NAVIGATING ETHICS TRAPS in BANKRUPTCY

Bench-Bar Retreat

October 11, 2019

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ATTORNEY FEES

Ohio Rule of Professional Conduct 1.5

1. "Zero Down" bankruptcies
    a. bifurcation of cases: bankruptcy financing companies
2. Post filing services and fees: dischargeability and collection of fees
3. 2016 Disclosure

Hypothetical 1:

Mr. Sadd is being garnished and has no funds to pay for a bankruptcy (and stop the garnishment). Can you bifurcate his case and get paid after the case is filed? Can you involve a third party to collect? What if Mr. Sadd is paying the filing fee by installment payments?

Hypothetical 2:

You meet with John Q. Client who is dissatisfied with his current chapter 13 attorney. How can you get paid in an already filed 7 or 13?

BANKRUPTCY PLANNING

Ohio Rule of Professional Conduct 1.2

1. Preferences and Fraudulent Transfers:
    a. Can you unwind a transfer?
    b. Can you return a gift or retitle an asset?
2. Advising clients regarding new debt before filing
3. Converting Non-exempt assets to exempt assets

Hypothetical 1:

Mrs. Green has some stocks and bonds that are not protected in a retirement account. These would be assets for the trustee if the case were filed immediately. What can you advice Mrs. Green to do? Can she put money in an IRA? Pay for medical treatment? Make home improvements? Can she buy a car with the cash?

Hypothetical 2:

Mr. Hall discloses at the initial meeting that he has paid back his mother $1800 over the last 12 months ($150/month) for money loaned. Can mom give back the money? What can you advise regarding the disclosure?

Hypothetical 3:

Husband and wife quit claim their property to wife only. What if husband then files a bankruptcy? Can they undo the transfer prior to filing?

Hypothetical 4:

Mr. and Mrs. Frugal have good incomes and live frugally, but found themselves in debt due to medical debt resulting from illness. They have two vehicles that are both 12 years old. They do not qualify for a chapter 7 without more secured debt payments.

Can you advise them to purchase vehicles prior to filing? Can you advise them to tithe more to church or to assist elderly family members?

RESPONSIBILITY AS A MEMBER OF THE BAR

Ohio Rule of Professional Conduct 8.3 and 8.4

1. What is your responsibility to the bar and to the process when you see an inexperienced attorney struggling?
2. Duty to report misconduct generally

Hypothetical:

You are waiting with your client while a 341 hearing is held. You notice many errors by the counsel of record that appear to adversely affect the debtor's case. Should you approach counsel after the 341?

LATE DISCLOSURE BY CLIENT

Ohio Rule of Professional Conduct 1.16, 4.1

1. Pre-341
2. During the 341
3. Post 341

What is the duty to report errors, misstatements or omissions by a client?

Hypothetical 1:

You file a chapter 13 for a client who subsequently becomes entitled to inherit real estate. The debtor does not inform you of this until the case is confirmed. What is your responsibility in this case?

Hypothetical 2:

What if the debtor informs you after the 341 that he has a vehicle but that he didn't list it because there is no lien on it? What steps must you take in this situation?

CONFLICTS OF INTEREST & SANCTIONS

Ohio Rule of Professional Conduct 1.7 through 1.13

1. Conflicts in commercial representations
    a. Creditors – where is the line for disinterestedness
    b. Shareholders – when should you start unraveling the representation
    c. Judges are people too and may have the appearance of conflicts
    d. Prior work conflicts – should you continue representation once a malpractice claim may exist, e.g., after a mistake

2. Sanctions
    a. Bankruptcy judges have power to issue them even in discovery matters
    b. Claim issues – do you have the proper documentation, did you give court notice of assignment
    c. Careful to perform appropriate due diligence in collection actions as CFPB still exists and is watching

RULE 1.16: DECLINING OR TERMINATING REPRESENTATION

(a) Subject to divisions (c), (d), and (e) of this rule, a lawyer shall not represent a client or, where representation has commenced, shall withdraw from the representation of a client if any of the following applies:

(1) the representation will result in violation of the Ohio Rules of Professional Conduct or other law;

(2) the lawyer's physical or mental condition materially impairs the lawyer's ability to represent the client;

(3) the lawyer is discharged.

(b) Subject to divisions (c), (d), and (e) of this rule, a lawyer may withdraw from the representation of a client if any of the following applies:

(1) withdrawal can be accomplished without material adverse effect on the interests of the client;

(2) the client persists in a course of action involving the lawyer's services that the lawyer *reasonably believes* is *illegal* or *fraudulent*;

(3) the client has used the lawyer's services to perpetrate a crime or *fraud*;

(4) the client insists upon taking action that the lawyer considers repugnant or with which the lawyer has a fundamental disagreement;

(5) the client fails *substantially* to fulfill an obligation, financial or otherwise, to the lawyer regarding the lawyer's services and has been given *reasonable* warning that the lawyer will withdraw unless the obligation is fulfilled;

(6) the representation will result in an unreasonable financial burden on the lawyer or has been rendered unreasonably difficult by the client;

(7) the client gives *informed consent* to termination of the representation;

(8) the lawyer sells the law practice in accordance with Rule 1.17;

(9) other good cause for withdrawal exists.

(c) If permission for withdrawal from employment is required by the rules of a *tribunal*, a lawyer shall not withdraw from employment in a proceeding before that *tribunal* without its permission.

(d) As part of the termination of representation, a lawyer shall take steps, to the extent *reasonably* practicable, to protect a client's interest. The steps include giving due notice to the client, allowing *reasonable* time for employment of other counsel, delivering to the client all papers and property to which the client is entitled, and complying with applicable laws and rules. Client papers and property shall be promptly delivered to the client. "Client papers and property" may include correspondence, pleadings, deposition transcripts, exhibits, physical evidence, expert reports, and other items *reasonably* necessary to the client's representation.

(e) A lawyer who withdraws from employment shall refund promptly any part of a fee paid in advance that has not been earned, except when withdrawal is pursuant to Rule 1.17.

Comment

[1] A lawyer shall not accept representation in a matter unless it can be performed competently, promptly, without improper conflict of interest, and to completion. Ordinarily, a representation in a matter is completed when the agreed-upon assistance has been concluded. See Rules 1.2(c) and 6.5. See also Rule 1.3, Comment [4].

Mandatory Withdrawal

[2] A lawyer ordinarily must decline or withdraw from representation if the client demands that the lawyer engage in conduct that is illegal or violates the Ohio Rules of Professional Conduct or other law. The lawyer is not obliged to decline or withdraw simply because the client suggests such a course of conduct; a client may make such a suggestion in the hope that a lawyer will not be constrained by a professional obligation.

[3] When a lawyer has been appointed to represent a client, withdrawal ordinarily requires approval of the appointing authority. See also Rule 6.2. Similarly, court approval or notice to the court is often required by applicable law before a lawyer withdraws from pending litigation. Difficulty may be encountered if withdrawal is based on the client's demand that the lawyer engage in unprofessional conduct. The court may request an explanation for the withdrawal, while the lawyer may be bound to keep confidential the facts that would constitute such an explanation. The lawyer's statement that professional considerations require termination of the representation ordinarily should be accepted as sufficient. Lawyers should be mindful of their obligations to both clients and the court under Rules 1.6 and 3.3.

Discharge

[4] A client has a right to discharge a lawyer at any time, with or without cause, subject to liability for payment for the lawyer's services. Where future dispute about the discharge may be anticipated, it may be advisable to prepare a written statement reciting the circumstances.

[5] Whether a client can discharge appointed counsel may depend on applicable law. A client seeking to do so should be given a full explanation of the consequences. These consequences may include a decision by the appointing authority that appointment of successor counsel is unjustified, thus requiring self-representation by the client.

[6] If the client has severely diminished capacity, the client may lack the legal capacity to discharge the lawyer, and in any event the discharge may be seriously adverse to the client's interests. The lawyer should make special effort to help the client consider the consequences and may take reasonably necessary protective action as provided in Rule 1.14.

Optional Withdrawal

[7] A lawyer may withdraw from representation in some circumstances. The lawyer has the option to withdraw if it can be accomplished without material adverse effect on the client's interests. Withdrawal is also justified if the client persists in a course of action that the lawyer reasonably believes is illegal or fraudulent, for a lawyer is not required to be associated with such conduct even if the lawyer does not further it. Withdrawal is also permitted if the lawyer's services were misused in the past even if that would materially prejudice the client. The lawyer may also withdraw where the client insists on taking action that the lawyer considers repugnant or with which the lawyer has a fundamental disagreement.

[8] A lawyer may withdraw if the client refuses to abide by the terms of an agreement relating to the representation, such as an agreement concerning fees or court costs or an agreement limiting the objectives of the representation.

Assisting the Client upon Withdrawal

[8A] A decision by a lawyer to withdraw should be made only on the basis of compelling circumstances, and in a matter pending before a tribunal he must comply with the rules of the tribunal regarding withdrawal. A lawyer should not withdraw without considering carefully and endeavoring to minimize the possible adverse effect on the rights of the client and the possibility of prejudice to the client as a result of the withdrawal. Even when the lawyer justifiably withdraws, a lawyer should protect the welfare of the client by giving due notice of the withdrawal, suggesting employment of other counsel, delivering to the client all papers and property to which the client is entitled, cooperating with counsel subsequently employed, and otherwise endeavoring to minimize the possibility of harm. Clients receive no benefit from a lawyer keeping a copy of the file and therefore can not be charged for any copying costs. Further, the lawyer should refund to the client any compensation not earned during the employment.

[9] Even if the lawyer has been unfairly discharged by the client, a lawyer must take all reasonable steps to mitigate the consequences to the client.

Comparison to former Ohio Code of Professional Responsibility

Rule 1.16 governs withdrawal from representation and replaces DR 2-110.

Rule 1.16(a)(1) corresponds to DR 2-110(B)(1) and (2), Rule 1.16(a)(2) corresponds to DR 2-110(B)(3), and Rule 1.16(a)(3) corresponds to DR 2-110(B)(4).

Rule 1.16(b)(1) generally corresponds to DR 2-110(A)(2).

Rule 1.16(b)(2) corresponds to DR 2-110(C)(1)(b).

Rule 1.16(b)(3) corresponds to DR 2-110 (C)(1)(c).

Rule 1.16(b)(4) corresponds to DR 2-110(C)(1)(c) and (d).

Rule 1.16(b)(5) corresponds to DR 2-110(C)(1)(f).

Rule 1.16(b)(6) corresponds to DR 2-110(C)(1)(d).

Rule 1.16(b)(7) corresponds to DR 2-110(C)(5).

Rule 1.16(b)(8) corresponds to DR 2-110(C)(7).

Rule 1.16(b)(9) corresponds to DR 2-110(C)(6).

Rule 1.16(c) is identical to DR 2-110(A)(1).

Rule 1.16(d) corresponds to DR 2-110(A)(2) and also requires the withdrawing lawyer to promptly return client papers and property to the client. "Client papers and property" are defined as including correspondence, pleadings, deposition transcripts, exhibits, physical evidence, expert reports, and other items reasonably necessary to the client's representation.

Rule 1.16(e) is identical to DR 2-110(A)(3) except that the reference to the sale of a law practice rule is appropriately designated as Rule 1.17.

Comparison to ABA Model Rules of Professional Conduct

Rule 1.16(b)(2) is revised to change "criminal" to "illegal." This allows the lawyer to withdraw when the client persists in a course of action involving the lawyer's services that the lawyer reasonably believes is illegal. This would include violations of statutes or administrative regulations for which there are no criminal penalties.

Rules 1.16(b)(7) and (8) are added to recognize additional circumstances in which withdrawal may be permitted.

Rule 1.16(d) is revised to include a list of items typically included in "client papers and property." This provision is further modified to require that a withdrawing lawyer must afford the client a reasonable time to secure new counsel. Comment [8A] is added to elaborate on the duties of a lawyer who is contemplating or effectuating withdrawal from representation.

RULE 1.2: SCOPE OF REPRESENTATION AND ALLOCATION OF AUTHORITY BETWEEN CLIENT AND LAWYER

(a) Subject to divisions (c), (d), and (e) of this rule, a lawyer shall abide by a client's decisions concerning the objectives of representation and, as required by Rule 1.4, shall consult with the client as to the means by which they are to be pursued. A lawyer may take action on behalf of the client as is impliedly authorized to carry out the representation. A lawyer does not violate this rule by acceding to requests of opposing counsel that do not prejudice the rights of the client, being punctual in fulfilling all professional commitments, avoiding offensive tactics, and treating with courtesy and consideration all persons involved in the legal process. A lawyer shall abide by a client's decision whether to settle a matter. In a criminal case, the lawyer shall abide by the client's decision as to a plea to be entered, whether to waive a jury trial, and whether the client will testify.

(b) [RESERVED]

(c) A lawyer may limit the scope of a new or existing representation if the limitation is *reasonable* under the circumstances and communicated to the client, preferably in *writing*.

(d)(1) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer *knows* is *illegal* or *fraudulent*. A lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client in making a good faith effort to determine the validity, scope, meaning, or application of the law.

(2) A lawyer may counsel or assist a client regarding conduct expressly permitted under Sub. H.B. 523 of the 131st General Assembly authorizing the use of marijuana for medical purposes and any state statutes, rules, orders, or other provisions implementing the act. In these circumstances, the lawyer shall advise the client regarding related federal law.

(e) Unless otherwise required by law, a lawyer shall not present, participate in presenting, or threaten to present criminal charges or professional misconduct allegations solely to obtain an advantage in a civil matter.

Comment

Allocation of Authority between Client and Lawyer

[1] Division (a) confers upon the client the ultimate authority to determine the purposes to be served by legal representation, within the limits imposed by law and the lawyer's professional obligations. The decisions specified in division (a), such as whether to settle a civil matter, must also be made by the client. See Rule 1.4(a)(1) for the lawyer's duty to communicate with the client about such decisions. With respect to the means by which the

client's objectives are to be pursued, the lawyer shall consult with the client as required by Rule 1.4(a)(2) and may take such action as is impliedly authorized to carry out the representation.

[2] On occasion, however, a lawyer and a client may disagree about the means to be used to accomplish the client's objectives. Clients normally defer to the special knowledge and skill of their lawyer with respect to the means to be used to accomplish their objectives, particularly with respect to technical, legal, and tactical matters. Conversely, lawyers usually defer to the client regarding such questions as the expense to be incurred and concern for third persons who might be adversely affected. Because of the varied nature of the matters about which a lawyer and client might disagree and because the actions in question may implicate the interests of a tribunal or other persons, this rule does not prescribe how such disagreements are to be resolved. Other law, however, may be applicable and should be consulted by the lawyer. The lawyer should also consult with the client and seek a mutually acceptable resolution of the disagreement. If such efforts are unavailing and the lawyer has a fundamental disagreement with the client, the lawyer may withdraw from the representation. See Rule 1.16(b)(4). Conversely, the client may resolve the disagreement by discharging the lawyer. See Rule 1.16(a)(3).

[3] At the outset of a representation, the client may authorize the lawyer to take specific action on the client's behalf without further consultation. Absent a material change in circumstances and subject to Rule 1.4, a lawyer may rely on such an advance authorization. The client may, however, revoke such authority at any time.

[4] In a case in which the client appears to be suffering diminished capacity, the lawyer's duty to abide by the client's decisions is guided by reference to Rule 1.14.

[4A] Division (a) makes it clear that regardless of the nature of the representation the lawyer does not breach a duty owed to the client by maintaining a professional and civil attitude toward all persons involved in the legal process. Specifically, punctuality, the avoidance of offensive tactics, and the treating of all persons with courtesy are viewed as essential components of professionalism and civility, and their breach may not be required by the client as part of the representation.

Independence from Client's Views or Activities

[5] A lawyer's representation of a client, including representation by appointment, does not constitute an endorsement of the client's political, economic, social, or moral views or activities. Legal representation should not be denied to people who are unable to afford legal services or whose cause is controversial or the subject of popular disapproval. By the same token, representing a client does not constitute approval of the client's views or activities.

Agreements Limiting Scope of Representation

[6] [RESERVED]

[7] Although division (c) affords the lawyer and client substantial latitude in defining the scope of the representation, any limitation must be reasonable under the circumstances. If,

for example, a client's objective is limited to securing general information about the law that the client needs in order to handle a common and typically uncomplicated legal problem, the lawyer and client may agree that the lawyer's services will be limited to a brief telephone consultation. Such a limitation would not be reasonable if the time allotted was not sufficient to yield advice upon which the client could rely. In addition, the terms upon which representation is undertaken may exclude specific means that might otherwise be used to accomplish the client's objectives. Such limitations may exclude actions that the client thinks are too costly or that the lawyer regards as repugnant or imprudent. Although an agreement for a limited representation does not exempt a lawyer from the duty to provide competent representation, the limitation is a factor to be considered when determining the legal knowledge, skill, thoroughness, and preparation reasonably necessary for the representation. See Rule 1.1.

[7A] Written confirmation of a limitation of a new or existing representation is preferred and may be any writing that is presented to the client that reflects the limitation, such as a letter or electronic transmission addressed to the client or a court order. A lawyer may create a form or checklist that specifies the scope of the client-lawyer relationship and the fees to be charged. An order of a court appointing a lawyer to represent a client is sufficient to confirm the scope of that representation.

[8] All agreements concerning a lawyer's representation of a client must accord with the Ohio Rules of Professional Conduct and other law. See, *e.g.*, Rules 1.1, 1.8 and 5.6.

Illegal, Fraudulent and Prohibited Transactions

[9] Division (d)(1) prohibits a lawyer from knowingly counseling or assisting a client to commit an illegal act or fraud. This prohibition, however, does not preclude the lawyer from giving an honest opinion about the actual consequences that appear likely to result from a client's conduct. Nor does the fact that a client uses advice in a course of action that is illegal or fraudulent of itself make a lawyer a party to the course of action. There is a critical distinction between presenting an analysis of legal aspects of questionable conduct and recommending the means by which an illegal act or fraud might be committed with impunity.

[10] When the client's course of action has already begun and is continuing, the lawyer's responsibility is especially delicate. The lawyer is required to avoid assisting the client, for example, by drafting or delivering documents that the lawyer knows are fraudulent or by suggesting how the wrongdoing might be concealed. A lawyer may not continue assisting a client in conduct that the lawyer originally supposed was legally permissible but then discovers is improper. See Rules 3.3(b) and 4.1(b).

[11] Where the client is a fiduciary, the lawyer may be charged with special obligations in dealings with a beneficiary.

[12] Division (d)(1) applies whether or not the defrauded party is a party to the transaction. Hence, a lawyer must not participate in a transaction to effectuate illegal or fraudulent avoidance of tax liability. Division (d)(1) does not preclude undertaking a criminal defense incident to a general retainer for legal services to a lawful enterprise. The last clause of

division (d)(1) recognizes that determining the validity or interpretation of a statute or regulation may require a course of action involving disobedience of the statute or regulation or of the interpretation placed upon it by governmental authorities.

[13] If a lawyer comes to know or reasonably should know that a client expects assistance not permitted by the Ohio Rules of Professional Conduct or other law or if the lawyer intends to act contrary to the client's instructions, the lawyer must consult with the client regarding the limitations on the lawyer's conduct. See Rule 1.4(a)(5).

Comparison to former Ohio Code of Professional Responsibility

Rule 1.2 replaces several provisions within Canon 7 of the Code of Professional Responsibility.

The first sentence of Rule 1.2(a) generally corresponds to EC 7-7 and makes what previously was advisory into a rule. The second sentence of Rule 1.2(a) states explicitly what is implied by EC 7-7. The third sentence of Rule 1.2(a) corresponds generally to DR 7-101(A)(1) and EC 7-10. Rule 1.2(a)(1) and (2) correspond to several sentences in EC 7-7.

Rule 1.2(c) does not correspond to any Disciplinary Rule or Ethical Consideration.

The first sentence of Rule 1.2(d)(1) corresponds to DR 7-102(A)(7). The second sentence of Rule 1.2(d)(1) is similar to EC 7-4.

Rule 1.2(e) is the same as DR 7-105 except for the addition of the prohibition against threatening "professional misconduct allegations."

Comparison to ABA Model Rules of Professional Conduct

Rule 1.2(a) is modified slightly from the Model Rule 1.2(a) by the inclusion of the third sentence, which does not exist in the Model Rules.

