

UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa

In the Matter of :
 :
SCOTTISH LINKS, INC., : Case No. 90-2243-W H
 : Chapter 11
Debtor. :
 :

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ORDER--APPLICATION FOR EMPLOYMENT OF COUNSEL

On October 31, 1990, Debtor's application for approval of employment of the law firm of Laughlin, Peterson and Lang ("Laughlin Firm"), as counsel for Debtor was heard. Mark L. Laughlin, Laughlin Firm, appeared for Debtor-in-Possession Scottish Links, Inc. ("Scottish Links"); Peter J. Peters, of Peter J. Peters, P.C., appeared for Bill D. Campbell; and John Waters appeared for the United States Trustee.

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

FINDINGS

1. Scottish Links filed a voluntary petition pursuant to Chapter 11 of the Bankruptcy Code on August 28, 1990, and is the Debtor-in-Possession.
2. Scottish Links filed its application for order approving the employment of the Laughlin Firm to represent the

estate on September 24, 1990.

3. Said application reveals that the Laughlin firm also represents McIntosh and Co., a related entity.

4. McIntosh and Co. is the Debtor-in-Possession in a separate Chapter 11 bankruptcy proceeding pending in the Southern District of Iowa, Bankruptcy No. 90-2155-W.

5. McIntosh and Co. has also filed an application to employ the Laughlin Firm as counsel in that case.

6. Scottish Links lists McIntosh and Co. as its sole equity security holder. Bill D. Campbell contends and alleges that he is the owner of 50 percent of the stock of Scottish Links, and McIntosh and Co. is the owner of the remaining 50 percent of the stock. These issues have been raised by Bill Campbell's motion to dismiss which is pending herein.

7. Scottish Links has listed McIntosh and Co. as a secured creditor with a real estate mortgage in the amount of \$287,840.00. McIntosh and Co.'s schedules list a receivable from Scottish Links in the amount of \$130,468.82. Accordingly, the amount of McIntosh and Co.'s claim may be subject to dispute, equitable subordination and classification as a capital contribution.

8. Scottish Links lists Turnbridge Limited Partnership (herein "Turnbridge") as an unsecured creditor in the amount of \$150,000.00. McRealty, Inc., a wholly owned subsidiary of McIntosh and Co., is a general partner of Turnbridge. Melvin

McIntosh, Chairman of the Board of McIntosh and Co., is a partner in Turnbridge. Turnbridge's claim in the scheduled amount of \$150,000.00 is based on an oral agreement to reimburse Turnbridge for improvements benefitting Scottish Links. This claim may be subject to objection or an action for equitable subordination.

9. Prior to the filing of the Scottish Links petition, the bank account of Scottish Links was attached by writ and Scottish Links began depositing receipts into the bank account of MFS, Inc., a wholly owned subsidiary of McIntosh and Co. This procedure continued until the first meeting of creditors in this case. Deposit of these funds in the MFS account could cause an action for turnover or avoidance as a fraudulent conveyance.

10. Scottish Links' Statement of Affairs reveals that Scottish Links issued \$50,000.00 worth of mortgage participation notes to John and Nell Aita in exchange for the surrender of \$50,000.00 worth of McIntosh and Co. debentures.

The Aitas appear to have moved from an unsecured position in McIntosh and Co. to a secured position in Scottish Links and there are consequent issues as to whether the Aitas exchanged worthless debentures for a valuable secured interest in Scottish Links real estate.

11. Stephen M. McIntosh has signed both Chapter 11 petitions as the president of Scottish Links and the Vice

Chairman of McIntosh and Co.

DISCUSSION

11 U.S.C. §327 provides in pertinent part:

(a) Except as otherwise provided in this section, the trustee, with the court's approval, may employ one 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.

...

(c) In a case under Chapter 7, 12, or 11 of this title, a person is not disqualified for employment under this section solely because of such person's employment by or representation of a creditor, unless there is objection by another creditor or the United States Trustee, in which case the court shall disapprove such employment if there is an actual conflict of interest.

The qualification requirements of 11 U.S.C. §327 apply to a Chapter 11 debtor-in-possession. In re Star Broadcasting, Inc., 81 B.R. 835, 838 (Bankr. D.N.J. 1988).

