Circuit in Pierce. Pierce, 809 F.2d at 1359, n.10.

$1,500.00 retainer applied to the filing fee expense.

IT IS ACCORDINGLY ORDERED as follows:

1) Brick, Seckington's July 26, 1989 application for fees and expenses is denied.

2) Brick, Seckington has an unsecured claim of $7,230.50 for $5,730.50 in fees and $1,500.00 in expenses incurred through June 7, 1989.

3) In order to have an unsecured claim for further pre-petition expenses and June 8, 1989 fees incurred pre-petition, Brick, Seckington must file an application with the Court itemizing those June 8, 1989 services performed pre-petition and those expenses incurred pre-petition.

4) Brick, Seckington must make a payment of $1,500.00 to the Rose Way estate as reimbursement for the $1,500.00 retainer applied to expenses incurred by Brick, Seckington.

Dated this ____21st_____ day of March, 1990.

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Russell J. Hill
U.S. Bankruptcy Judge