Model Rule 1.2(b) has been moved to Comment [5] of Rule 1.2 because the provision is more appropriately addressed in a comment rather than a black-letter rule.

Rule 1.2(c) differs from Model Rule 1.2(c) in that it requires only that the limitation be communicated to the client, preferably in writing. The Model Rule requires that the client give informed consent to the limitation.

Rule 1.2(d)(1) is similar to Model Rule 1.2(d) but differs in two aspects. The Model Rule language "criminal" was changed to "illegal" in Rule 1.2(d)(1), and Model Rule 1.2(d) was split into two sentences in 1.2(d)(1).

Rule 1.2(d)(2) does not exist in the Model Rules.

Rule 1.2(e) does not exist in the Model Rules.

RULE 1.3: DILIGENCE

A lawyer shall act with *reasonable* diligence and promptness in representing a client.

Comment

[1] A lawyer should pursue a matter on behalf of a client despite opposition, obstruction, or personal inconvenience to the lawyer. A lawyer also must act with commitment and dedication to the interests of the client.

[2] A lawyer must control the lawyer's work load so that each matter can be handled competently.

[3] Delay and neglect are inconsistent with a lawyer's duty of diligence, undermine public confidence, and may prejudice a client's cause. Reasonable diligence and promptness are expected of a lawyer in handling all client matters and will be evaluated in light of all relevant circumstances. The lawyer disciplinary process is particularly concerned with lawyers who consistently fail to carry out obligations to clients or consciously disregard a duty owed to a client.

[4] A lawyer should carry through to conclusion all matters undertaken for a client, unless the client-lawyer relationship is terminated as provided in Rule 1.16. Doubt about whether a client-lawyer relationship still exists should be clarified by the lawyer, preferably in writing, so that the client will not mistakenly suppose the lawyer is looking after the client's affairs when the lawyer has ceased to do so. For example, if a lawyer has handled a judicial or administrative proceeding that produced a result adverse to the client and the lawyer and the client have not agreed that the lawyer will handle the matter on appeal, the lawyer must consult with the client about post-trial alternatives including the possibility of appeal before relinquishing responsibility for the matter. See Rule 1.4(a)(2). Whether the lawyer is obligated to pursue those alternatives or prosecute the appeal for the client depends on the scope of the representation the lawyer has agreed to provide to the client. See Rules 1.2(c) and 1.5(b).

[5] To prevent neglect of client matters in the event of a sole practitioner's death or disability, the duty of diligence may require that each sole practitioner prepare a plan, in conformity with applicable rules, that designates another competent lawyer to review client files, notify each client of the lawyer's death or disability, and determine whether there is a need for immediate protective action. *Cf.* Rule V, Section 26 of the Supreme Court Rules for the Government of the Bar of Ohio.

Comparison to former Ohio Code of Professional Responsibility

Rule 1.3 replaces both DR 6-101(A)(3) (a lawyer shall not neglect a legal matter entrusted to him) and DR 7-101(A)(1) (with limited exceptions, a lawyer shall not fail to seek the lawful objectives of his client through reasonably available means permitted by law and the disciplinary rules).

RULE 1.5: FEES AND EXPENSES

(a) A lawyer shall not make an agreement for, charge, or collect an *illegal* or clearly excessive fee. A fee is clearly excessive when, after a review of the facts, a lawyer of ordinary prudence would be left with a definite and firm conviction that the fee is in excess of a *reasonable* fee. The factors to be considered in determining the reasonableness of a fee include the following:

(1) the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;

(2) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;

(3) the fee customarily charged in the locality for similar legal services;

(4) the amount involved and the results obtained;

(5) the time limitations imposed by the client or by the circumstances;

(6) the nature and length of the professional relationship with the client;

(7) the experience, reputation, and ability of the lawyer or lawyers performing the services;

(8) whether the fee is fixed or contingent.

(b) The nature and scope of the representation and the basis or rate of the fee and expenses for which the client will be responsible shall be communicated to the client, preferably in *writing*, before or within a *reasonable* time after commencing the representation, unless the lawyer will charge a client whom the lawyer has regularly represented on the same basis as previously charged. Any change in the basis or rate of the fee or expenses is subject to division (a) of this rule and shall promptly be communicated to the client, preferably in *writing*.

(c) A fee may be contingent on the outcome of the matter for which the service is rendered, except in a matter in which a contingent fee is prohibited by division (d) of this rule or other law.

(1) Each contingent fee agreement shall be in a *writing* signed by the client and the lawyer and shall state the method by which the fee is to be determined, including the percentage or percentages that shall accrue to the lawyer in the event of settlement, trial, or appeal; litigation and other expenses to be deducted from the recovery; and whether such expenses are to be deducted before or after the contingent fee is calculated. The agreement shall clearly

notify the client of any expenses for which the client will be liable whether or not the client is the prevailing party.

(2) If the lawyer becomes entitled to compensation under the contingent fee agreement and the lawyer will be disbursing funds, the lawyer shall prepare a closing statement and shall provide the client with that statement at the time of or prior to the receipt of compensation under the agreement. The closing statement shall specify the manner in which the compensation was determined under the agreement, any costs and expenses deducted by the lawyer from the judgment or settlement involved, and, if applicable, the actual division of the lawyer's fees with a lawyer not in the same *firm*, as required in division (e)(3) of this rule. The closing statement shall be signed by the client and lawyer.

(d) A lawyer shall not enter into an arrangement for, charge, or collect any of the following:

(1) any fee in a domestic relations matter, the payment or amount of which is contingent upon the securing of a divorce or upon the amount of spousal or child support, or property settlement in lieu thereof;

(2) a contingent fee for representing a defendant in a criminal case;

(3) a fee denominated as "earned upon receipt," "nonrefundable," or in any similar terms, unless the client is simultaneously advised in *writing* that if the lawyer does not complete the representation for any reason, the client may be entitled to a refund of all or part of the fee based upon the value of the representation pursuant to division (a) of this rule.

(e) Lawyers who are not in the same *firm* may divide fees only if all of the following apply:

(1) the division of fees is in proportion to the services performed by each lawyer or each lawyer assumes joint responsibility for the representation and agrees to be available for consultation with the client;

(2) the client has given *written* consent after full disclosure of the identity of each lawyer, that the fees will be divided, and that the division of fees will be in proportion to the services to be performed by each lawyer or that each lawyer will assume joint responsibility for the representation;

(3) except where court approval of the fee division is obtained, the *written* closing statement in a case involving a contingent fee shall be signed by the client and each lawyer and shall comply with the terms of division (c)(2) of this rule;

(4) the total fee is *reasonable*.

(f) In cases of a dispute between lawyers arising under this rule, fees shall be divided in accordance with the mediation or arbitration provided by a local bar association. When a local bar association is not available or does not have procedures to resolve fee disputes between lawyers, the dispute shall be referred to the Ohio State Bar Association for mediation or arbitration.

Comment

Reasonableness of Fee

[1] Division (a) requires that lawyers charge fees that are reasonable under the circumstances. The factors specified in divisions (a)(1) through (8) are not exclusive. Nor will each factor be relevant in each instance.

Nature and Scope of Representation; Basis or Rate of Fee and Expenses

[2] The detail and specificity of the communication required by division (b) will depend on the nature of the client-lawyer relationship, the work to be performed, and the basis of the rate or fee. A writing that confirms the nature and scope of the client-lawyer relationship and the fees to be charged is the preferred means of communicating this information to the client and can clarify the relationship and reduce the possibility of a misunderstanding. When the lawyer has regularly represented a client, they ordinarily will have evolved an understanding concerning the basis or rate of the fee and the expenses for which the client will be responsible. In a new client-lawyer relationship, however, an understanding as to fees and expenses must be established promptly. Unless the situation involves a regularly represented client, the lawyer should furnish the client with at least a simple memorandum or copy of the lawyer's customary fee arrangements that states the general nature of the legal services to be provided, the basis, rate or total amount of the fee, and whether and to what extent the client will be responsible for any costs, expenses, or disbursements in the course of the representation. So long as the client agrees in advance, a lawyer may seek reimbursement for the reasonable cost of services performed in-house, such as copying.

[3] Contingent fees, like any other fees, are subject to the reasonableness standard of division (a) of this rule. In determining whether a particular contingent fee is reasonable, or whether it is reasonable to charge any form of contingent fee, a lawyer must consider the factors that are relevant under the circumstances. Applicable law may impose limitations on contingent fees, such as a ceiling on the percentage allowable, or may require a lawyer to offer clients an alternative basis for the fee. Applicable law also may apply to situations other than a contingent fee, for example, government regulations regarding fees in certain tax matters.

Terms of Payment

[4] A lawyer may require advance payment of a fee, but is obliged to return any unearned portion. See Rule 1.16(e). A lawyer may accept property in payment for services,

such as an ownership interest in an enterprise, providing this does not involve acquisition of a proprietary interest in the cause of action or subject matter of the litigation contrary to Rule 1.8 (i). However, a fee paid in property instead of money may be subject to the requirements of Rule 1.8(a) because such fees often have the essential qualities of a business transaction with the client.

[5] An agreement may not be made whose terms might induce the lawyer improperly to curtail services for the client or perform them in a way contrary to the client's interest. For example, a lawyer should not enter into an agreement whereby services are to be provided only up to a stated amount when it is foreseeable that more extensive services probably will be required, unless the situation is adequately explained to the client. Otherwise, the client might have to bargain for further assistance in the midst of a proceeding or transaction. However, it is proper to define the extent of services in light of the client's ability to pay. A lawyer should not exploit a fee arrangement based primarily on hourly charges by using wasteful procedures.

[5A] If all funds held by the lawyer are not disbursed at the time the closing statement required by division (c)(2) is prepared, the lawyer's obligation with regard to those funds is governed by Rule 1.15.

Prohibited Contingent Fees

[6] Division (d) prohibits a lawyer from charging a contingent fee in a domestic relations matter when payment is contingent upon the securing of a divorce or upon the amount of spousal or child support or property settlement to be obtained. This provision does not preclude a contract for a contingent fee for legal representation in connection with the recovery of post-judgment balances due under support or other financial orders because such contracts do not implicate the same policy concerns.

Retainer

[6A] Advance fee payments are of at least four types. The "true" or "classic" retainer is a fee paid in advance solely to ensure the lawyer's availability to represent the client and precludes the lawyer from taking adverse representation. What is often called a retainer is in fact an advance payment to ensure that fees are paid when they are subsequently earned, on either a flat fee or hourly fee basis. A flat fee is a fee of a set amount for performance of agreed work, which may or may not be paid in advance but is not deemed earned until the work is performed. An earned upon receipt fee is a flat fee paid in advance that is deemed earned upon payment regardless of the amount of future work performed. When a fee is earned affects whether it must be placed in the attorney's trust account, see Rule 1.15, and may have significance under other laws such as tax and bankruptcy. The reasonableness requirement and the application of the factors in division (a) may mean that a client is entitled to a refund of an advance fee payment even though it has been denominated "nonrefundable," "earned upon receipt," or in similar terms that imply the client would never receive a refund. So that a client is not misled by the use of such terms, division (d)(3) requires certain minimum disclosures that must be included in the written fee agreement. This does not mean the client will always be entitled to a refund upon early termination of the representation [*e.g.*, factor (a)(2) might justify the entire fee], nor does it

determine how any refund should be calculated (e.g., hours worked times a reasonable hourly rate, quantum meruit, percentage of the work completed, etc.), but merely requires that the client be advised of the possibility of a refund based upon application of the factors set forth in division (a). In order to be able to demonstrate the reasonableness of the fee in the event of early termination of the representation, it is advisable that lawyers maintain contemporaneous time records for any representation undertaken on a flat fee basis.

Division of Fee

[7] A division of fee is a single billing to a client covering the fee of two or more lawyers who are not in the same firm. A division of fee facilitates association of more than one lawyer in a matter in which neither alone could serve the client as well, and most often is used when the fee is contingent and the division is between a referring lawyer and a trial lawyer. Division (e) permits the lawyers to divide a fee either on the basis of the proportion of services they render or if each lawyer assumes responsibility for the representation as a whole. Within a reasonable time after disclosure of the identity of each lawyer, the client must give written approval that the fee will be divided and that the division of fees is in proportion to the services performed by each lawyer or that each lawyer assumes joint responsibility for the representation. Except where court approval of the fee division is obtained, closing statements must be in a writing signed by the client and each lawyer and must otherwise comply with division (c) of this rule. Joint responsibility for the representation entails financial and ethical responsibility for the representation as if the lawyers were associated in a partnership. A lawyer should only refer a matter to a lawyer whom the referring lawyer reasonably believes is competent to handle the matter. See Rules 1.1 and 1.17.

[8] Division (e) does not prohibit or regulate division of fees to be received in the future for work done when lawyers were previously associated in a law firm.

Disputes over Fees

[9] If a procedure has been established for resolution of fee disputes between a client and a lawyer, such as an arbitration or mediation procedure established by a local bar association, the Ohio State Bar Association, or the Supreme Court of Ohio, the lawyer must comply with the procedure when it is mandatory, and, even when it is voluntary, the lawyer should conscientiously consider submitting to it. Law may prescribe a procedure for determining a lawyer's fee, for example, in representation of an executor or administrator, a class or a person entitled to a reasonable fee as part of the measure of damages. The lawyer entitled to such a fee and a lawyer representing another party concerned with the fee should comply with the prescribed procedure.

[10] A procedure has been established for resolution of fee disputes between lawyers who are sharing a fee pursuant to division (e) of this rule. This involves use of an arbitration or mediation procedure established by a local bar association or the Ohio State Bar Association. The lawyer must comply with the procedure. A dispute between lawyers who are splitting a fee shall not delay disbursement to the client. See Rule 1.15.

IV. TRANSACTIONS WITH PERSONS OTHER THAN CLIENTS

RULE 4.1: TRUTHFULNESS IN STATEMENTS TO OTHERS

In the course of representing a client a lawyer shall not *knowingly* do either of the following:

(a) make a false statement of material fact or law to a third person;

(b) fail to disclose a material fact when disclosure is necessary to avoid assisting an *illegal* or *fraudulent* act by a client.

Comment

Misrepresentation

[1] A lawyer is required to be truthful when dealing with others on a client's behalf. A misrepresentation can occur if the lawyer incorporates or affirms a statement of another person that the lawyer knows is false. Misrepresentations can also occur by partially true but misleading statements or omissions that are the equivalent of affirmative false statements. For dishonest conduct that does not amount to a false statement or for misrepresentations by a lawyer other than in the course of representing a client, see Rule 8.4.

Statements of Fact

[2] This rule refers to statements of fact. Whether a particular statement should be regarded as one of fact can depend on the circumstances. Under generally accepted conventions in negotiation, certain types of statements ordinarily are not taken as statements of material fact. Estimates of price or value placed on the subject of a transaction and a party's intentions as to an acceptable settlement of a claim are ordinarily in this category, and so is the existence of an undisclosed principal except where nondisclosure of the principal would constitute fraud. Lawyers should be mindful of their obligations under applicable law to avoid criminal and tortious misrepresentation.

Disclosure to Prevent Illegal or Fraudulent Client Acts

[3] Under Rule 1.2(d), a lawyer is prohibited from counseling or assisting a client in conduct that the lawyer knows is illegal or fraudulent. Rule 4.1(b) requires a lawyer to disclose a material fact, including one that may be protected by the attorney-client privilege, when the disclosure is necessary to avoid the lawyer's assistance in the client's illegal or fraudulent act. See also Rule 8.4(c). The client can, of course, prevent such disclosure by refraining from the wrongful conduct. If the client persists, the lawyer usually can avoid assisting the client's illegal or fraudulent act by withdrawing from the representation. If withdrawal is not sufficient to avoid such assistance, division (b) of the rule requires disclosure of material facts necessary to prevent the assistance of the client's illegal or fraudulent act. Such disclosure may include disaffirming

an opinion, document, affirmation, or the like, or may require further disclosure to avoid being deemed to have assisted the client's illegal or fraudulent act. Disclosure is not required unless the lawyer is unable to withdraw or the client is using the lawyer's work product to assist the client's illegal or fraudulent act.

[4] Division (b) of this rule addresses only ongoing or future illegal or fraudulent acts of a client. With respect to past illegal or fraudulent client acts of which the lawyer later becomes aware, Rule 1.6(b)(3) permits, but does not require, a lawyer to reveal information reasonably necessary to mitigate substantial injury to the financial or property interests of another that has resulted from the client's commission of an illegal or fraudulent act, in furtherance of which the client has used the lawyer's services.

Comparison to former Ohio Code of Professional Responsibility

Rule 4.1 addresses the same issues contained in several provisions of the Ohio Code of Professional Responsibility. Division (a) of the rule is virtually identical to DR 7-102(A)(5). Division (b) parallels DR 7-102(A)(3) and the "fraud on a person" portion of DR 7-102(B)(1). The "fraud on a tribunal" portion of DR 7-102(B)(1) is now found in Rule 3.3.

No Ohio case has construed DR 7-102(B) in the context of a lawyer failing to disclose a fraud on a person. Nevertheless, revealing such an ongoing or future fraud is justified under Rule 4.1(b) when the client refuses to prevent it, and the lawyer's withdrawal from the matter is not sufficient to prevent assisting the fraud.

The mitigation of past fraud on a person, addressed in DR 7-102(B), is now found in Rule 1.6(b)(3).

Comparison to ABA Model Rules of Professional Conduct

Rule 4.1 incorporates two changes in Model Rule 4.1(b) that are intended to track Ohio law. First, division (b) prohibits lawyers from assisting "illegal" and fraudulent acts of clients, (rather than "criminal" and fraudulent acts) consistent with proposed Rule 1.2(d) and DR 7-102(A)(7). Second, the "unless" clause at the end of division (b), which conditions the lawyer's duty to disclose on exceptions in Rule 1.6, is deleted. Deleting this phrase results in a clearer stand alone anti-fraud rule because it does not require reference to Rule 1.6, and also because such a provision is more consistent with DR 7-102(B)(1).

Comment [3] is rewritten and Comment [4] inserted to clarify the scope and meaning of division (b), and to add appropriate cross-references to other rules.

RULE 4.2: COMMUNICATION WITH PERSON REPRESENTED BY COUNSEL

In representing a client, a lawyer shall not communicate about the subject of the representation with a person the lawyer *knows* to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized to do so by law or a court order.

Comment

[1] This rule contributes to the proper functioning of the legal system by protecting a person who has chosen to be represented by a lawyer in a matter against possible overreaching by other lawyers who are participating in the matter, interference by those lawyers with the client-lawyer relationship, and the uncounselled disclosure of information relating to the representation.

[2] This rule applies to communications with any person who is represented by counsel concerning the matter to which the communication relates.

[3] The rule applies even though the represented person initiates or consents to the communication. A lawyer must immediately terminate communication with a person if, after commencing communication, the lawyer learns that the person is one with whom communication is not permitted by this rule.

[4] This rule does not prohibit communication with a represented person, or an employee or agent of such a person, concerning matters outside the representation. For example, the existence of a controversy between a government agency and a private party, or between two organizations, does not prohibit a lawyer for either from communicating with nonlawyer representatives of the other regarding a separate matter. Nor does this rule preclude communication with a represented person who is seeking advice from a lawyer who is not otherwise representing a client in the matter. A lawyer may not make a communication prohibited by this rule through the acts of another. See Rule 8.4(a). Parties to a matter may communicate directly with each other, and a lawyer is not prohibited from advising a client concerning a communication that the client is legally entitled to make. Also, a lawyer having independent justification or legal authorization for communicating with a represented person is permitted to do so.

[5] Communications authorized by law may include communications by a lawyer on behalf of a client who is exercising a constitutional or other legal right to communicate with the government. Communications authorized by law may also include investigative activities of lawyers representing governmental entities, directly or through investigative agents, prior to the commencement of criminal or civil enforcement proceedings. When communicating with the accused in a criminal matter, a government lawyer must comply with this rule in addition to honoring the constitutional rights of the accused. The fact that a communication does not violate a state or federal constitutional right is insufficient to establish that the communication is permissible under this rule.

RULE 8.3: REPORTING PROFESSIONAL MISCONDUCT

(a) A lawyer who possesses unprivileged knowledge of a violation of the Ohio Rules of Professional Conduct that raises a question as to any lawyer's honesty, trustworthiness, or fitness as a lawyer in other respects, shall inform a disciplinary authority empowered to investigate or act upon such a violation.