The Bankruptcy Code does not state a definition of "representing an interest adverse to the estate," but case law provides a definition. Several courts have defined representing an interest adverse to the estate as serving as an attorney for a person possessing: (1) an economic interest

that would tend to lessen the value of the bankruptcy estate or that would create either an actual or potential dispute in which the estate is a rival claimant; or (2) a predisposition under circumstances that render such a bias against the estate. Star Broadcasting, Inc., 81 B.R. at 838; Roger J. Au & Son, Inc. v. Aetna Insurance Company (In re Roger J. Au & Son, Inc.), 64 B.R. 600, 604 (N.D. Ohio 1986); In re Roberts, 46 B.R. 815, 822-23 (Bankr. D. Utah 1985). Therefore, the question before the Court is whether the Laughlin Firm, through its representation of McIntosh and Co., represents a person holding an interest that might reduce the value of the Scottish Links estate, might result in a dispute with the Scottish Links estate, or might cause bias against the Scottish Links estate.

The American Bar Association Code of Professional Responsibility provides a separate basis for attorney disqualification. See State of Arkansas v. Dean Foods Products Co., Inc., 605 F.2d 380 (8th Cir. 1979); Fred Weber, Inc. v Shell Oil Co., 566 F.2d 602 (8th Cir. 1977), cert. den. 436 U.S. 905 (1978).¹ The Iowa Code of Professional Responsibility, adopted by the Iowa Supreme Court, has

¹Both Dean Foods and Fred Weber were overruled on grounds unrelated to attorney disqualification by In re Multi-Piece Rim Products Liability, 612 F.2d 377 (8th Cir. 1980). EZ Paintr Corp. v. Padco, Inc., 746 F.2d 1459, 1461 (Fed. Cir. 1984); Hallmark Cards, Inc. v. Hallmark Dodge, Inc., 616 F.Supp. 516, 520 (W.D. Mo. 1985).

incorporated virtually all of the provisions of the ABA Code.

Canon 9 of the ABA Code is incorporated into the Iowa Code of Professional Responsibility. Canon 9 provides: "a lawyer should avoid even the appearance of professional impropriety."

Thus, the Court must also determine whether a member of the public or of the bar would see an impropriety in the Laughlin Firm's representation of Scottish Links and McIntosh and Co.

In the instant case, the Court finds that the following circumstances disqualify the Laughlin Firm from representing Scottish Links:

1. McIntosh and Co. is an equity security holder of Scottish Links, with the percentage of equity held by McIntosh and Co. subject to dispute;
2. McIntosh and Co. is a creditor of Scottish Links, and the amount of McIntosh and Co.'s claim may be subject to dispute, equitable subordination and classification as a capital contribution;
3. McRealty, Inc. (a wholly owned subsidiary of McIntosh and Co.) and Melvin McIntosh (Chairman of the Board of McIntosh and Co.) are partners in Turnbridge, an unsecured creditor of Scottish Links. The Turnbridge claim may be subject to objection or an action for equitable subordination;
4. the funds deposited by Scottish Links into the bank account of MFS, Inc. (a wholly owned subsidiary of McIntosh and Co.) could cause an action for turnover or avoidance as a fraudulent conveyance; and
5. there are issues as to whether the Aitas exchanged worthless McIntosh and Co. debentures for a valuable secured interest in Scottish Links real estate.

The above-described circumstances establish that McIntosh

and Co. holds an interest that might reduce the value of the Scottish Links estate, might result in a dispute with the Scottish Links estate, and might cause bias against the Scottish Links estate. Therefore, McIntosh and Co. holds an interest adverse to the Scottish Links estate, and the Laughlin Firm's representation of McIntosh and Co. disqualifies the Laughlin Firm from representing Scottish Links under 11 U.S.C. §327.

Further, due to the circumstances described above, a member of the public or of the bar could see impropriety in the Laughlin Firm's simultaneous representation of McIntosh and Co. and Scottish Links, and said simultaneous representation is not in compliance with Canon 9 of the Iowa Code of Professional Responsibility. Finally, the Court finds that an actual conflict would exist if the Laughlin Firm simultaneously represented Scottish Links and McIntosh and Co., an equity security holder and creditor of Scottish Links, and a debtor-in-possession in a separate Chapter 11 case. See In re Hoffman, 53 B.R. 564, 566 (Bankr. W.D. Ark. 1985).

IT IS ACCORDINGLY ORDERED that the Scottish Links application for employment of the Laughlin Firm is denied.

Dated this 10th day of December, 1990.

RUSSELL J. HILL
U.S. BANKRUPTCY JUDGE