(b) A lawyer who possesses unprivileged knowledge that a judge has committed a violation of the Ohio Rules of Professional Conduct or applicable rules of judicial conduct shall inform the appropriate authority.

(c) Any information obtained by a member of a committee or subcommittee of a bar association, or by a member, employee, or agent of a nonprofit corporation established by a bar association, designed to assist lawyers with substance abuse or mental health problems, provided the information was obtained while the member, employee, or agent was performing duties as a member, employee, or agent of the committee, subcommittee, or nonprofit corporation, shall be privileged for all purposes under this rule.

Comment

[1] Self-regulation of the legal profession requires that a member of the profession initiate disciplinary investigation when the lawyer knows of a violation of the Ohio Rules of Professional Conduct involving that lawyer or another lawyer. A lawyer has a similar obligation with respect to judicial misconduct. An apparently isolated violation may indicate a pattern of misconduct that only a disciplinary investigation can uncover. Reporting a violation is especially important where the victim is unlikely to discover the offense.

[2] A report about misconduct is not required where it would involve the disclosure of privileged information. However, a lawyer should encourage a client to consent to disclosure where it would not substantially prejudice the client's interests.

[3] [RESERVED]

[4] The duty to report professional misconduct does not apply to a lawyer retained to represent a lawyer whose professional conduct is in question. Such a situation is governed by the rules applicable to the client-lawyer relationship. See Rule 1.6.

[5] Information about a lawyer's or judge's misconduct or fitness may be received by a lawyer in the course of that lawyer's participation in an approved lawyers or judges assistance program. In that circumstance, providing for an exception to the reporting requirements of divisions (a) and (b) of this rule encourages lawyers and judges to seek treatment through such a program. Conversely, without such an exception, lawyers and judges may hesitate to seek assistance from these programs, which may then result in additional harm to their professional careers and additional injury to the welfare of clients and the public.

Comparison to former Ohio Code of Professional Responsibility

Rule 8.3 is comparable to DR 1-103 but differs in two respects. First, Rule 8.3 does not contain the strict reporting requirement of DR 1-103. DR 1-103 requires a lawyer to report all misconduct of which the lawyer has unprivileged knowledge. Rule 8.3 requires a lawyer to report misconduct only when the lawyer possesses unprivileged knowledge that raises a question as to any lawyer's honesty, trustworthiness, or fitness in other respects. Second, Rule 8.3 requires a lawyer to self-report.

Comparison to ABA Model Rules of Professional Conduct

Rule 8.3 is revised to comport more closely to DR 1-103. Division (a) is rewritten to require the self-reporting of disciplinary violations. In addition, the provisions of divisions (a) and (b) are broadened to require reporting of (1) any violation by a lawyer that raises a question regarding the lawyer's honesty, trustworthiness, or fitness, and (2) any ethical violation by a judge. In both provisions, language is included to limit the reporting requirement to circumstances where a lawyer's knowledge of a reportable violation is unprivileged.

Division (c), which deals with confidentiality of information regarding lawyers and judges participating in lawyers' assistance programs, has been strengthened to reflect Ohio's position that such information is not only confidential, but "shall be privileged for all purposes" under DR 1-103(C). The substance of DR 1-103(C) has been inserted in place of Model Rule 8.3(c).

In light of the substantive changes made in divisions (a) and (b), Comment [3] is no longer applicable and is stricken. Further, due to the substantive changes made to confidentiality of information regarding lawyers and judges participating in lawyers' assistance programs, the last sentence in Comment [5] has been stricken.

RULE 8.4: MISCONDUCT

It is professional misconduct for a lawyer to do any of the following:

(a) violate or attempt to violate the Ohio Rules of Professional Conduct, *knowingly* assist or induce another to do so, or do so through the acts of another;

(b) commit an *illegal* act that reflects adversely on the lawyer's honesty or trustworthiness;

(c) engage in conduct involving dishonesty, *fraud*, deceit, or misrepresentation;

(d) engage in conduct that is prejudicial to the administration of justice;

(e) state or imply an ability to influence improperly a government agency or official or to achieve results by means that violate the Ohio Rules of Professional Conduct or other law;

(f) *knowingly* assist a judge or judicial officer in conduct that is a violation of the Ohio Rules of Professional Conduct, the applicable rules of judicial conduct, or other law;

(g) engage, in a professional capacity, in conduct involving discrimination prohibited by law because of race, color, religion, age, gender, sexual orientation, national origin, marital status, or disability;

(h) engage in any other conduct that adversely reflects on the lawyer's fitness to practice law.

Comment

[1] Lawyers are subject to discipline when they violate or attempt to violate the Ohio Rules of Professional Conduct, knowingly assist or induce another to do so, or do so through the acts of another, as when they request or instruct an agent to do so on the lawyer's behalf. Division (a), however, does not prohibit a lawyer from advising a client concerning action the client is legally entitled to take.

[2] Many kinds of illegal conduct reflect adversely on fitness to practice law, such as offenses involving fraud and the offense of willful failure to file an income tax return. However, some kinds of offenses carry no such implication. Traditionally, the distinction was drawn in terms of offenses involving "moral turpitude." That concept can be construed to include offenses concerning some matters of personal morality, such as adultery and comparable offenses, that have no specific connection to fitness for the practice of law. Although a lawyer is personally answerable to the entire criminal law, a lawyer should be professionally answerable only for offenses that indicate lack of those characteristics relevant to law practice. Offenses

involving violence, dishonesty, breach of trust, or serious interference with the administration of justice are in that category. A pattern of repeated offenses, even ones of minor significance when considered separately, can indicate indifference to legal obligation.

[2A] Division (c) does not prohibit a lawyer from supervising or advising about lawful covert activity in the investigation of criminal activity or violations of constitutional or civil rights when authorized by law.

[3] Division (g) does not apply to a lawyer's confidential communication to a client or preclude legitimate advocacy where race, color, religion, age, gender, sexual orientation, national origin, marital status, or disability is relevant to the proceeding where the advocacy is made.

[4] A lawyer may refuse to comply with an obligation imposed by law upon a good faith belief that no valid obligation exists. The provisions of Rule 1.2(d) concerning a good faith challenge to the validity, scope, meaning, or application of the law apply to challenges of legal regulation of the practice of law.

[5] Lawyers holding public office assume legal responsibilities going beyond those of other citizens. A lawyer's abuse of public office can suggest an inability to fulfill the professional role of lawyers. The same is true of abuse of positions of private trust such as trustee, executor, administrator, guardian, agent, and officer, director, or manager of a corporation or other organization.

Comparison to former Ohio Code of Professional Responsibility

Rule 8.4 is substantively comparable to DR 1-102 and 9-101(C).

Rule 8.4 removes the "moral turpitude" standard of DR 1-102(A)(3) and replaces it with Rule 8.4(b), which states that a lawyer engages in professional misconduct if the lawyer "commit[s] an illegal act that reflects adversely on the lawyer's honesty or trustworthiness."

Comparison to ABA Model Rules of Professional Conduct

Rule 8.4 is substantially similar to Model Rule 8.4 except for the additions of the anti-discrimination provisions of DR 1-102(B) and the fitness to practice provision of DR 1-102(A)(6). Comment [2A] is added to indicate that a lawyer's involvement in lawful covert activities is not a violation of Rule 8.4(c). The last sentence of DR 1-102(B) is inserted in place of Model Rule Comment [3].

2019 BENCH-BAR RETREAT

Sanctions

In re Bavelis, 743 Fed.Appx. 670 (6th Cir. 2018)

Claimants and counsel sanctioned for concealing the fact that the claim had been assigned. As a litigation strategy, assignor and assignee and their attorneys decided to try the case as if the original claimant still owned the note. Once debtor learned of the assignment (approximately 2 years later), debtor advised the court, which sanctioned counsel and claimants. Sixth Circuit upheld sanctions.

Conflicts

Cruickshank v. Dixon (In re Blast Fitness Grp.), Nos. 16-10236-MSH, 18-01011 [Doc. # 282], 2019 Bankr. LEXIS 41 (Bankr. D. Mass. Jan. 8, 2019)

Trustee brought malpractice claims against attorneys for having a “material, undisclosed and unwaivable conflict of interest” in dual representation of closely held company and its indirect sole manager. Bankruptcy court overruled the motions to dismiss and noted that while it may not be a conflict in all instances, a firm should know when a conflict may arise (e.g., where the equity holder is benefiting or self-dealing to the detriment of the company).

In re Gemstones Solutions Group, Inc. (f/k/a Gymboree Group, Inc.), No. 19-30258 [Doc. # 354] (Bankr. E.D. Va. Feb. 15, 2019)

Although a significant secured creditor contributed to over 4% of the revenue of firm, bankruptcy court held that there was no conflict under § 327, where disclosures were clear, there appeared to be no adverse relationship, and debtor’s counsel was significant to the success of the bankruptcy.

CFPB Still Exists

Bureau of Consumer Financial Protection v. Forster & Garbus, LLP, No. 19-cv-02928 (EDNY May 17, 2019)

CFPB filed complaint against law firm for automated collection, alleging that the firm received substantial sums from consumers who may not have even owed money. The firm is alleged to have filed numerous actions against people without doing any due diligence into the facts or without reviewing or preparing pleadings. The firm has denied these allegations and intends to defend itself.

Judges Are People Too

Clark et al v. Kapila, No. 1:18-cv-24578-FAM [Doc. # 38] (SD Fla. Sept. 9, 2019)

Court reversed a number of decisions made by judge who ruled in favor of trustee on multiple issues after judge refused to recuse himself from adversary proceedings after his fiancé received an offer and job at the firm representing trustee. Court held that there was a clear appearance of impropriety and judge should have recused himself. Trustee is appealing this decision.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

BUREAU OF CONSUMER FINANCIAL PROTECTION,

Plaintiff,

v.

FORSTER & GARBUS, LLP,

Defendant.

Civil Action No. 2:19-cv-2928

COMPLAINT

Plaintiff, the Bureau of Consumer Financial Protection (Bureau), alleges as follows:

Introduction

1. The Bureau brings this action against Forster & Garbus, LLP, a debt-collection law firm, to address its practice of filing collection lawsuits against consumers without meaningful attorney involvement.

2. Since at least January 2014, Forster & Garbus has relied on non-attorney support staff, automation, and both a cursory and deficient review of account files to attempt to collect more than 99,000 debts that consumers allegedly owe to Forster & Garbus's clients.

3. Using high-volume litigation tactics, Forster & Garbus collects substantial sums of money from consumers who may not actually owe debts or may not owe debts in the amounts claimed in the collection suits.

Jurisdiction and Venue

4. This Court has subject-matter jurisdiction over this action because it presents a federal question, 28 U.S.C. § 1331, and is brought by an agency of the United States, 28 U.S.C. § 1345.

5. Venue is proper because Forster & Garbus is located, resides, and transacts business in this district. 12 U.S.C. § 5564(f).

Parties

6. The Bureau is an agency of the United States charged with regulating the offering and providing of consumer-financial products and services under federal consumer-financial laws, including the Fair Debt Collection Practices Act (FDCPA), 12 U.S.C. § 5491(a), and the Consumer Financial Protection Act of 2010 (CFPA), 12 U.S.C. §§ 5531, 5536(a)(1). The Bureau's regulatory authority extends to persons engaged in the collection of debt related to any consumer-financial product or service. 12 U.S.C. §§ 5481(5), (15)(A)(x). The Bureau has independent litigating authority to address violations of federal consumer-financial laws, including the FDCPA and the CFPA. 12 U.S.C. § 5564(a)-(b); 15 U.S.C. § 1692l(b)(6).

7. Forster & Garbus is headquartered and maintains its principal place of business at 60 Motor Parkway, Commack, New York 11725. At all times material to this Complaint, Forster & Garbus has regularly collected or attempted to collect,

directly or indirectly, consumer debts. Forster & Garbus is therefore a "covered person" under the CFPA and a "debt collector" under the FDCPA. 12 U.S.C. §§ 5481(6), (15)(A)(x); 15 U.S.C. § 1692a(6).

Facts

8. For several decades, Forster & Garbus has collected debts incurred primarily for personal, family, or household purposes. Creditors and debt buyers refer credit-card, auto-loan, student-loan, and home-equity-loan debts, among others, to Forster & Garbus for collection.

9. Between 2014 and 2016, at any given time, Forster & Garbus employed roughly ten or eleven attorneys, in addition to its two named partners.

10. Since January 1, 2014, Forster & Garbus's clients have placed more than 136,700 accounts with the firm for collection.

11. Accounts placed with Forster & Garbus have generally been electronically sent to Forster & Garbus with the data needed to populate Forster & Garbus's templates for communications with consumers, including templates for civil complaints. This data includes the consumer's name, address, and social-security number, the original account number, the date the account was opened, the name of the present creditor, the name of the original creditor, the date of charge-off, the amount of the debt, and the last payment date.

12. Historically, unless a consumer disputes a debt, Forster & Garbus has generally not conducted any inquiry into the facts surrounding an alleged debt or requested supporting documentation, such as account applications, billing statements, payment histories, the terms and conditions governing an account, or consumer correspondence, from its clients to corroborate purported debts before filing suit. In addition, Forster & Garbus does not conduct reviews for contractual disclaimers related to debt sales, even though many of Forster & Garbus's clients are debt buyers.

Forster & Garbus engages in mass litigation.

13. Despite maintaining a small roster of attorneys, Forster & Garbus files suits in New York courts on a massive scale.

14. In 2014, Forster & Garbus filed collection lawsuits on more than 45,600 consumer accounts; in 2015, it filed collection lawsuits on more than 34,100 consumer accounts; and in 2016, it filed collection lawsuits on more than 20,000 consumer accounts. Forster & Garbus filed more than 99,000 collection lawsuits between 2014 and 2016 (the "Collection Suits").

15. Forster & Garbus's Collection Suits bore the names and signatures of attorneys despite those attorneys not being meaningfully involved in reviewing the merits of the lawsuits, including conducting any inquiry into the facts, or in preparing the pleadings.

Forster & Garbus relies on non-attorney staff and automated processes to identify accounts for suit and to prepare relevant pleadings.

16. Forster & Garbus relies on non-attorney staff and automated processes to identify accounts for potential legal action. Upon placement of an account with Forster & Garbus, the firm's software automatically scrubs the file to determine, among other things, whether the relevant consumer has filed for bankruptcy, is in active military status, or is deceased. The software also assesses whether a statute of limitations bars collection.

17. Non-attorney support staff then attempt to collect the debt for Forster & Garbus's clients outside of the legal system.

18. If the non-attorney personnel do not receive a response from a consumer to demands for payment or an account cannot otherwise be resolved, Forster & Garbus's non-attorney personnel will identify the account as "suit-worthy."

19. Accounts deemed "suit-worthy" are then, again, run against bankruptcy, deceased, and military databases.

20. After these scrubs are run, files that are not rejected by one of the scrubs are transferred to one of Forster & Garbus's partners, Mark Garbus, for review.

21. Garbus uses two computer screens to compare a complaint related to a particular account, which Forster & Garbus's software generates by populating a

template with data provided by Forster & Garbus's clients upon account placement, against information on the account, such as account balance and venue. Garbus reviews the information available on the account, any staff notes on the account, and, if available, any documents provided by clients upon account placement; historically, however, Forster & Garbus has not received any original or supporting documentation from its clients before filing suit.

22. Garbus generally approves for suit more than 90% of the accounts that are presented to him. In his review, he looks for "obvious" reasons to reject a suit, such as a recent payment on the account or the consumer having filed for bankruptcy.

23. Following Garbus's review and approval, the complaint and summons are printed by the firm's clerical unit and given to an associate attorney for further review and for signature. The associate attorney has the authority to reject the lawsuit.

24. Forster & Garbus's associate attorney conducts the same type of review as Garbus, examining the content included in the physical complaint against account data provided by the relevant client and any notes and available documents. The associate attorney may also review client affidavits to ensure consistency with the data in Forster & Garbus's system. If the associate attorney approves the account for suit, he or she signs the complaint.

25. One former associate attorney with Forster & Garbus received and reviewed finished complaints from Forster & Garbus's back office. If the information in the complaint accurately matched the client-supplied information in the firm's computer system, he would sign the complaint. His review of each complaint only took "a minute or two," and he would allocate roughly two minutes to reviewing a debtor's file before approving and signing a complaint.

26. For the majority of accounts placed by debt buyers and creditors with Forster & Garbus between 2014 and 2016, Forster & Garbus's attorneys signed the complaints that initiated the Collection Suits without reviewing the following types of documentation in any form (electronically or otherwise) related to the purported debts: account applications, billing statements, copies of payments, payment histories, cash-advance check copies, the terms and conditions governing an account, and consumer correspondence.

27. Forster & Garbus's attorneys do not conduct reviews for warranties or disclaimers of warranties related to debt sales, and did not do so between 2014 and 2016. This means that debt buyers represented by Forster & Garbus may buy and seek to collect debts without any warranty that the debts are valid, accurate, or were owned by the seller. More broadly, this practice suggests that Forster & Garbus is generally unfamiliar with (and fails to conduct significant review of) its clients' contracts.

Forster & Garbus often files suit without investigating or otherwise verifying the facts it alleges.

28. When electronic records are received from a client, Forster & Garbus historically has checked to make sure that the firm has certain pieces of information: (1) the consumer's name, address, and social-security number; (2) name of the present creditor; (3) name of the original creditor; (4) original credit-card-account number; (5) date the account was opened; (6) date of charge off; and (7) account balance—information needed to complete a form complaint. Where supporting documentation has not been provided by one of its clients and a consumer has not requested substantiation of a debt, Forster & Garbus has generally not sought to investigate or otherwise verify information, such as the debt's validity or accuracy, before filing suit. It has not sought payment histories, account applications, billing statements, copies of payments, cash-advance check copies, the terms and conditions governing an account, or consumer correspondence.

29. In 2014, of the 45,621 accounts on which Forster & Garbus filed suit, Forster & Garbus possessed original or supporting documentation for only 8,958 of those accounts—19.6% of accounts.

30. In 2015, of the 34,103 accounts on which Forster & Garbus filed suit, Forster & Garbus possessed original or supporting documentation for only 14,965 of those accounts—43.9% of accounts.

31. In 2016, of the 20,006 accounts on which Forster & Garbus filed suit, Forster & Garbus possessed original or supporting documentation for only 15,113 of those accounts—75.5% of accounts. In 2016, Forster & Garbus began to possess more original or supporting documentation for its accounts before filing suit because clients stopped referring accounts to Forster & Garbus until those clients were able to ensure the firm had sufficient information to permit the firm to sue and obtain judgments under the regulations of the Office of Court Administration.

32. At least one former associate attorney with Forster & Garbus did not know, when he worked at Forster & Garbus, whether the information supplied by the firm's clients was accurate, and he considered the issue outside of his purview. He also did not review any materials other than what he received from the client before signing a complaint. This attorney signed complaints for 41,508 accounts from January 1, 2014 through December 31, 2016.

33. Forster & Garbus files debt-collection lawsuits on behalf of debt buyers, including: (1) many of the National Collegiate Student Loan Trusts; (2) Asset Acceptance, LLC; and (3) Midland Funding, LLC.

34. Asset Acceptance, LLC and Midland Funding, LLC are subsidiaries of Encore Capital Group, Inc. Encore Capital Group, together with Midland Credit Management, Inc. and Asset Acceptance Capital Corp., is one of the nation's largest debt buyers. In September 2015, Midland Funding (as well as Encore

Capital Group, Midland Credit Management, and Asset Acceptance Capital Corp.) stipulated to a Bureau consent order that found that it had attempted to collect debts that it knew, or should have known, were inaccurate or could not legally be enforced based on contractual disclaimers, past practices of debt sellers, or consumer disputes.

35. In September 2017, the Bureau took action against the 15 National Collegiate Student Loan Trusts and their debt collector, Transworld Systems, Inc., alleging that they sued consumers for private student-loan debt that the companies could not prove was owed or was too old to sue over.

36. Despite filing lawsuits on behalf of debt buyers, including debt buyers that have been accused of unlawful debt-collection practices such as alleging that consumers owe amounts that they do not actually owe, Forster & Garbus does not conduct reviews for contractual disclaimers related to debt sales, nor did it request and review supporting documentation for many of the accounts on which it filed suit between January 1, 2014 and December 31, 2016.

37. Forster & Garbus also files lawsuits on behalf of creditors that have been accused of unlawful debt-collection practices, including alleging that consumers owe amounts that they do not actually owe. For example, Forster files lawsuits on behalf of (1) Discover Bank; (2) Citibank, N.A.; and (3) Department Stores National Bank, an affiliate of Citibank, N.A. In July 2015, Discover and

affiliated entities stipulated to a Bureau consent order that found that, among other violations, they had overstated the minimum amount due for certain borrowers by incorrectly including interest on loans that were still in deferment and were not required to be paid. The Bureau also found that Discover acquired a portfolio of defaulted debt from Citibank but failed to comply with the consumer notices required by federal law. Specifically, the Bureau found that the company failed to provide consumers with information about the amount and source of the debt and the consumer's right to contest the debt's validity.

38. In February 2016, Citibank stipulated to a Bureau consent order that found that Citibank sold credit-card debt with inflated interest rates and failed to forward consumer payments promptly to debt buyers. The same day, Citibank, and other persons, including Department Stores National Bank, also stipulated to a Bureau consent order that found that they had falsified court documents filed in debt-collection cases in New Jersey state courts.

39. Despite filing lawsuits on behalf of creditors that have been accused of unlawful debt-collection practices, including alleging that consumers owe amounts that they do not actually owe, Forster & Garbus has filed suits against purported debtors on behalf of those creditors without investigating or verifying the summary information that served as the basis for those lawsuits.

40. Forster & Garbus is generally not sufficiently familiar with its clients' contracts and practices to reasonably rely on the limited summary information that its clients provide. For example, as noted above, Forster & Garbus's attorneys do not conduct reviews for warranties or disclaimers of warranties related to debt sales, and they did not do so between 2014 and 2016. This means that debt buyers represented by Forster & Garbus may buy and seek to collect debts without any warranty that the debts are valid, accurate, or were owned by the seller, and Forster & Garbus would not know.

Forster & Garbus uses a few designated signers.

41. Since 2014, Forster & Garbus has charged between one and five of its associate attorneys with the task of reviewing and signing the vast majority of complaints initiating the Collection Suits.

42. Forster & Garbus also has those attorneys make court appearances on a regular basis; prepare motions and opposition papers and affidavits in support of those motions and oppositions; conduct discovery; respond to orders to show cause; prepare for trial; engage in settlement negotiations; and review and sign other legal documents related to judgments and collecting on judgments.

43. Forster & Garbus's associate attorneys generally work 40 to 45 hours a week and manage at least 450 to 500 files, although the designated signers may have fewer cases.

44. In 2014, Forster & Garbus filed collection suits on 45,621 accounts. A single associate attorney signed complaints for 41,498 of those accounts, in addition to handling other tasks, including frequent court appearances.

45. In 2015, Forster & Garbus rotated four associate attorneys to serve as the primary signer of complaints at various periods during the year. That year, Forster & Garbus filed suit on 34,103 accounts. One associate attorney signed complaints for 14,586 of those accounts, another associate attorney signed complaints for 12,510 of those accounts, a third associate attorney signed complaints for 5,068 of those accounts, and the fourth associate attorney signed complaints for 1,927 of those accounts, in addition to handling other tasks, including frequent court appearances.

46. In 2016, Forster & Garbus filed collection suits on 20,006 accounts. A single associate attorney signed complaints for 18,173 of those accounts, in addition to handling other tasks, including frequent court appearances.

Count I
Defendant's Violations of the FDCPA
(Filing Deceptive Collection Suits)

47. The Bureau incorporates the allegations of paragraphs 1-46 of this Complaint.

48. The Collection Suits featured the signatures of attorneys, but they were prepared and filed without meaningful attorney involvement.

49. Forster & Garbus falsely represented to consumers that the Collection Suits were from attorneys when, in fact, attorneys were not meaningfully involved in preparing or filing the suits.

50. Section 807(3) and (10) of the FDCPA prohibits a debt collector from using any false, deceptive, or misleading representation or means to collect a debt, including the false representation or implication that any individual is an attorney or that any communication is from an attorney. 15 U.S.C. § 1692e(3), (10).

51. Forster & Garbus's acts and practices violate § 807(3) and 807(10) of the FDCPA, 15 U.S.C. § 1692e(3), (10).

Count II
Defendant's Violations of the CFPA
(Filing Deceptive Collection Suits)

52. The Bureau incorporates the allegations of paragraphs 1-46 of this Complaint.

53. Section 1036(a)(1)(A) of the CFPA prohibits a covered person from committing any act or omission in violation of a federal consumer-financial law. 12 U.S.C. § 5536(a)(1)(A).

54. Forster & Garbus's FDCPA violations, described above in Count I, therefore constitute violations of § 1036(a)(1)(A) of the CFPA. 12 U.S.C. § 5536(a)(1)(A).

Count III
Defendant's Deceptive Acts and Practices in Violation of the CFPA
(Filing Deceptive Collection Suits)

55. The Bureau incorporates the allegations of paragraphs 1-46 of this Complaint.

56. The complaints filed in the Collection Suits represented, directly or indirectly, expressly or by implication, that attorneys were meaningfully involved in preparing and filing the complaints.

57. In fact, the complaints filed in the Collection Suits were prepared and filed without meaningful attorney involvement.

58. Forster & Garbus's material misrepresentations, as set forth above, were likely to mislead consumers acting reasonably under the circumstances.

59. Sections 1031(a) and 1036(a)(1)(B) of the CFPA prohibit a covered person from engaging in any deceptive act or practice. 12 U.S.C. §§ 5531(a), 5536(a)(1)(B).

60. Forster & Garbus's acts and practices constituted deceptive acts or practices in violation of §§ 1031(a) and 1036(a)(1)(B) of the CFPA, 12 U.S.C. §§ 5531(a), 5536(a)(1)(B).

Demand for Relief

The Bureau requests that the Court:

a. permanently enjoin Forster & Garbus from committing future violations of the FDCPA and CFPA;

b. grant additional injunctive relief as the Court may determine to be just and proper;

c. award damages or other monetary relief against Forster & Garbus;

d. order Forster & Garbus to pay redress or restitution to consumers harmed by its unlawful conduct;

e. order Forster & Garbus to disgorge all ill-gotten gains;

f. impose civil money penalties on Forster & Garbus;

g. award costs against Forster & Garbus; and

h. award additional relief as the Court may determine to be just and proper.

Respectfully Submitted,

KRISTEN A. DONOGHUE
Enforcement Director

JEFFREY PAUL EHRLICH
Deputy Enforcement Director

OWEN P. MARTIKAN
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UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS
EASTERN DIVISION

In re:	)	Chapter 7
	)	Case No. 16-10236-MSH
BLAST FITNESS GROUP, LLC,	)	
Debtor	)	
GARY W. CRUICKSHANK, CHAPTER 7 TRUSTEE OF THE ESTATE OF BLAST FITNESS GROUP LLC,	)	
Plaintiff,	)	Adversary Proceeding No. 18-01011
v.	)	
HAROLD R. DIXON *et al.*,	)	
Defendants.	)	

MEMORANDUM OF DECISION ON MOTIONS TO DISMISS OF GOODWIN PROCTER LLP, JOHN R. LECLAIRE AND JEREMIAH J. SULLIVAN AND MOTION FOR PARTIAL SUMMARY JUDGMENT OF GOODWIN PROCTER LLP AND JOHN R. LECLAIRE

I. Introduction

In a thirty-count complaint,[1] Gary W. Cruickshank, the chapter 7 trustee of the bankruptcy estate of Blast Fitness Group, LLC ("BFG"), seeks damages and injunctive relief against forty-seven named[2] and dozens of unnamed John Doe defendants for allegedly depriving BFG of or diverting from it valuable assets and profit opportunities, ultimately leading to BFG's

[1] As amended by a First Amended Complaint (ECF #130).
[2] Since the filing of the complaint, four of the original named defendants have been dismissed from this proceeding by stipulation with the trustee.

filing of a petition under chapter 7 of the United States Bankruptcy Code on January 26, 2016.[3] This adversary proceeding was commenced two years after the petition date on January 26, 2018.

Several of the defendants, including the law firm of Goodwin Procter LLP ("Goodwin"), John R. LeClaire, a Goodwin partner, and Jeremiah J. Sullivan, a former Goodwin attorney (collectively, the "Goodwin Defendants") have filed motions to dismiss with Goodwin and Mr. LeClaire also filing a joint motion for partial summary judgment.[4] Specifically, Goodwin and Mr. LeClaire jointly moved to dismiss count I (fraudulent transfer under Bankruptcy Code § 548(a)(1)(B)),[5] count XII (legal malpractice), count XIII (breach of professional fiduciary duty), count XIV (violation of Mass. Gen. Laws. ch. 93A, §§ 2 and 11), count XXII (breach of contract pursuant to Bankruptcy Code §§ 544 and 550) and the correlative portions of count VII (turnover pursuant to Bankruptcy Code § 550), count VIII (unjust enrichment), count XXIX (attorneys' fees) and count XXX (costs). They moved for partial summary judgment with respect to count III (fraudulent transfer under Massachusetts Fraudulent Transfer Act ("MFTA") § 5(a)(2)), count IV (fraudulent transfer under MFTA § 6(a)),[6] count VIII (unjust enrichment)[7] and the correlative portions of count VII (turnover pursuant to Bankruptcy Code § 550). Mr. Sullivan seeks dismissal of all of the counts asserted against him, namely count VIII (unjust enrichment), count XII (legal malpractice), count XIII (breach of professional fiduciary duty), count XIV (violation of Mass. Gen. Laws. ch. 93A, §§ 2 and 11), count XXII (breach of contract

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[3] All references to the Bankruptcy Code or the Code are to 11 U.S.C. § 101 *et seq.*
[4] ECF ## 175, 213, and 177, respectively. These motions relate to the First Amended Complaint (ECF #130).
[5] Goodwin is a named defendant in count I, and Mr. LeClaire is not.
[6] Goodwin is a named defendant in counts III and IV, and Mr. LeClaire is not.
[7] Goodwin and Mr. LeClaire seek both dismissal and summary judgment on counts VII and VIII.

pursuant to Bankruptcy Code §§ 544 and 550) and the correlative portions of count XXIX (attorneys' fees) and count XXX (costs).

The causes of action asserted against the Goodwin Defendants fall into two categories: legal malpractice claims and unjust enrichment claims. The legal malpractice claims, including those styled as breaches of fiduciary duty, breach of contract and violation of Mass. Gen. Laws ch. 93A, arise from 2012 and 2013 corporate transactions involving BFG, defendant Harold R. Dixon, who controlled BFG, and others. Fees paid to Goodwin in 2013 form the basis for the unjust enrichment claims. The legal malpractice claims are the subject of the Goodwin Defendants' motions to dismiss while the unjust enrichment claims are the subject of the joint motion for partial summary judgment filed by Goodwin and Mr. LeClaire.

At the outset, I note that Trustee Cruickshank concedes that his claim under count I (fraudulent transfer under Bankruptcy Code § 548(a)(1)(B)) against Goodwin is time-barred and should be dismissed. I will, therefore, enter an order granting Goodwin and Mr. LeClaire's motion to dismiss count I as well as count VII, which seeks to effectuate any judgment that the trustee might recover under count I.[8] I will also enter an order allowing Mr. Sullivan's motion to dismiss count VIII (unjust enrichment) against him as the trustee failed to plead that Mr. Sullivan received any compensation from BFG or that he was in any way enriched. In addressing the remaining dispositive motions, I begin with the motions to dismiss.

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[8] Count VII for turnover under Bankruptcy Code § 550 is brought against the "Count I Defendants," among others. Count VII is thus applicable to Goodwin because of its status as a count I defendant. Hence, dismissal of count I against Goodwin necessitates the dismissal of count VII against it. The trustee's other fraudulent transfer counts against Goodwin (counts III and IV) contain references to Bankruptcy Code §§ 544(b) and 550(a) and would enable the trustee, if successful on either of those counts, to recover fraudulently transferred property from Goodwin.

II. Motions to Dismiss

A. Legal Standards

In ruling on the motions to dismiss, I must accept all well-pleaded factual allegations in the complaint as true, drawing all reasonable inferences in the trustee's favor. *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009); *Langadinos v. American Airlines, Inc.*, 199 F.3d 68, 69 (1st Cir. 2000). A claim cannot be dismissed if the trustee has demonstrated a "plausible entitlement to relief." *Sanchez v. Pereira–Castillo*, 590 F.3d 31, 41 (1st Cir. 2009) (citing *Iqbal*, 556 U.S. at 678). Conclusory or speculative allegations, however, must be disregarded. *Ocasio-Hernandez v. Fortuno-Burset,* 640 F.3d 1, 12 (1st Cir. 2011).

B. Trustee's Factual Allegations[9]

1. BFG

In 2010, Mr. Dixon met Steven Borghi, and the two discussed going into business together. ¶ 72. Mr. Borghi operated various Work Out World ("WOW") health clubs with Tony Beninati and, when Mr. Beninati died, with his widow, Elizabeth Beninati. ¶ 71. Mr. Borghi allowed Mr. Dixon to learn about the discount fitness center business by giving him access to the offices and proprietary information of WOW. ¶ 73.

On February 14, 2011, CapeCapital LLC, a Massachusetts limited liability company ("CapeCapital"), formed BFG.[10] ¶¶ 3, 74. CapeCapital was the sole manager of BFG, and Mr. Dixon, in turn, was the sole manager of CapeCapital. ¶ 3. At its peak, BFG owned and operated

[9] Factual allegations are cross-referenced to the relevant paragraphs (symbol ¶) of the first amended complaint.

[10] Although not specifically pleaded in the complaint, there is no dispute that BFG is a Massachusetts limited liability company.

over sixty fitness clubs bearing its name throughout the United States. (Intro., p. 2). At all relevant times, BFG acted at the direction of CapeCapital and Mr. Dixon. ¶ 92.

2. Dispute with Elizabeth Beninati

In 2011, Mr. Dixon and Mr. Borghi began operating various health clubs in New England using the WOW trade name, triggering a dispute with Ms. Beninati. ¶¶ 77, 79. Mr. Dixon, Mr. Borghi and BFG hired Mr. Dixon's longtime personal lawyer, defendant Mr. LeClaire of Goodwin, to represent them in negotiations with Ms. Beninati in April 2011. ¶ 80. Negotiations failed, and Ms. Beninati commenced a Massachusetts state court lawsuit against Mr. Dixon, Mr. Borghi and BFG on May 24, 2012, seeking millions of dollars in damages. ¶¶ 79, 376. Goodwin represented Mr. Dixon, BFG and Mr. Borghi in that litigation. ¶¶ 107, 376. In July 2014, the state court entered judgment against Messrs. Dixon and Borghi. ¶¶ 88, 315. Final judgment against them in excess of $4.5 million entered on January 9, 2015. ¶¶ 90, 317.

3. The Bally Transaction

In addition to its work on the Beninati litigation, Goodwin attorneys did other legal work for BFG starting in 2011, including in connection with BFG's acquisition and transfer of fitness clubs, the formation of various limited liability companies (LLCs) ancillary to these acquisitions and transfers and the drafting of corporate and transactional documents. ¶¶ 102-03, 105, 107. In 2012, while the Beninati dispute was going on, BFG was in negotiations with Bally Total Fitness Inc. to purchase thirty-nine work-out clubs and certain real estate. ¶ 105. The Goodwin Defendants acted as counsel to BFG and its wholly-owned subsidiary, Blast Fitness Acquisition, LLC ("Blast Acquisition"), in that transaction, and in that capacity participated in drafting an asset purchase agreement dated April 10, 2012. ¶¶ 106, 110, 113. Under the terms of the asset purchase agreement, BFG was to receive three pieces of commercial real estate from Bally

located in Maryland Heights, Missouri, West Hartford, Connecticut and Irving, Texas which were to be "sold pursuant to the terms of a separate purchase agreement . . . for an aggregate purchase price of $1,000,000 to an entity identified by [BFG] prior to Closing." ¶ 62, 118. Three of the thirty-nine work-out clubs being purchased by BFG operated at these locations. ¶¶ 114, 118.

According to emails exchanged between defendant Mr. Sullivan of Goodwin and Bally's counsel on April 12, 2012, the Goodwin Defendants knew by that date that Mr. Dixon wanted to designate entities not owned by BFG to take title to the Bally real estate. ¶¶ 131-133. On April 25, 2012, Mr. Dixon formed CapeCapital Maryland Heights, LLC, a Missouri LLC, CapeCapital West Hartford, LLC, a Connecticut LLC, and CapeCapital Irving, LLC, a Texas LLC, all of which were managed by Mr. Dixon and effectively owned by him. ¶¶ 18, 20, 22, 62, 145, 152, 157, 164. None of these entities was owned by BFG. ¶¶ 62, 163-64.

To raise part of the cash needed to complete the Bally transaction, the members of BFG agreed to sell a preferred membership interest in BFG to the Dixon Family Limited Partnership (an affiliate of Dixon). ¶¶ 138-39. The Goodwin Defendants drafted and presented to BFG and its members a member consent dated April 27, 2012, which provided in part:

> WHEREAS, the Members and Managers [of BFG] are seeking to raise additional capital for the Company for purposes including, but not limited [sic], financing the growth of the Company's business through the acquisition, from Bally Total Fitness Corporation, a Delaware corporation ("Bally") and certain of ts [sic] affiliates, of operating assets ***and real property associated with additional health club facilities*** (the "Bally Acquisition") ***by a direct subsidiary of the Company.*** (Emphasis added).

Id. This consent was presented to BFG's members at a time when Mr. Dixon and the Goodwin Defendants were already planning to transfer the Bally real estate to entities not owned by BFG. ¶ 140. Members of BFG, including Mr. Borghi, relied on the member consent when they

approved the admission of the Dixon Family Limited Partnership as a member of BFG and allowed the Bally transaction to move forward. ¶ 142. They did so believing that BFG would receive the Bally real estate. *Id.*

The Bally transaction closed on April 30, 2012,[11] and on or by that date, Bally had sold the Bally real estate to Mr. Dixon's LLCs, CapeCapital Maryland Heights, LLC, CapeCapital West Hartford, LLC and CapeCapital Irving, LLC. ¶¶ 146, 153, 158. Mr. Dixon used BFG funds to subsidize his purchase of the Bally real estate. ¶¶ 63, 178. Following the closings, CapeCapital and Mr. Dixon directed BFG and/or its subsidiaries to make above-market lease payments for the BFG clubs operating at the three Dixon-controlled properties, enabling Mr. Dixon to receive rent payments from BFG at inflated rates. ¶¶ 63, 166, 181-83. By 2014, all three real estate properties had been sold to third parties for prices in excess of their purchase prices. ¶¶ 148, 154, 159.

4. The Lexfit and Newfit Transactions

In late 2012, while the Beninati litigation was pending, Mr. Dixon began transferring profitable BFG clubs to new entities in order to shield them from BFG's creditors such as Ms. Beninati. ¶¶ 82, 273, 309. Lexfit, LLC, a Massachusetts LLC, and Newfit, LLC, a Delaware LLC, both managed by CapeCapital and Mr. Dixon, were two of these entities. ¶¶ 9, 10, 103, 273. On December 6, 2012, Mr. Dixon, Cape Capital and another defendant transferred sixteen of BFG's more profitable fitness clubs to Lexfit for no or nominal consideration. ¶¶ 274, 276. Goodwin is not alleged to have been involved in this transfer. On January 30, 2013, Mr. Dixon, Cape Capital and another defendant transferred an additional eight of BFG's more profitable clubs to Newfit. ¶ 283. Goodwin drafted the asset transfer agreement for the Newfit transfers. ¶

[11] This fact was not pleaded by the trustee but is not disputed.

288. BFG did not receive full consideration for these transfers. ¶ 285. Also on January 30, 2013, Lexfit transferred eight of the clubs received from BFG in the December 2012 transaction to Newfit for less than full consideration. ¶¶ 289, 291, 293. Goodwin drafted the transfer agreement even though BFG was not a party to the agreement. ¶ 292. Shortly after these transactions, in March 2013, Mr. LeClaire gave Mr. Dixon advice on how to protect his personal assets. ¶ 301. As late as December 2014, Goodwin had agreed to "move assets the right way out of BFG." ¶ 203.

C. Trustee's Claims Against the Goodwin Defendants

1. The Bally Transaction

The trustee alleges that Goodwin had a material, undisclosed and unwaivable conflict of interest in its dual representation of Mr. Dixon and BFG in connection with the Bally transaction which benefitted Mr. Dixon and harmed BFG. ¶¶ 65, 103, 137, 170-72. He also claims that the Goodwin Defendants failed to advise BFG and its principals regarding the duties of loyalty, care and candor. ¶¶ 123, 126, 129, 167. Specifically, the trustee alleges that the Goodwin Defendants knew the Bally real estate was being diverted away from BFG for the benefit of Mr. Dixon, they allowed the transfers to occur and they breached their duty to BFG when they failed to inform BFG and its members of Mr. Dixon's plan, and in fact purposely concealed from them that plan. ¶¶ 65, 119, 130, 168-169. According to the trustee, the Goodwin Defendants knowingly presented BFG's members with a fraudulent and misleading member consent on April 27, 2012, a date after they learned of Mr. Dixon's intention to divert the real estate. ¶ 141. The Goodwin Defendants' conduct, the trustee maintains, caused BFG significant damage in the form of inflated rent payments and lost cash used to subsidize Mr. Dixon's acquisition of the Bally real

estate and lost corporate opportunity as the properties were later sold for a significant profit by Mr. Dixon's LLCs. ¶¶ 63, 143, 166, 178, 181-82.

The Goodwin Defendants argue that even assuming the allegations against them are true, the claims relating to the Bally transaction are time-barred by the three year statute of limitations governing malpractice actions under Mass. Gen. Laws ch. 260, § 4.[12] As the Goodwin Defendants note, the statute of limitations begins to run as soon as "the plaintiff knows or reasonably should know that he or she has been harmed by the defendant's conduct." *Williams v. Ely*, 423 Mass. 467, 473 (1996). "The plaintiff need not know the extent of the injury or know that the defendant was negligent for the cause of action to accrue." *Id.* According to the Goodwin Defendants, BFG should have realized that it had not acquired the Bally real estate as of April 30, 2012, when the Bally transaction closed or, at the latest, when it began paying rent to the Dixon entities which had acquired the properties. In their view the statute had run by mid-2015, many months before BFG's bankruptcy filing.

The trustee asserts that the statute of limitations was tolled. First he argues that under the doctrine of continuing representation, the statute of limitations did not begin to run until December 2014 when Goodwin, Mr. LeClaire, and presumably Mr. Sullivan, ended their representation of BFG. Thus, he argues, the statute of limitations under Mass. Gen. Laws ch. 260, § 4 had not run as of January 26, 2016, when BFG filed its bankruptcy petition, and was extended to January 26, 2018, by Bankruptcy Code § 108(a).[13]

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[12] The statute provides: "Actions of contract or tort for malpractice, error or mistake against attorneys . . . shall be commenced only within three years next after the cause of action accrues." Mass. Gen. Laws ch. 260, § 4. Actions under Chapter 93A are subject to a four year statute of limitations. *See* Mass. Gen. Laws ch. 260, § 5A.

[13] Code § 108(a), in part, provides: "(a) If applicable nonbankruptcy law . . . fixes a period within which the debtor may commence an action, and such period has not expired before the date of the filing of the petition, the trustee may commence such action only before the later

The continuing representation doctrine tolls the statute of limitations for professional malpractice claims until the professional has ceased its representation of the injured party. The Massachusetts Supreme Judicial Court summarized the doctrine in *Lyons v. Nutt*, 436 Mass. 244, 249–50 (2002).

> The continuing representation doctrine, which we adopted in *Murphy v. Smith,* 411 Mass. 133, 579 N.E.2d 165 (1991), recognizes that a person seeking professional assistance has a right to repose confidence in the professional's ability and good faith, and realistically cannot be expected to question and assess the techniques employed or the manner in which the services are rendered. . . . The doctrine has no application, however, where the client actually knows that he suffered appreciable harm as a result of his attorney's conduct. If the client has such knowledge, then there is no innocent reliance which the continued representation doctrine seeks to protect.

Id. (internal citations and quotation marks omitted).

In order for the continuing representation doctrine to apply, however, the continuing representation must be with respect to the same matter. *Hodas v. Sherburne, Powers & Needham, P.C.*, 938 F. Supp. 58, 60 (D. Mass. 1996) (holding that client's complaint sufficiently invoked continuing representation doctrine where allegations of malpractice pertained to the "matters that form[ed] the basis of the allegations"); *see also Cambridge Biotech Corp. v. Deliotte & Touche*, Civ. A. No. 96-1480-A, 1997 WL 42516, at *2 (Mass. Super. Ct. Jan. 28, 1997) (quoting *F.D.I.C. v. Deloitte & Touche*, 834 F. Supp. 1129, 1148-1149 (E.D. Ark. 1992)) ("The continuous treatment we mean, however, is treatment for the same or related illnesses or injures, continuing after the alleged acts or malpractice, not mere continuity of a general physician-patient relationship."); *DeGiacomo v. Tobin & Assocs., P.C. (In re Inofin Inc.)*, No.

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of--
(1) the end of such period, including any suspension of such period occurring on or after the commencement of the case; or
(2) two years after the order for relief." 11 U.S.C. § 108(a).

12-1091, 2012 WL 5457415, at *24 (Bankr. D. Mass. Nov. 8, 2012) (quoting *Cambridge Biotech*, 1997 WL 42516 at *2). Here it was not.

While the trustee points to Goodwin and Mr. LeClaire's representation of BFG in the Lexfit and Newfit transactions and in the Beninati litigation which continued into 2014, these matters were separate and distinct from the Bally transaction, and they did not arise out of or relate in any way to the Bally transaction. The Goodwin Defendants' representation of BFG in the Bally transaction ended with the consummation of that transaction in April 2012. Thus, the continuing representation doctrine does not toll the statute of limitations here.

The trustee raises a second argument as to why the statute of limitations was tolled. He asserts that knowledge of the alleged harm was fraudulently concealed from BFG thereby tolling the statute of limitations under Mass. Gen. Laws ch. 260, § 12.[14] "When a defendant fraudulently conceals a cause of action from the knowledge of a plaintiff, the statute of limitations is tolled under G.L. c. 260, § 12, for the period prior to the plaintiff's discovery of the cause of action." *Demoulas v. Demoulas Super Markets, Inc.*, 424 Mass. 501, 519 (1997). The trustee relies on the Goodwin Defendants' preparation of the member consent falsely stating that a direct subsidiary of BFG would be acquiring the Bally real estate. The trustee alleges that the Goodwin Defendants knew prior to the preparation of the member consent that Mr. Dixon intended to designate non-BFG entities to acquire the Bally real estate and that they "purposefully concealed" that plan from the members of BFG. ¶ 130-31.

[14] The statute provides: "If a person liable to a personal action fraudulently conceals the cause of such action from the knowledge of the person entitled to bring it, the period prior to the discovery of his cause of action by the person so entitled shall be excluded in determining the time limited for the commencement of the action." Mass. Gen. Laws ch. 260, § 12.

The Goodwin Defendants assert that BFG knew or should have known by April 30, 2012, when the Bally transaction closed, that BFG had not acquired the Bally real estate. They point to Mr. Dixon's knowledge of the real estate transfers, which they assert should be imputed to BFG, and to BFG's payment of rent to the Dixon-controlled owners of the properties. Additionally, they blame the inaccurate members' consent on a "scrivener's error." These defenses are insufficient to overcome the tolling provisions of Mass. Gen. Laws ch. 260, § 12.

"Where a fiduciary relationship exists, the failure adequately to disclose the facts that would give rise to knowledge of a cause of action constitutes fraudulent conduct and is equivalent to fraudulent concealment for purposes of applying [Mass. Gen. Laws ch. 260,] § 12." *Demoulas,* 424 Mass. at 519. The Goodwin Defendants drafted the member consent and presented it to the members for signature as BFG's attorneys. A fiduciary relationship existed between BFG and the Goodwin Defendants. Scrivener's error or not, the Goodwin Defendants had a duty to inform the members of BFG other than Mr. Dixon that BFG was paying for but not acquiring the Bally real estate. That BFG paid rent for the three locations is irrelevant as the disinterested members of BFG, even if they were aware of the rental payments, would not have been required to make independent inquiry to determine that the landlords were not BFG-controlled entities. *Demoulas*, 424 Mass. at 520. Without the disinterested BFG members having had actual knowledge, the fraudulent concealment continued. *Id*. at 519.

With respect to the contention that Mr. Dixon's knowledge about the real estate transfer should be imputed to BFG, "an agent's knowledge of his own unauthorized acts is not imputed to the principal when the agent has acted fraudulently toward the principal and is engaged in an independent fraudulent act from which the principal does not benefit." *Sunrise Props., Inc. v. Bacon, Wilson, Ratner, Cohen, Salvage, Fialky &*

Fitzgerald, P.C., 425 Mass. 63, 67, (1997) (citing *Tremont Trust Co. v. Noyes*, 246 Mass. 197, 207, 141 N.E. 93 (1923) and Restatement (Second) of Agency § 282 (Am. Law Inst. 1958) ("[a] principal is not affected by the knowledge of an agent in a transaction in which the agent secretly is acting adversely to the principal and entirely for his own or another's purposes . . . . "); *see also GTE Prods. Corp. v. Broadway Elec. Supply Co.*, 42 Mass. App. Ct. 293, 299–300 (1997) ("Indeed in cases like this where the agent and a third party have colluded to defraud the principal, the agent's knowledge generally is *not* imputed to the principal. . . . The rationale for imputing an agent's knowledge to his principal in order to do justice to an innocent third party is totally lacking here.") (emphasis in original).

In *Demoulas*, the Massachusetts Supreme Judicial Court recognized the "adverse domination" doctrine. "Under this doctrine, the statute of limitations is tolled while a corporate plaintiff continues under the domination of the wrongdoers." *Demoulas*, 424 Mass. at 523 (citing 3A William Meade Fletcher et al., Law of Private Corporations § 1306.20 (perm. ed. 1994 & Supp. 1996)). As noted in *Demoulas* there are several versions of the doctrine.

> The most common one is the "disinterested majority" test, under which the statute does not run until a majority of board members are disinterested and the board is therefore able to act on behalf of the corporation against the wrongdoers. . . . Other courts have proposed a stricter "complete domination" test, under which a plaintiff seeking to toll the statute of limitations must show that the culpable directors had full, complete, and exclusive control for the period at issue, so that there was no director or shareholder with knowledge who could have induced the corporation to bring an action.

Id. at 523-24 (internal citations omitted).

Although Mr. Dixon, the sole manager of CapeCapital, which, in turn, was the sole manager of BFG, knew BFG was not acquiring the Bally real estate, that knowledge is not

enough to prevent the tolling of the statute of limitations. The Goodwin Defendants' motions to dismiss must be denied with respect to the counts in the complaint related to the Bally transaction.

2. The Lexfit and Newfit Transactions

The trustee alleges that Goodwin and Mr. LeClaire were in a conflict of interest position in violation of their duty of loyalty to BFG when they represented multiple parties in the Lexfit and Newfit transactions, which aided Mr. Dixon and harmed BFG. ¶¶ 288, 292. He adds that the Lexfit and Newfit transactions furthered fraudulent transfers by BFG and breaches of duty by Dixon that were already taking place. ¶ 292. The trustee alleges that this conduct gives rise to legal malpractice (count XII), breach of professional fiduciary duty (count XIII) and breach of contract (count XXII).

The parties dispute whether the complaint alleges sufficient facts to show that Goodwin's actions in the Lexfit and Newfit transactions breached a duty to BFG and, if there was a breach, whether the breach caused harm to BFG.[15] Relying on Massachusetts Rule of Professional Conduct 1.2(a),[16] the Goodwin Defendants allege that there was no breach of duty in the Lexfit and Newfit transactions because Mr. Dixon, through Cape Capital, BFG's manager, directed the

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[15] For a plaintiff to succeed on a legal malpractice claim, the plaintiff must show:

> "(1) an attorney-client relationship; (2) a duty to exercise a reasonable degree of care and skill in the performance of the attorney's legal duties; (3) a violation of this duty; and (4) reasonably foreseeable harm caused by the attorney's negligence."

Alicea v. Commonwealth, 466 Mass. 228, 234 n.9 (2013).

[16] The Rule provides in relevant part: "A lawyer shall seek the lawful objectives of his or her client through reasonably available means permitted by law and these Rules." Mass. R. Prof. C. 1.2(a).

transfers. The Goodwin Defendants maintain that the firm was simply carrying out the lawful instructions of its client, BFG. Additionally, they argue that there was no conflict of interest in representing both BFG and Mr. Dixon, asserting that it is not unlawful to represent a Massachusetts LLC while simultaneously representing its controlling equity holder and that it is common for law firms to represent organizations in transactions designed to favor an equity holder. The trustee, on the other hand, alleges that there are times when a lawyer must refuse to carry out his client's instructions, and this was one of those times. He relies on Mass. R. Prof. C. 1.2(d)[17] and alleges that Goodwin assisted Mr. Dixon in conduct it knew or should have known was fraudulent. He also asserts that BFG's and Mr. Dixon's business interests and objectives were in conflict— BFG desired to earn profit for its owners, while Mr. Dixon sought to enrich himself by shielding assets from creditors, including Ms. Beninati. This, he contends, was a conflict of interest that should have prevented Goodwin from representing both parties.

Clearly Goodwin and Mr. LeClaire owed a duty of undivided loyalty to BFG, *see Bartle v. Berry*, 80 Mass. App. Ct. 372, 378 (2011) ("There is no question that an attorney owes a duty of undivided loyalty to his client."), and the conflict presented by their simultaneous representations of other potentially adverse parties may have breached that duty. It is enough at this stage of the proceeding that the complaint plausibly states such a claim.

Alternatively, the Goodwin Defendants argue that even if there was a breach of duty, there was no causation, and accordingly the malpractice claim must fail. For causation to exist in a legal malpractice claim, the plaintiff must show that it would have been better off had the attorney not breached his duty. *See, e.g.*, *Shimer v. Foley, Hoag & Eliot LLP*, 795 N.E.2d 599,

[17] The Rule provides in relevant part: "A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent . . . ." Mass. R. Prof. C. 1.2(d).

606 (Mass. App. Ct. 2003) (noting plaintiff must show that it suffered loss due to attorney's negligence); *McCann v. Davis, Malm & D'Agostine*, 423 Mass. 558, 560 (1996) (denying relief because the plaintiff was not harmed by the lawyer's negligence); *Colucci v. Rosen, Goldberg, Slavet, Levenson & Wekstein, P.C.*, 515 N.E.2d 891, 895 (Mass. App. Ct. 1987) ("A client in a malpractice action based on an allegation of attorney negligence must show that, but for the attorney's failure, the client probably would have been successful in the prosecution of the litigation giving rise to the malpractice claim.").

The trustee alleges that there were two harms to BFG directly resulting from the Goodwin Defendants' malpractice. First, the trustee alleges that BFG was harmed by receiving less than fair market value for the clubs transferred in the Lexfit and Newfit transactions. ¶¶ 283-85, 306. Second, he alleges the transfers deprived BFG of the revenue from its most profitable clubs. ¶¶ 66, 283. Goodwin argues that despite these allegations, the complaint does not adequately plead causation because it does not allege what would have happened had it acted differently. The complaint, however, alleges that other unconflicted attorneys would not have let the transactions occur and without the transfers of its more profitable clubs, BFG would have been in a stronger financial position. ¶¶ 66, 68. Therefore, the trustee's amended complaint states a claim upon which relief can be granted, and the Goodwin Defendants' motions to dismiss must be denied with respect to the Lexfit and Newfit transactions as related to counts XII, XIII, and XXII.[18]

[18] The three counts are so "inextricably intertwined" that as goes one, so go the rest. *See Cholfin v. Gordon*, No. CA 943623C, 1996 WL 1185106, at *4 (Mass. Super. Ct. Jan. 2, 1996); *see also Herbert A. Sullivan, Inc. v. Utica Mut. Ins. Co.*, 439 Mass. 387, 397 n.7 (2003) ("There is little practical difference between the elements of proof in a tort action for negligence and a contract action for the negligent provision of legal services."); *Thomas v. Mass. Bay Transp. Auth.*, 389 Mass. 408, 409-410 (1983) (noting the overwhelming similarities between contract and negligent tort claims in personal injury suits).

3. Mass. Gen. Laws ch. 93A

To successfully state a claim under Mass. Gen. Laws ch. 93A, §11, a plaintiff must establish:

> (1) that the defendant engaged in an unfair method of competition or committed an unfair or deceptive act or practice, as defined by G.L. c. 93A, § 2, or the regulations promulgated thereunder; (2) a loss of money or property suffered as a result; and (3) a causal connection between the loss suffered and the defendant's unfair or deceptive method, act, or practice.

Auto Flat Car Crushers, Inc. v. Hanover Ins. Co., 469 Mass. 813, 820 (2014) (footnote omitted); *see also 477 Harrison Ave., LLC v. Jace Boston, LLC*, 477 Mass. 162, 171-172 (2017) (quoting *Auto Flat*).

Courts have discretion in determining what constitutes an unfair or deceptive act or practice, but should consider: "1) whether the practice falls within the penumbra of common-law, statutory, or other established concepts of unfairness; 2) whether it is immoral, unethical, oppressive, or unscrupulous; and 3) whether it causes substantial injury to consumers, competitors, or other businessmen." *Bridge Over Troubled Waters, Inc. v. Argo Tea, Inc.*, 220 F. Supp. 3d 213, 220 (D. Mass. 2016) (quoting *Boyle v. Int'l Truck and Engine Corp.*, No. 01-10039-DPW, 2002 WL 823810, at *6 (D. Mass. Apr. 23, 2002)). Despite the court's discretion in determining unfair or deceptive acts or practices, negligent legal representation alone does not satisfy the requirements of ch. 93A. *See Meyer v. Wagner*, 429 Mass. 410, 423-24 (1999). Absent conduct involving dishonesty, fraud, deceit or misrepresentation, legal malpractice does not constitute a ch. 93A violation. *Poly v. Moylan*, 423 Mass. 141, 151 (1996); *Spenlinhauer v. Kane*, No Civ. A. 9601ST-044887, 1998 WL 474170, at *2 (Mass. App. Ct. Aug. 4, 1998); *O'Brien v. Kelly*, No. 05-P-1469, 2007 WL 121337, at *2 (Mass. App. Ct. Jan. 18, 2007).

The trustee alleges the Goodwin Defendants had a duty to act loyally to BFG due to their attorney-client relationship. He points to the Bally, Lexfit and Newfit transactions as evidence of

the breach of that loyalty, arguing that it is a fair inference that Goodwin and Mr. LeClaire consistently remained loyal to Mr. Dixon to the detriment of BFG and its members and that they intended to deceive BFG's members by failing to inform them of their loyalty to Mr. Dixon, which was a violation of ch. 93A. ¶¶ 68, 167, 169, 171, 288. By Goodwin's representation of both Mr. Dixon and BFG in transactions to the detriment of BFG, the trustee's complaint alleges sufficient facts to plausibly support the conclusion that the Goodwin Defendants had a conflict of interest that was unethical under Massachusetts law, *see* Mass. R. Prof. C. 1.7,[19] coupled with an intent to deceive its client, BFG. The trustee's complaint therefore states a claim upon which relief can be granted under ch. 93A, and the Goodwin Defendants' motions to dismiss will be denied with respect to that count. *See generally Karasavas v. Gargano*, 31 Mass. L. Rptr. 624, (Mass. Super. Ct. 2014), *aff'd*, 87 Mass. App. Ct. 1125 (Mass. App. Ct. 2015) (holding that attorney's charging of excessive fee and handling of client funds in violation of ethical

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[19] The Rule provides:

> (a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:
>
> > (1) the representation of one client will be directly adverse to another client; or
> >
> > (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.
>
> (b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:
>
> > (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;
> >
> > (2) the representation is not prohibited by law;
> >
> > (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and
> >
> > (4) each affected client gives informed consent, confirmed in writing.

Mass. R. Prof. C. 1.7.

requirements constituted unfair or deceptive acts or practices in violation of Mass. Gen. Laws ch. 93A).

4. Unjust Enrichment Claim Against Mr. Sullivan

The trustee asserts a claim for unjust enrichment (count VIII) against all defendants. Although he specifically alleges that Goodwin and Mr. LeClaire received substantial payments from BFG to which they were not entitled, *see* ¶¶ 176, 369, he has not done so with respect to Mr. Sullivan and has identified him as a former Goodwin attorney, not a Goodwin partner. In the absence of any allegation against Mr. Sullivan that he was unjustly enriched or received fees paid by or behalf of BFG, I will dismiss count VIII as against him.

III. Motion for Partial Summary Judgment

A. Legal Standards

Fed. R. Civ. P. 56 governs motions for summary judgment in bankruptcy proceedings, per Fed. R. Bank. P. 7056. "The court shall grant summary judgment if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(a). "A 'genuine' issue is one supported by such evidence that 'a reasonable jury, drawing favorable inferences,' could resolve it in favor of the nonmoving party." *Triangle Trading Co. v. Robroy Indus., Inc.*, 200 F.3d 1, 2 (1st Cir. 1999) (quoting *Smith v. F.W. Morse & Co*., *Inc.* 76 F.3d 413, 428 (1st Cir. 1996)). "Material" means that a disputed fact has "the potential to change the outcome of the suit" under the governing law if the dispute is resolved in favor of the nonmovant. *McCarthy v. Nw. Airlines, Inc*., 56 F.3d 313, 315 (1st Cir. 1995).

B. Claims Against Goodwin and Mr. LeClaire

It is undisputed that on January 25, 2013, BFG wired $175,000 to Goodwin, and on August 30, 2013, Blast Acquisition wired $375,000 to Goodwin. The trustee seeks to avoid those payments as fraudulent transfers under sections 5 and 6 of the Massachusetts Fraudulent Transfer Act[20] ("MFTA") (counts III and IV) and to recover the payments under Bankruptcy Code § 550 (count VII).[21] He also seeks to recover them on a claim of unjust enrichment from property of the estate (count VIII).

Goodwin and Mr. LeClaire seek partial summary judgment on these counts, asserting that BFG received reasonably equivalent value for both transfers in the form of legal services rendered by Goodwin and that the second transfer was not made by the debtor, BFG. They also seek summary judgment with respect to the unjust enrichment count, asserting that it is nothing more than a recycled avoidance claim which fails as a matter of law because the trustee is not entitled to a declaration of an interest in transfers when he cannot avoid those transfers.

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[20] Section 5(a) of the MFTA provides, in part: "A transfer made or obligation incurred by a debtor is fraudulent as to a creditor . . . if the debtor made the transfer or incurred the obligation: (1) with actual intent to hinder, delay, or defraud any creditor of the debtor; or (2) without receiving a reasonably equivalent value in exchange for the transfer or obligation . . . ." Mass. Gen. Laws ch. 109A, § 5(a).

Section 6(a) of the MFTA provides: "A transfer made or obligation incurred by a debtor is fraudulent as to a creditor . . . if the debtor made the transfer or incurred the obligation without receiving a reasonably equivalent value in exchange for the transfer or obligation and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation." Mass. Gen. Laws ch. 109A, § 6(a).

[21] As stated above, count VII (turnover under Bankruptcy Code § 550) has been dismissed against Goodwin due to the dismissal of count I against it. Notwithstanding the dismissal of that count, the trustee would still be able to recover fraudulently transferred property from Goodwin under counts III and IV (fraudulent transfers under MFTA) should he ultimately prevail against it on either of those two counts as they contain references to Bankruptcy Code §§ 544(b) and 550(a).

The trustee counters that additional discovery will permit him to demonstrate a genuine dispute over whether BFG or Blast Acquisition paid the $375,000 to Goodwin and whether there was reasonably equivalent value given for both transfers. *See* Fed. R. Civ. P. 56(d), made applicable to this proceeding by Fed. R. Bankr. P. 7056. He maintains that he reasonably expects discovery to produce useful and material evidence on the claims in question, and that I should not permit Goodwin and Mr. LeClaire to parachute away from them before completion of discovery by using summary judgment to avoid claims they could not otherwise escape through a motion to dismiss.

Rule 56(d) provides:

> d) **When Facts Are Unavailable to the Nonmovant.** If a nonmovant shows by affidavit or declaration that, for specified reasons, it cannot present facts essential to justify its opposition, the court may:
>
> (1) defer considering the motion or deny it;
>
> (2) allow time to obtain affidavits or declarations or to take discovery; or
>
> (3) issue any other appropriate order.

Fed. R. Civ. P. 56(d). "[C]ourts should construe motions that invoke the rule generously, holding parties to the rule's spirit rather than its letter." *Resolution Tr. Corp. v. N. Bridge Assocs., Inc.*, 22 F.3d 1198, 1203 (1st Cir. 1994).

> A litigant who desires to invoke Rule 56(f) must make a sufficient proffer. In all events, the proffer should be authoritative; it should be advanced in a timely manner; and it should explain why the party is unable currently to adduce the facts essential to opposing summary judgment. . . . When, as is often the case, the reason relates to incomplete discovery, the party's explanation must take a special form: it should show good cause for the failure to have discovered the facts sooner; it should set forth a plausible basis for believing that specified facts, susceptible of collection within a reasonable time frame, probably exist; and it should indicate how the emergent facts, if adduced, will influence the outcome of the pending summary judgment motion.

Id. (internal citations omitted).[22]

The trustee's counsel submitted an affidavit setting forth his efforts to obtain discovery related to the two payments received by Goodwin as well as information as to the source of a third payment. The trustee points to Blast Acquisition's bank statement for August 2013 which reflects an incoming wire transfer of $375,000 on August 23, a week before the outgoing wire transfer to Goodwin, suggesting that Blast Acquisition was not the source of those funds. The trustee seeks Goodwin's invoices and detailed time records to determine the nature of the legal services and whether those services provided any benefit to BFG. The trustee also pointed in his affidavit to a payment of $800,000 made by Newfit to Goodwin. The trustee seeks discovery to determine why and at whose direction that payment was made.

Goodwin and Mr. LeClaire point to the trustee's delay of almost two years after his appointment before bringing this adversary proceeding as undercutting the trustee's claim for additional discovery. The relevant issue, however, is not whether the trustee waited two years to bring this adversary proceeding but whether, upon the commencement of the proceeding, the trustee delayed in seeking discovery. He clearly did not. The affidavit of the trustee's counsel establishes his diligent but as yet unsuccessful efforts to obtain documents responsive to his inquiry into whether BFG paid legal fees to Goodwin for services provided to others. Until the trustee has been provided with the necessary discovery, the motion for partial summary judgment is premature and will be denied without prejudice.

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[22] *Resolution Tr. Corp*. discusses then-Rule 56(f), which is now Rule 56(d). Rule 56(d) "carrie[d] forward without substantial change the provisions of former subdivision (f)." Fed. R. Civ. P. 56 advisory committee's note to 2010 amendments.

IV. Conclusion

Based on the foregoing, an order shall enter granting the motion to dismiss of Goodwin and Mr. LeClaire with respect to counts I and VII of the complaint against Goodwin, and denying the Goodwin Defendants' motions to dismiss with respect to counts XII, XIII, XIV, XXII and the correlative portions of counts VIII, XXIX and XXX, except that an order shall enter allowing Mr. Sullivan's motion to dismiss count VIII against him. An order denying without prejudice the motion for partial summary judgment will also enter.

Dated: January 8, 2019

By the Court,

Melvin. S. Hoffman
United States Bankruptcy Judge

Counsel Appearing: Ilyas J. Rona, Esq.
Milligan Rona Duran & King LLC
Boston, MA
for the plaintiff, Gary W. Cruickshank, Trustee of the Estate of Blast Fitness Group, LLC

Peter Sabin Willett, Esq.
Morgan, Lewis & Bockius LLP
Boston, MA
for defendants, Goodwin Procter LLP, John R. LeClaire and Jeremiah J. Sullivan

UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF FLORIDA
Miami Division

Case Number: 18-24578-CIV-MORENO

RICHARD I. CLARK AS TRUSTEE FOR
MATTHEW WORTLEY TRUST d/b/a X CO.
FINANCE, *et al.*,

Appellants,

vs.

SONEET R. KAPILA, Trustee in Bankruptcy
for TRAFFORD DISTRIBUTING CENTER,
INC.,

Appellee.
_______________________________________/

ORDER REVERSING AND REMANDING FOR NEW TRIAL

Appellant Richard I. Clark, as trustee for the Matthew Wortley Trust d/b/a X. Co. Finance, and appearing in various other capacities, appeals the final judgment and orders entered below in favor of the Appellee, Soneet R. Kapila, the trustee in Bankruptcy for Trafford Distributing Center, Inc.[1] Specifically, Appellant appeals the bankruptcy court's (1) Findings of Fact and Conclusions of Law, (2) Final Judgment in Favor of Plaintiff (Appellee), and (3) Order Denying Motions for Rehearing, Motions to Alter or Amend Final Judgment and Findings of Fact and Conclusions of Law, Motions to Disqualify and for Leave to Take Discovery.

Appellant argues, among other things, that the initial bankruptcy judge who presided over the case failed to timely recuse himself due to the fact that his fiancé had been recently hired by

[1] The main underlying bankruptcy case below is *In re Trafford Distributing Center, Inc.*, No. 11-23492 (Bankr. S.D. Fla. filed June 13, 2008). The adversary proceeding giving rise to this case is *Kapila v. Richard I. Clark as Trustee for Matthew Wortley Trust d/b/a/ X. Co. Finance, et al.*, Adv. No. 11-01996 (Bankr. S.D. Fla. filed Nov. 12, 2008).

the law firm representing Appellee. Consistent with Judge Altonaga's recently issued order in a related appeal,[2] this Court finds in favor of Appellant and holds that the initial bankruptcy judge should have recused himself before adjudicating the merits of this case. Accordingly, the Court vacates the final judgment and orders below, and remands the case for a new trial.

I. BACKGROUND

A. The Relevant Adversary Proceeding

The relevant facts of this case begin on November 12, 2008, when Appellee initiated an adversary proceeding against Appellant seeking to determine the validity, priority, and amount of any lien Appellant may allegedly possess against the debtor's estate, Trafford Distributing Center, Inc., and, to the extent a lien does exist, to avoid and recover preferential and fraudulent transfers. On the same day that Appellee filed his complaint, Appellant wrote a demand letter to Appellee explaining he had "proof that this Trust through my Trust Account paid over $231,000 to Trafford under Factoring Agreements by which XCo purchased the receivables from Trafford." Appellant further noted that "[t]he trust is [now] owed $231,000 plus it intends to get paid from Heinz. XCo is the owner of the Heinz receivables and will be pursuing Heinz for the balance owed." A month before, Appellee had initiated adversary proceedings against H.J. Heinz Company in which it sought to directly recover the disputed Heinz receivable on behalf of the debtor.[3]

In response to the November 12 letter, Appellee filed an amended complaint seeking injunctive relief to prohibit Appellant from collecting on the Heinz receivable outside the context of the bankruptcy proceedings. Appellee claimed that the letter violated the automatic stay of the

[2] *See Liberty Props. at Trafford LLC, et al., v. Kapila*, No. 18-24579 (S.D. Fla. Aug. 9, 2019). While the main holding of Judge Altonaga's case is directly applicable to this case, that case stems from a different adversary proceeding: *Kapila v. Liberty Props. at Trafford, LLC, et al.*, Adv. No. 11-01997 (Bankr. S.D. Fla. filed Nov. 21, 2008).

[3] *See Kapila v. H.J. Heinz Co.*, Adv. No. 08-01723 (Bankr. S.D. Fla. filed Oct. 21, 2008).

Bankruptcy Code, 11 U.S.C. § 362. Appellee also filed an emergency *ex parte* motion for a temporary restraining order based on the same letter, arguing that the "matter is not capable of being resolved by consent." On November 24, 2008, the bankruptcy judge, Judge John K. Olson, granted the motion. However, at a December 17, 2008 hearing, he dissolved the restraining order since Appellant, in the interim, had made both written and verbal affirmations that he would not be seeking to collect on the Heinz receivable outside the bankruptcy context. Upon hearing these promises, Judge Olson asked Appellee, "so what are we fighting about for purposes of today? . . . With the concession that the litigation over the receivables and, indeed, perhaps collection efforts themselves, will be conducted here, and that the defendants in your litigation will take no action against Heinz except with leave of this Court . . . what do you need an injunction for?"

In June 2009, Appellant submitted its Proof of Claim, asserting he owned the Heinz receivable pursuant to a Factoring Agreement between X Co. and the debtor. The following summer, Appellee moved for summary judgment, attacking the validity of Appellant's claim to the Heinz receivable and seeking an "an injunction to foreclose the Defendants from attempting to collect the Debtor's receivables." Despite evidence including the Factoring Agreement and receipts of wire transfers made from X Co. to the debtor, Judge Olson held that Appellant did not have a claim to the Heinz receivable since the lien was unperfected. He then entered a permanent injunction, based on the November 12 letter, prohibiting Appellant from collecting the receivable. Finally, and again based on the November 12 letter, he found that Appellant "willfull[y]" violated the automatic stay, and awarded attorney's fees and costs as a sanction. The judge did so even though Appellee conceded at the summary judgment hearing that "we did not seek summary judgment on the issue of whether or not there is any basis, as far as a stay violation here." Appellee, by way of attorney Michael R. Bakst of the Ruden, McClosky, Smith, Schuster & Russell, P.A.

law firm, accordingly submitted an affidavit of fees and costs totaling $77,082.50.

Appellant sought reconsideration, and Judge Olson partially vacated his order regarding ownership of the Heinz receivable. He did not, however, revisit his entry of a permanent injunction or finding that Appellant willfully violated the automatic stay and therefore merited sanctions. On June 30, 2010, following a two-day bench trial, Judge Olson entered his Findings of Fact and Conclusions of Law and Final Judgment in Favor of Plaintiff. In the former, Judge Olson concluded that Appellant did not own the Heinz receivable in any of his capacities, and that the "multiple alleged trusts are [not] anything other than *ex post facto* fabrications designed to drain the bankruptcy estate." In the latter, Judge Olson repeated his earlier finding that Appellant willfully violated the automatic stay, and noted that he would again be awarding fees and costs as a sanction. Appellant responded, noting that Appellee's affidavit of fees "seems to be seeking all fees and costs incurred in connection with this Adversary, as well as other Adversaries," rather than seeking fees and costs associated only with the violation of the automatic stay—which, Appellant argued, meant efforts in connection with seeking the temporary restraining order.

B. Following Final Judgment, Defendants Move to Disqualify Judge Olson

In August 2010, Appellant discovered that during the summer of 2009, when motions for summary judgment were under consideration by Judge Olson, Appellee's counsel, the Ruden McClosky law firm, made contact with, negotiated with, and ultimately hired the judge's fiancé: George Fender. Upon learning these facts, the defendants across the multiple adversary proceedings, including Appellant, moved to disqualify the judge pursuant to 28 U.S.C. § 455(a), and 28 U.S.C. §§ 455(b)(5)(ii) & (iii). The defendants explained that "[t]he court . . . appears to have an intimate relationship with Mr. Fender," noting that the two lived together while employment negotiations with the Ruden McClosky firm were taking place in the summer of 2009.

Fender joined a relatively small bankruptcy practice group in the firm's West Palm Beach branch comprised of four attorneys led by Bakst, Appellee's lead counsel.

Defendants argued that Fender "works closely with—essentially for—Mr. Bakst," and as proof pointed to cases where the two had served as co-counsel in the past. In one case, defendants noted, both Fender and Bakst represented the same trustee appearing in the present case. Making matters worse, defendants contended, was that Judge Olson would not just be adjudicating the merits of the adversary proceedings before him, he would also be deciding the amount of attorney's fees the Ruden McClosky firm may receive. Thus far, the firm sought more than $500,000 in fees "while Plaintiff's written demands before suit were $339,000." That the relationship between Judge Olson and Fender was "never disclosed by Mr. Bakst or the Court to undersigned counsel, nor to any of the Defendants in any of these related cases . . . give[s] rise to the appearance of impropriety in violation of 28 U.S.C. § 455 and the Code of Judicial Conduct."

In a more than nine-page order, Judge Olson vehemently denied the recusal motion, explaining that neither he nor his fiancé had any interest substantially affected by the outcome of the proceedings. Judge Olson emphasized that Fender had joined the Ruden McClosky firm as a salaried employee, not equity partner, and was not staffed on the present case. Thus, the relationship, the judge believed, was tenuous at best. Having reviewed the applicable case law, the judge concluded: "fiery, impassioned oral argument [by the defendants] in the face of a glass mountain of precedent, with no acknowledgment of that glass mountain, and no hint at a good faith basis for a change in the law? This is normally sanctionable under Fed. R. Bankr. P. 9011(b)."

Defendants appealed to this Court.[4] At a status conference, this Court said the following

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[4] At the relevant status hearing, this Court expressed reservation regarding its jurisdiction over the interlocutory appeal. *See In re Am. Ready Mix, Inc.*, 14 F.3d 1497, 1499 (10th Cir. 1994) (reviewing a bankruptcy appeal and holding that

regarding the appearance of impropriety in this case:

> By the same token, I would have to be candid that I'm concerned with the allegations. It's a matter of public concern because it gets in the media [and] whenever something goes to the integrity of the judicial system, it's just not good, you know, and I'm not prejudging the matter. But because of the relationship between [the bankruptcy judge] and one of the lawyers in the firm, of counsel—we can quibble about what counsel means—and then you all haven't briefed the actual substance of it, but it's uncomfortable and it's something that I agree is a matter of great interest in order for people to be more satisfied that the decision was made totally unrelated to the relationship between the judge and the lawyer.
>
> . . . .
>
> I will tell you, that's why I brought you in for status, it's uncomfortable, because no matter what it is, there's going to be a feeling that it's a tainted judgment . . . .

Following the status hearing, Judge Olson recused himself and the appeal became moot.

C. Reassignment and Post-Judgment Motions

After Judge Olson recused himself, the case was reassigned to a second bankruptcy judge. At that point, defendants filed a Supplemental and Renewed Motion to Vacate Orders and Final Judgment on November 24, 2010. Before deciding the motion, however, the second judge recused himself. Judge A. Jay Cristol was eventually assigned to the case in 2011 and held a hearing on the renewed motion to vacate. At the hearing, the judge commented, in relevant part, that "[t]his court is not an appellate court for other bankruptcy judges. The remedy for that matter is an appeal." On October 2, 2014, four years after the renewed motion to vacate was filed, Judge Cristol denied it. That same day, defendants filed a Motion for Rehearing. In a substantive order, again another four years after the motion was filed,[5] Judge Cristol denied it, writing, in relevant

"[a]n order denying a motion to recuse or disqualify a judge is interlocutory, not final, and is [therefore] not immediately appealable.").

[5] Appellee explains in his brief that the four-year delay from 2010 to 2014 in ruling on the renewed motion to vacate was due to defendants and Appellant initiating a separate state court proceeding against attorneys Bakst and Fender, which was subsequently dismissed. The four-year delay from 2014 to 2018 in ruling on the motion for rehearing, as

part, "[i]n denying the motions to vacate the Judgment, the Court previously stated it would not act as an appellate court to review the Judgment and Findings and Conclusions. The Court stated it believed the Defendants' remedies lie in an appeal . . . ."

Appellant now appeals the final judgment and relevant orders.

II. STANDARD OF REVIEW

In general, "[t]he bankruptcy court's factual findings are reviewed for clear error, and the legal conclusions . . . are reviewed *de novo*." *In re Se. Bank Corp.*, 97 F.3d 476, 478 (11th Cir. 1996) (citations omitted). This standard applies to the bankruptcy court's Factual Findings and Conclusions of Law. *See In re Optical Techs., Inc.*, 246 F.3d 1332, 1335 (11th Cir. 2001).

As for the denial of the motion for rehearing, the Court reviews the order for an abuse of discretion. *In re Kellogg*, 197 F.3d 1116, 1119 (11th Cir. 1999) ("Denials of motions . . . for rehearing are reviewed for abuse of discretion."). To the extent Appellant is also appealing the initial denial of his motion to vacate, "[m]otions under . . . rule [9024/60(b)] are directed to the sound discretion of the district court. Appellate review therefore is limited to whether the district court abused its discretion in denying the Rule 60 motion." *Griffin v. Swim-Tech Corp.*, 722 F.2d 677, 680 (11th Cir. 1984). Likewise, since the central issue on appeal concerns the first bankruptcy court's decision to not recuse, the standard of review specifically for recusal decisions is abuse of discretion. *In re Am. Ready Mix, Inc.*, 14 F.3d 1497, 1500-01 (10th Cir. 1994). "An abuse of discretion can occur where the district court [or bankruptcy court] applies the wrong law, follows the wrong procedure, bases its decision on clearly erroneous facts, or commits a clear error in judgment." *United States v. Brown*, 415 F.3d 1257, 1266 (11th Cir. 2005).

Judge Altonaga explains in her related order, was also due to the initiation of a state court proceeding "related to many of the issues presented in the pending [motion for rehearing]." It was also ultimately dismissed.

III. ANALYSIS

Appellant makes three arguments on appeal. First, he argues that the first bankruptcy judge should have recused himself as soon as his fiancé was contacted by, and negotiated with, Appellee's counsel while motions for summary judgment were pending. As a result of these actions, Appellant contends there was an appearance of impropriety pursuant to 28 U.S.C. § 455(a).[6] Appellant argues the appearance was so great that the only remedy is vacatur of the entire "tainted" proceeding. Second, Appellant argues that the Matthew Wortley Trust does, in fact, own the disputed Heinz receivable account under the plain language of the Factoring Agreement. Third, Appellant contends that he never violated the automatic stay, much less "willfully" did so, as Judge Olson found during summary judgment. Appellee, meanwhile, disagrees that there was any appearance of impropriety below, and that, even if such an appearance existed, the error was harmless. The first bankruptcy court's decision regarding ownership of the Heinz receivable, and whether there was a willful violation of the automatic stay, are correct on the merits.

Because the Court finds that the proceedings below are in fact tainted pursuant to Appellant's first argument on appeal, it need not address the latter two contentions.

A. Judge Olson Should Have Recused Himself Pursuant to 28 U.S.C. § 455(a)

Upon review, the Court holds that Judge Olson abused his discretion in failing to recuse himself as soon as his fiancé was contacted by and engaged in recruitment discussions with Appellee's counsel. By way of background, 28 U.S.C. § 455(a) mandates disqualification of a judge "in any proceeding in which his impartiality might reasonably be questioned." *Id.* This statute applies to bankruptcy judges, as well. *See* FED. R. BANKR. P. 5004 ("A bankruptcy judge

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[6] Appellant, for one reason or another, does not seek reversal under 28 U.S.C. §§ 455(b)(5)(ii) & (iii), even though he did so in his original motion to recuse. Accordingly, those arguments are waived on appeal. *See Carmichael v. Kellogg, Brown & Root Servs., Inc.*, 572 F.3d 1271, 1283 (11th Cir. 2009).

shall be governed by 28 U.S.C. § 455."). The purpose of section 455(a), as the Supreme Court of the United States explained, is to "promote confidence in the judiciary by avoiding even the appearance of impropriety whenever possible." *Liljeberg v. Health Servs. Acquisition Corp.*, 486 U.S. 847, 865 (1988). "Inherent in § 455(a)'s requirement that a judge disqualify himself if his impartiality might reasonably be questioned is the principle that our system of 'justice must satisfy the appearance of justice.'"[7] *Parker v. Connors Steel Co.*, 855 F.2d 1510, 1523 (11th Cir. 1988) (quoting *Offutt v. United States*, 348 U.S. 11, 14 (1954)). The test to determine whether a judge might reasonably be impartial is an objective one: "whether an objective, disinterested, lay observer fully informed of the facts underlying the grounds on which recusal was sought would entertain a significant doubt about the judge's impartiality." *Id.* at 1523.

Just as Judge Altonaga opined in her related appeal, the Court finds that a reasonable observer, armed with the relevant facts of this case, would reasonably question the impartiality of Judge Olson pursuant to section 455(a). A review of the objective facts makes this evident (as does a reading of Judge Altonaga's order). Appellee's counsel, the Ruden McClosky law firm, negotiated with and hired the judge's fiancé, Fender, in the summer of 2009, when motions for summary judgment were pending. Upon being hired, Fender joined a relatively small bankruptcy practice group comprised of only four attorneys led by Bakst, Appellee's lead counsel. At the time, and even for some time after, neither Judge Olson nor Bakst disclosed this material fact to Appellant. Contrary to Judge Olson's order, it does not matter that Fender was not a partner or directly involved in representing the Appellee. What matters, instead, is that he worked for Bakst, a partner, who had suddenly found himself for the first time during the course of the proceedings

[7] So important is appearing impartial and its role in promoting public confidence in the judiciary that the same statute, section 455(a), appears in the Code of Conduct for United States Judges. The code states: "A Judge Should Avoid Impropriety and the Appearance of Impropriety in All Activities." CODE OF JUDICIAL CONDUCT Canon 2 (2019).

in a prime position to affect Judge Olson's household income by way of offering a salary and other benefits, including raises, to the judge's fiancé. Other facts equally suggest that the judge did not appear impartial. Shortly after Fender joined the Ruden McClosky firm, Judge Olson ruled conclusively in Appellee's favor in his summary judgment findings and awarded attorney's fees and costs as a sanction for violating the automatic stay. That Judge Olson entered a permanent injunction in summary judgment and awarded sanctions, when just eight months before he had dissolved a temporary restraining order, augments the appearance of personal bias or prejudice.

The issue, pursuant to the plain language of the relevant statute, is whether Judge Olson's "impartiality might reasonably be questioned." 28 U.S.C. § 455(a). Upon careful review of the facts unique to this case, the Court holds that there is a reasonable basis for questioning the judge's impartiality. Consider: neither Judge Olson nor Appellee disclosed the hiring of Fender; Fender's hiring offered a "thing of value" to the judge with whom he was living and with whom he was engaged to be married; this thing of value was offered for the first time while motions for summary judgment were pending; shortly after Fender's hiring, the judge issued a permanent injunction and sanctions based on the same conduct for which he previously dissolved the temporary restraining order. These facts create the inescapable and obvious appearance of impropriety.

Furthermore, that this occurred in the bankruptcy context buttresses the notion that Judge Olson's impartiality appeared compromised. As Appellant notes, the present case comes amid a long history of concerns of favoritism in the bankruptcy bar. Congress has recognized the dangers inherit in a system in which trustees and their counsel regularly appear before the same bankruptcy court. In the debate on the Bankruptcy Reform Act of 1978, for instance, Congress noted: "There is an unusually close relationship between the bankruptcy judges and the bankruptcy bar, especially the debtors' and trustees' bars. They are in frequent contact with the judge as a result

of the necessity for the judge's review of administrative actions of the trustee or debtor . . . . All of these contacts and relationships have led to a feeling among non bankruptcy practitioners that there is a 'bankruptcy ring' that has an inside track on all bankruptcy matters, including the judges' favoritism." H.R. Rep. No. 95-595, 95th Cong. 1st Sess. 88 *reprinted in* U.S.Code Cong. & Ad. News 1978, 5787, 6056; *accord Dougherty v. Capitol Cities Commc'ns, Inc.*, 631 F. Supp. 1566, 1571-72 (E.D. Mich. 1986). Here, the judge's fiancé did not just join any law firm. Instead, he joined the law firm representing the trustee—the same law firm that Judge Olson himself had approved earlier to represent the trustee in the main underlying proceeding.

"No man is allowed to be a judge in his own cause; because his interest would certainly bias his judgment, and, not improbably, corrupt his integrity." THE FEDERALIST NO. 10, at 59 (James Madison) (J. Cooke ed. 1961). Those words, though written in a different era, are just as true today as they were then. Judge Olson became the ultimate arbiter in a case in which his "own cause" was at stake, by extension through his fiancé, when he gained the ability to affect the financial situation of his household through an award of attorney's fees to the Ruden McClosky firm. Relatedly, his own cause was at stake when his fiancé initially sought employment with that firm. "The dignity and independence of the judiciary are diminished when the judge comes before the lawyers in the case in the role of a suppliant for employment. The public cannot be confident that a case tried under such conditions will be decided in accordance with the highest traditions of the judiciary." *Pepsico, Inc. v. McMillen*, 764 F.2d 458, 461 (7th Cir. 1985). The judge, an observer would note, transformed from independent judicial officer to suppliant for employment upon the contacting and recruiting of his fiancé while litigation was ongoing.

The cases Judge Olson cites in his recusal order supporting his position of non-recusal are irrelevant because, as Judge Altonaga explained, in none of those cases was a new thing of value

added to the judge's household while litigation was pending. Short of outright payments, a job offer by a firm to a judge's spouse that affects the judge's household income—when that spouse joins a small practice, not "the catacombs of a large law firm"—may appear to be an illicit form of payment requiring recusal. Judge Olson was disqualified as soon as the firm offered a thing of value to him during the course of litigation. *See Shell Oil Co. v. United States*, 672 F.3d 1283, 1289 (Fed. Cir. 2012) (holding that because the district judge's wife owned a financial interest in certain plaintiff companies, the judge should have recused himself); *Chase Manhattan Bank v. Affiliated FM Ins. Co.*, 343 F.3d 120, 128 (2d Cir. 2003) ("Congress has . . . provided that a known financial interest in a party, no matter how small, is a disqualifying conflict of interest . . . .").

Judge Olson's initial written order is wrong for the chief reason that he failed to judge the case from the point of view of an objective observer. By doing so, he committed clear error. "The hypothetical reasonable observer is not the judge himself or a judicial colleague but a person outside the judicial system. Judges, accustomed to the process of dispassionate decision making and keenly aware of their Constitutional and ethical obligations to decide matters solely on the merits, may regard asserted conflicted to be more innocuous than an outsider would." *United States v. DeTemple*, 162 F.3d 279, 287 (4th Cir. 1998). That, unfortunately, is what occurred here.

B. Under the *Liljeberg* Factors, the Court Vacates Final Judgment

Having found that Judge Olson should have recused himself pursuant to section 455(a), the Court must decide the appropriate remedy. The Supreme Court has set forth three factors to consider in determining whether a judgment should be vacated for a violation of section 455(a): "[1] the risk of injustice to the parties in the particular case, [2] the risk that the denial of relief will produce injustice in other cases, and [3] the risk of undermining the public's confidence in the judicial process." *Liljeberg*, 486 U.S. at 864. Regarding the first factor, the Eleventh Circuit has

added that "[f]irst, the reviewing court should consider whether the party seeking vacatur has pointed to particular circumstances that may indicate a risk of injustice to that party. Second, the court should consider the seriousness of the violation of section 455(a) that is involved." *United States v. Cerceda*, 172 F.3d 806, 813 (11th Cir. 1999) (footnotes omitted).

i. The Risk of Injustice to the Parties

The Court concludes that a review of all three factors mandates vacatur of the final judgment and orders on appeal. Appellant has carried his burden of showing a substantial risk of injustice. That Judge Olson suddenly found a violation of the automatic stay, and that it was willful—when no new evidence of a breach was presented, and when Appellee's counsel had conceded that he was not seeking a determination at that time on that exact issue—gives the Court pause. Only eight months before, Judge Olson dissolved the temporary restraining order (which was based on the same November 12 demand letter) after review of the numerous written and verbal affirmations by Appellant promising to not violate the stay. In fact, Judge Olson was left asking Appellee, "so what are we fighting about for purposes of today? . . . With the concession that the litigation over the receivables and, indeed, perhaps collection efforts themselves, will be conducted here, and that the defendants in your litigation will take no action against Heinz except with leave of this Court . . . what do you need an injunction for?" An objective observer armed with the facts above would reason that the only discernable difference between the order dissolving the temporary restraining order and the order suddenly granting the injunction and sanctions is the fact that the Ruden McClosky firm had hired the judge's fiancé in the interim.

The error was not harmless. *See Parker*, 855 F.2d at 1526 (applying the harmless error standard to vacatur judgments). In fact, the seriousness of the error and violation of section 455(a) was so great that the Court's only available remedy is to deprive the Appellee of his judgment.

Judge Olson's order led to Appellant facing a nearly $80,000 fee award as a sanction for a "continuing" violation that arguably never even was a violation in the first place, much less continuing. As Appellant notes, the November 12 demand letter was ambiguous regarding whether Appellant would seek the Heinz receivable outside the relevant bankruptcy proceedings. Further, the violation was not continuous—the sanctions were based on the same November 12 demand letter that resulted in the imposition of the temporary restraining order in the first place.

The Court is not alone in finding that the appearance of impropriety and the seriousness of the violation of section 455(a) mandate near-total vacatur of the trial proceedings. Judge Altonaga found similarly in her related appeal. Just as in that case, although "it is burdensome to appellee[] for [the Court] to require a new trial . . . it is not unfair." *Chase Manhattan Bank*, 343 F.3d at 132. The Court recognizes that the adversary proceeding below has unfortunately spanned more than ten years and numerous appeals. The record is extensive and the federal judiciary has devoted considerable time and resources to this case. But Congress has directed federal judges by law to recuse themselves in certain situations, like this one, and the Court must accept that guidance. "[F]ederal judges must early and often consider potential conflicts that may arise in a case and, in close cases, must err on the side of recusal. And if a judge must step aside, it is better to do it sooner instead of later." *Murray v. Scott*, 253 F.3d 1308, 1313 (11th Cir. 2001) (footnote omitted).

The Court agrees with Judge Altonaga that the most conservative course of action is to revert the proceedings back to the summary judgment phase, before any new bankruptcy court may make a finding regarding the alleged violation of the automatic stay. In this way, Appellant and Appellee need not return all the way to the starting blocks when resuming litigation.

ii. The Risk that the Denial of Relief Will Produce Injustice in Other Cases

The second factor the Court must analyze is whether the risk of denial of relief will produce

injustice in other cases. "This factor weighs in favor of vacating the judgment when so doing would 'encourag[e] a judge or litigant to more carefully examine possible grounds for disqualification and to promptly disclose them when discovered.'" *Cerceda*, 172 F.3d at 815 (alteration in original) (quoting *Liljeberg*, 486 U.S. at 868). The Court seeks in this Order to achieve that aim particularly where, as here, the proceedings below are centered around the bankruptcy context where the risk of favoritism may be high.

iii. The Risk of Undermining the Public's Confidence in the Judicial Process

The final factor requires an analysis of the risk undermining the public's confidence in the judicial process. For all the reasons set forth above, a failure to vacate the proceedings below will likely jeopardize the public's trust and confidence in the judiciary.

IV. CONCLUSION

"An independent, fair and impartial judiciary is indispensable to our system of justice." MODEL CODE OF JUDICIAL CONDUCT Preamble (2011). So is avoiding the appearance of impartiality. The bankruptcy judge's personal and financial entanglement with the Ruden McClosky firm, through his fiancé, appeared to "compromise[] what Edmund Burke justly regarded as the 'cold neutrality of an impartial judge.'" *United States v. Microsoft Corp.*, 253 F.3d 34, 115 (D.C. Cir. 2001). Public trust and confidence in the judiciary depend upon the appearance of integrity and independence of judges, which must be carefully safeguarded. Only reversal and remand in this case will restore that appearance. Accordingly, it is

ADJUDGED that

(1). The bankruptcy court's (a) Findings of Fact and Conclusions of Law, (b) Final Judgment in Favor of Plaintiff, and (c) Order Denying Motions for Rehearing, Motions to Alter or Amend Final Judgment and Findings of Fact and Conclusions of Law, Motions to Disqualify and for Leave to Take Discovery are **SET ASIDE**.

(2) The case is **REMANDED** to the summary judgment phase for further proceedings consistent with this Order.

DONE AND ORDERED in Chambers at Miami, Florida, this 9th of September 2019.

FEDERICO A. MORENO
UNITED STATES DISTRICT JUDGE

Copies furnished to:

Counsel of Record

1 IN THE UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF VIRGINIA (RICHMOND)

2

In Re:	)	Case No. 19-30258-KLP
	)	Richmond, Virginia
GYMBOREE GROUP, INC., et al.,	)	
	)	
Debtors.	)	February 15, 2019
	)	10:06 a.m.
-------------------------------	)	
KATHERINE POCRASS, et al.,	)	Adv. Proc. 19-03010 (KLP)
	)	
Plaintiffs,	)	
v.	)	
	)	
GYMBOREE GROUP, INC., et al.,	)	
	)	
Defendants.	)	
-------------------------------	)	

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11 TRANSCRIPT OF HEARING ON
DEBTORS' APPLICATION FOR ENTRY OF AN ORDER AUTHORIZING THE
12 DEBTORS TO EMPLOY AND RETAIN KUTAK ROCK LLP AS CO-COUNSEL
EFFECTIVE NUNC PRO TUNC TO THE PETITION DATE [DOCKET NO. 162];
13 DEBTORS' MOTION TO RETAIN BERKELEY RESEARCH GROUP, LLC TO
PROVIDE THE DEBTORS WITH A CHIEF RESTRUCTURING OFFICER AND
14 CERTAIN ADDITIONAL PERSONNEL NUNC PRO TUNC TO THE PETITION DATE
[DOCKET NO. 175];
15 DEBTORS' MOTION FOR ENTRY OF AN ORDER AUTHORIZING THE DEBTORS
TO RETAIN AND COMPENSATE PROFESSIONALS UTILIZED IN THE ORDINARY
16 COURSE OF BUSINESS [DOCKET NO. 179];
DEBTORS' MOTION FOR ENTRY OF AN ORDER AUTHORIZING EXPEDITED
17 PROCEDURES FOR REJECTING UNEXPIRED LEASES AND ABANDONMENT OF
PERSONAL PROPERTY [DOCKET NO. 108];
18 DEBTORS' MOTION FOR ENTRY OF AN ORDER (I) SETTING BAR DATES FOR
FILING PROOFS OF CLAIM, INCLUDING REQUESTS FOR PAYMENT UNDER
19 SECTION 503(B)(9), (II) ESTABLISHING AMENDED-SCHEDULES BAR DATE
AND REJECTION-DAMAGES BAR DATE, (III) APPROVING THE FORM OF AND
20 MANNER FOR FILING PROOFS OF CLAIM, INCLUDING SECTION 503(B)(9)
REQUESTS, (IV) APPROVING NOTICE OF BAR DATES, AND (V) GRANTING
21 RELATED RELIEF [DOCKET NO. 180];
DEBTORS' MOTION FOR ENTRY OF INTERIM AND FINAL ORDERS
22 (I) AUTHORIZING THE DEBTORS TO (A) PAY PRE-PETITION WAGES,
SALARIES, OTHER COMPENSATION, AND REIMBURSABLE EXPENSES AND
23 (B) CONTINUE EMPLOYEE-BENEFITS PROGRAMS, AND (II) GRANTING
RELATED RELIEF [DOCKET NO. 22];
24 DEBTORS' MOTION FOR ENTRY OF INTERIM AND FINAL ORDERS
(I) AUTHORIZING THE PAYMENT OF CERTAIN TAXES AND FEES AND
25 (II) GRANTING RELATED RELIEF [DOCKET NO. 8];

1 MR. FLECK: We do. We've worked with all of them in
2 other cases and are pleased, notwithstanding the fact that
3 they're really taking us to task on every single matter, and
4 that's what they're supposed to do. We've had a tremendous
5 amount of interaction with them, and I'm pleased to report that
6 we've made progress such that most of the matters on today's
7 agenda are consensual. And there're a couple things --
8 THE COURT: Very good.
9 MR. FLECK: -- we need to do on the record as it
10 pertains to their objections, but we've made a lot of progress.
11 There're changes to the orders; we're comfortable with them; we
12 think they advance transparency and disclosure and all the,
13 kind of, key principles of bankruptcy. So we're pleased to
14 have made that progress and we appreciate Mr. Van Arsdale,
15 who's here on behalf of that office.
16 Again we have our -- certain members of our management
17 team; I'd just like to recognize them. Our CFO, Mr. Kimmins,
18 is in the courtroom, in the first row; our general counsel, Ms.
19 Holtz MacMillan. We also have Mr. Coulombe of BRG, our CRO;
20 and also Mr. Doak, who's a couple of rows back, our investment
21 banker, as well. And Your Honor probably recalls them from the
22 first-day hearing. They were also in town because we had some
23 interaction yesterday with our creditors at the 341 meeting, as
24 well as our initial interview with the Office of the United
25 States Trustee.

1 Your Honor, the second words of apprec -- second set
2 of words of appreciation, outside of the Court, Your Honor, and
3 then the Office of the United States Trustee, is for a new
4 constituency in the case. We're very happy to have the
5 official committee of unsecured creditors. They were appointed
6 on January 23rd. They have wasted no time getting up to speed,
7 not just up to speed but getting fully engaged in the case.
8 They've retained highly qualified counsel, the Pachulski firm,
9 as well as Province, and Whiteford Taylor. We're pleased to be
10 working with those professionals again.
11 I would like to be a little bit more specific in terms
12 of their engagement, Your Honor. And it's pretty remarkable;
13 within hours, literally, of those professionals being engaged,
14 we started engaging in emails and kind of dispensed with some
15 of the formalities and just got right to work with them on
16 talking about the key issues in the case and how to hopefully
17 preserve value for the stakeholders and their constituency.
18 In addition, at their request we had an in-person
19 meeting on February 4th at our offices in New York.
20 Management-team members joined from San Francisco via
21 videoconference. The members of the committee were present in
22 person and certain of them on the phone. And we spent hours
23 together going over key drivers in the case, risks, and
24 opportunities. And we look forward to continued collaboration
25 with those professionals and with the members of the committee.

1 the declaration. I've reviewed the program. I think that the
2 proposed revisions are beneficial, and with those revisions it
3 certainly appears to me that the requirements of Section 503(c)
4 are met. And I believe that the programs should be approved.
5 So I will grant the motion.
6 MR. FLECK: Thank you, Your Honor. We're now, in
7 terms of the agenda, on the last item. I think this is the
8 reason why everyone came to court today, item number 163 on the
9 docket. This is the application of the debtors to retain
10 Milbank, Tweed, Hadley & McCloy as counsel for the debtors.
11 May I proceed, Your Honor?
12 THE COURT: You may.
13 MR. FLECK: Thank you, Your Honor. In some ways my
14 comment was in jest, but this application, as you might
15 imagine, is quite serious as it pertains to our firm. We take
16 conflicts matters and retention matters appropriately seriously
17 and go to great pains with our internal procedures to be sure
18 that, in connection with matters particularly in a bankruptcy
19 court, that we've run all the traps multiple times, and we're
20 quite comfortable that the application here is no different.
21 In fact, the application that was filed on January
22 30th of the debtors to retain our firm is quite routine. And
23 although our firm hasn't been subject to an objection such as
24 this one before, we're happy to justify the basis for the
25 debtors' retention of our firm and believe that there are no

1 conflicts that would preclude our retention here.
2 Your Honor, as kind of evidence to the fact that this
3 is sort of unusual, we did -- in that there was the objection
4 that was filed, we did submit several affidavits or
5 declarations, rather, in support of the application. And at
6 this point I'd request the Court to move those into evidence.
7 These are my declaration, the first one that's at docket 163;
8 it comes with the original application. My second declaration,
9 which is at docket number 272, and then a declaration of Mr.
10 Coulombe, the CRO, that's at docket number 306.
11 Your Honor, the application, on its face, is quite
12 similar to applications that have been before this Court, and
13 indeed pretty much every bankruptcy court where a Chapter 11
14 case has been heard. We recite in the application our
15 qualifications for service, our billing rates, our policies
16 with respect to retainers, which is an advance-payment
17 retainer, Your Honor, under New York law, and then attach as
18 exhibits the various conflicts and connections that we're
19 disclosing because, indeed, in Chapter 11, we are required to
20 make disclosures to enhance transparency.
21 We are here today, though, Your Honor, on the
22 objection of John Fitzgerald, the acting United States Trustee
23 for Region 4, to our retention application, on the basis that
24 Milbank is not disinterested in respect of this matter.
25 Your Honor, the objection spends many pages talking

1 about an issue that we think we've actually satisfied and
2 probably doesn't even need to get into the case law. And it
3 comes up right in a preliminary statement. They say:
4 "Allowing Milbank to represent the debtors undermines the aura
5 of transparency and integrity that every bankruptcy case must
6 have."
7 Your Honor, this process, in fact, that we've gone
8 through, our application and then the supplemental
9 declarations, the Coulombe declaration, the objection of the
10 United States Trustee, all go to the transparency that the
11 United States Trustee is, at least on paper, seeking to protect
12 and preserve by virtue of their application.
13 We have gone into painstaking detail with respect to
14 our relationship with everybody in the case, everybody, small
15 and large, but yet the issue that seems to be causing the
16 Office of the United States Trustee, which we think is a
17 somewhat extraordinary position for them, even in the context
18 of other objections they filed, is the fact that Goldman Sachs
19 and Bank of America are existing clients of our firm in wholly
20 unrelated matters.
21 There is no allegation being made by the Office of the
22 United States Trustee that we've had any relationship to those
23 institutions in connection with these cases. Our position that
24 we can seek to and actually represent the debtors is wholly
25 unremarkable. Pretty much every other -- any other law firm,

1 including ours, has relationships with other parties in the
2 case. Indeed, any large law firm, including ours, that has
3 offices around the world and has relationships and connections
4 in various practice areas, it would stand to reason that we
5 would have relationships with parties who would come to finance
6 debtors on a pre-petition basis or on a post-petition basis.
7 So what does the United States Trustee cite as a basis
8 for why our firm -- notwithstanding the fact that they make
9 note of our excellent work in the cases to date -- our firm is
10 disinterested from this representation?
11 Their argument starts and ends with Section 327(a) of
12 the Bankruptcy Code. Everyone's familiar with that section.
13 But as the Eastern District of Virginia, in the Johnson case,
14 has said, that that's not really where the inquiry starts and
15 ends. There's another section of the Bankruptcy Code, rather a
16 subsection of 327, which is 327(c), which actually goes to the
17 very issue of whether or not a counsel is interested or
18 disinterested, in connection with relationships where that
19 counsel does represent other parties in the case.
20 And in fact, the United States Trustee's office cites
21 to many cases where courts actually have allowed counsel to
22 represent creditors and other interested parties when they are
23 also representing the debtors in those cases on related
24 matters. That's not what we have before the Court, Your Honor,
25 at all.

1 What the U.S. Trustee's office sort of takes us
2 through is sort of a tour of case law outside of the Fourth
3 Circuit to try to suggest that other courts have found factual
4 circumstances similar to this to be grounds for
5 disqualification. And, Your Honor, we would respectfully
6 submit that none of those cases are either on point or stand
7 for those propositions.
8 We'll start with Project Orange, Your Honor, which is
9 from my home jurisdiction in the Southern District of New York,
10 Judge Glenn's fairly well-known case. That's not on point,
11 Your Honor. In that case, DLA Piper, the law firm, represented
12 a GE entity. GE was in active litigation against the debtors'
13 estates. Judge Glenn took note in his decision that the law
14 firm was not appropriately transparent and didn't have
15 appropriate candor with the court with respect to its
16 relationships. And ultimately, the court took specific note of
17 the fact that, in DLA Piper's case, and in fact, specifically
18 in the case of GE, Your Honor, the litigation that was being
19 pursued by GE against the debtors' estates was so pervasive
20 that having DLA Piper also represent the debtors' estates was
21 problematic.
22 And again, in reading the decision, it's quite clear
23 that Judge Glenn was particularly concerned with the lack of
24 disclosure with respect to those relationships. There can be
25 no doubt, Your Honor, that we have been open and transparent

1 with respect to our relationship with certain parties-in-
2 interest, including Bank of America and Goldman Sachs, all of
3 which are in matters unrelated to these cases.
4 Next, Your Honor, instead of coming to cases within
5 the Fourth Circuit, the United States Trustee elects to take us
6 into Iowa, in the case of Premier Farms where the Court
7 determined that 327(c) doesn't actually mean what courts in
8 this circuit have said it means.
9 In Premier Farms the court said that you had to
10 satisfy 327(a) and also 327(c). 327(c) was not what this Court
11 has said it actually means. And I'll get into that in a few
12 more minutes. Premier Farms is also distinguishable from the
13 facts here, Your Honor because the court perceived there to be
14 an actual conflict, based upon the facts and circumstances of
15 the case, where the parties that the law firm had represented
16 in that case were -- in that case it was the Sonnenschein
17 firm -- were actively engaged in litigation or there were
18 disputed matters that were obviously going to come up. So
19 there were actual conflicts that were before the court at the
20 time of the retention of the cases, and the court found that to
21 be untenable. Hardly a remarkable conclusion by the court from
22 Iowa in these cases.
23 I think at this point it's appropriate to move to a
24 discussion around what we think the law actually is, and we
25 think the law is set out pretty clearly by In re: Johnson,

1 Your Honor. That's 312 B.R. 810. That's from this district,
2 the Eastern District of Virginia, a 2004 decision where the
3 court affirmed the bankruptcy court decision in that matter,
4 where the court went on, and really, I think, starts and ends
5 the inquiry here, for relevant purposes.
6 The court said that Section 327 is an exception to the
7 general rule. It provides a much less -- this is not a quote,
8 Your Honor; this is a summary of the decision -- and provides a
9 much less stringent standard for determining the qualifications
10 of counsel challenged solely on the grounds that it represents
11 a debtors' creditors.
12 As the district court for the Eastern District of
13 Virginia explained, where the debtors request to employ counsel
14 is challenged on the grounds that such counsel also represents
15 the debtors' creditors, the -- and this is a quote, Your
16 Honor -- "the stringent two-pronged test in 327(a) does not
17 apply". So according to decisions that are persuasive, Your
18 Honor, as it pertains to this Court, we should be looking to
19 Section 327(a).
20 Johnson goes on to explain; I quote: "Section 327(c)
21 was intended to broaden the debtors' choices to include
22 competent and experienced bankruptcy attorneys provided there
23 was no actual conflict. Horrible imaginings alone cannot be
24 allowed to carry the day."
25 There aren't even horrible imaginings here, Your

1 Honor. The United States Trustee does not actually even
2 attempt to present the case that there's an actual conflict.
3 Their position, as we understand it, is that the fact that we
4 represent Goldman Sachs and Bank of America in unrelated
5 matters is an actual conflict on its face.
6 If that were the law, Your Honor, no law firm -- well,
7 a wide swath of law firms would be ineligible to represent
8 debtors. And we don't think that was the case at all. In
9 fact, as the legislative history for 327(c) suggests -- and
10 this is a quote: "It was becoming increasingly difficult, in
11 large bankruptcy actions, for trustees to find and employ the
12 services of a competent and experienced bankruptcy attorney who
13 was not also representing a creditor."
14 And again, Your Honor, Johnson contemplates a scenario
15 where the law firm representing the debtor also represented the
16 creditor in connection with those cases. That's exactly what
17 happened in Johnson, and the court -- this court, as well as
18 the district court, approved it and said it was appropriate.
19 The Richter Miller & Finn firm, from Washington, D.C.
20 had represented a creditor in connection with the Johnson case,
21 pursuing claims, actual litigation claims against Johnson. And
22 then, subsequently, the trustee sought to retain that law firm
23 to represent the estate as debtors' counsel. The court
24 approved that retention on the same basis that there was no
25 actual conflict of interest. There was no basis, as such, to

1 disqualify the law firm.
2 Your Honor, there are many other cases, and we cite
3 them on page 5 of our reply, where there are actually law
4 firms -- the same law firm representing the debtor is
5 representing the creditors in the same action. That's not what
6 we proposed here. I'm not going to weigh in on whether that's
7 something that we would even consider, but we don't even need
8 to get there, Your Honor, because we don't think it's relevant.
9 I want to move now to talk about whether or not --
10 even if you thought that we were, sort of, within the penumbra
11 of cases that we have to consider around conflict, is there any
12 conflict that the Court should be concerned with that needs to
13 be considered as it relates to Goldman Sachs, Bank of America
14 and Milbank Tweed?
15 I think it's here, Your Honor, where the facts sort of
16 make the question a lot easier. And this is a different case
17 than those that were discussed even in the cases in the outer
18 jurisdictions that the United States Trustee elected to cite.
19 What we have here are secured lenders who came out of
20 the prior cases. Why is that relevant, Your Honor? Because in
21 connection with the prior cases, Your Honor entered an order on
22 September 7th of 2017, and in that order -- it's a lengthy
23 order; we had active participation by the counsel to the DIP
24 lenders in that case. In that order it goes -- this is just
25 the order. The order goes on and on and talks about the liens

1 that were granted in connection with that case on the exit
2 facility loans. Those lenders, in connection with those
3 cases -- where, by the way, Kirkland & Ellis represented the
4 debtors; we did not.
5 Your order, Your Honor, goes on, in appropriate
6 detail, around issues that pertain to the liens and perfection
7 of those liens. This is not the kind of case where, when
8 you're looking at the liens and a potential lien challenge of
9 the current secured lenders, you need to go back in time and
10 start to do your lien searches in the local county offices.
11 Your Honor entered an order that provides, in
12 paragraph 99, among other things, that all of the liens and
13 security interests to be granted in accordance with the exit
14 facility documents -- and I move on to subsection (c) -- "shall
15 be deemed perfected on the effective date subject only to the
16 liens and security interests as may be permitted under the exit
17 facility documents."
18 And it goes on: "shall not be subject to
19 recharacterization or equitable subordination for any purposes
20 whatsoever, shall not be otherwise subject to avoidance".
21 There are pages that continue in the same vein, Your Honor.
22 That's Bank of America and Goldman Sachs.
23 Why do I raise this? Because one of the key issues
24 that one might consider as to whether we would have a conflict
25 is whether or not we would expect the debtors to be in a

1 position of conflict with Bank of America and Goldman Sachs.
2 Well, the answer is resoundingly no. And in large part it's
3 because there is no challenge that the debtors could reasonably
4 expect to have with respect to the liens and security interests
5 on account of those pre-petition interests.
6 Now, Bank of America is differently situated than
7 Goldman Sachs at this point, and the Coulombe declaration helps
8 to alleviate any confusion on the part of the United States
9 Trustee as to what role Bank of America is playing at this
10 point.
11 Your Honor will recall that, in connection with the
12 payments that were made to the estate by the liquidators,
13 effectively, Bank of America's collateral was being purchased.
14 They had a first lien on that inventory. It was purchased by
15 the liquidator. So it stands to reason -- and in fact in every
16 case that we're aware of, and Mr. Coulombe's declaration speaks
17 to this -- where this scenario happens, that payment comes in
18 and it goes to the secured party on that inventory that they
19 purchased.
20 So the suggestion in the U.S. Trustee's papers that
21 somehow the basis for paying Bank of America for their
22 collateral out of the agency proceeds was maybe because Milbank
23 represents Bank of America on unrelated matters, that couldn't
24 be further from the truth. It's a dangerous suggestion.
25 And we think and are hopeful that a combination of the

1 declaration, which helps to clarify the facts, and the relevant
2 law on the point, alleviates that concern. That's not even a
3 perception of a conflict and certainly not an actual conflict.
4 We don't expect that Bank of America would have an
5 active role in connection with these cases, save for the fact
6 that there is some residual interest in connection with the
7 liens and certain of their -- well, this is all dealt with in
8 the order. But they will have a continuing role in connection
9 with the cases. They'll have a role. In connection with a
10 challenge, that would be pursued by our friends at the
11 creditors' committee, if there is one. And I think, as was
12 addressed earlier in these proceedings, that period of time has
13 been extended, the budget has been made more robust. But
14 that's not a debtor adversity vis-a-vis Bank of America, and
15 therefore it stands to reason that, as counsel to the debtors,
16 there's no concern with respect to adversity on that issue.
17 Goldman Sachs might be more complicated, but it really
18 leads to the same result. We've addressed the fact, I hope,
19 Your Honor, with respect to Goldman Sachs' liens, because we
20 were dealing with a pre-petition -- the pre-petition liens that
21 were addressed in connection with Your Honor's order, which is
22 clearly a final order. There are liens, obviously, that arise
23 in connection with the debtor-in-possession financing, the
24 original one, and what was amended and approved by Your Honor
25 today.

1 And so in connection with their financing role, we
2 don't anticipate any conflict. And this is exactly the type of
3 analysis that the courts -- even the courts where they didn't
4 look to 327(c) but looked to 327(a), engaged in to see, well,
5 we can't just say that, on the basis of a perception, that
6 there's a problem; we have to look at the facts and
7 circumstances of the case.
8 So in the case of Goldman Sachs, I think we've
9 addressed their role as DIP lender and pre-petition lender.
10 And Mr. Coulombe's declaration also speaks to their role as a
11 stalking-horse party. I think the record should be clear and
12 is replete with examples, and we cite them at paragraph 19 of
13 our reply, and also in Mr. Coulombe's declaration, of the role
14 that SSIG is playing in these cases as stalking-horse bidders.
15 They're not receiving bid protections. They were there to set
16 a floor, to start a process, to hopefully encourage a robust
17 bidding which, as we've alluded to during the course of these
18 hearings, we're engaged in quite actively.
19 A couple more points, Your Honor, one is that we do
20 have co-counsel in these cases. Kutak Rock is our co-counsel
21 and is qualified. To the extent that there ever were an actual
22 conflict which, as Your Honor has heard, our view is that no
23 such conflict is reasonably foreseeable in these cases, they
24 would be available. We know that there are other law firms
25 locally that have expressed an interest and are conflict free,

1 and we appreciate them reaching out in response to the U.S.
2 Trustee's objection. The creditors' committee could perform a
3 role, if that were necessary. And so I think that's not really
4 a question, to the extent -- and Your Honor is obviously very
5 much engaged in these cases should such a conflict rear its
6 head.
7 Secondly, Your Honor, is the disruption. Unlike some
8 of the cases that were cited, including the case from Colorado
9 that the U.S. Trustee brought to our attention, where debtors'
10 counsel was retained for the purpose of these cases, we've been
11 working with the debtors since the prior cases.
12 Your Honor's aware that there has been a significant
13 attrition at the debtors, and we do provide certain continuity
14 with respect to the affairs of the debtors. As we lose more
15 employees of the debtors, it's helpful to have our colleagues,
16 who have been working in different practice areas, tax and
17 employee benefits, and other matters, to be facilitated in the
18 process and continuity of these cases.
19 And courts have found that to be relevant. The
20 Johnson court noted that specifically, and other courts that
21 have been cited, even by the U.S. Trustee, have recognized
22 that, even in the face of a conflict, the Court and the parties
23 should take into account the facts and circumstances of the
24 case, and if the disruption that could be caused by replacing
25 counsel would not be efficient to the cases, that needs to be

1 taken into account.

2 The Fourth Circuit in Harold & Williams Development

3 Co., 977 F.2d 906, Fourth Circuit 1992, specifically notes that

4 a court should consider these issues in a way that best serves

5 the objectives of the bankruptcy system. It would not serve

6 the efficient, expeditious, and economical resolution of the

7 bankruptcy proceedings to replace counsel premised on vague

8 allegations of conflict.

9 Your Honor, I believe, at this point, that concludes

10 my affirmative remarks with respect to our application. I

11 would appreciate the opportunity to respond -- have time to

12 respond to Mr. Van Arsdale, to the extent he has argument in

13 support of his own objection.

14 THE COURT: All right. You had asked, I think, to

15 have your declarations of Mr. Coulombe's declaration admitted?

16 MR. FLECK: Yes, Your Honor. Mr. Coulombe, as well as

17 my own declarations.

18 THE COURT: Well, yours at docket number 163 and 272,

19 Mr. Coulombe number 306. Any objection to the admission of

20 those declarations?

21 MR. VAN ARSDALE: No, Your Honor.

22 THE COURT: All right. They're admitted.

23 (Declaration of Mr. Coulombe, docket number 306, was hereby

24 received into evidence as of this date)

25 (Declarations of Mr. Fleck, docket numbers 163 and 272,

1 were hereby received into evidence as of this date)
2 MR. FLECK: Thank you, Your Honor.
3 MR. VAN ARSDALE: Robert Van Arsdale for the U.S.
4 Trustee.
5 Your Honor, the U.S. Trustee objects to the retention
6 application of Milbank as main bankruptcy counsel because the
7 U.S. Trustee is concerned that Milbank represents a significant
8 adverse interest and has an actual conflict in these cases.
9 I would like to start off by saying that the objection
10 was filed in no way as a criticism of Milbank's work or
11 reputation. The U.S. Trustee does not question Milbank's
12 qualifications or skills to be employed as debtors' counsel in
13 these cases, and we think highly of them and the attorneys who
14 are here today.
15 I will also say when Mr. Fleck read a section of our
16 motion that indicated that we were concerned about disclosures,
17 I don't think that's true. And to the extent that's in our
18 papers, I apologize for that. In fact, the facts on which we
19 based the objection were from reading Mr. Fleck's disclosures
20 that he did make. And that's when the -- you know, it's not a
21 question of not being disclosures; there were disclosures.
22 Your Honor, I have several pages of things that I
23 could say, but I think I'm just going to cut to the chase here
24 because much of what Mr. Fleck said struck home. But I do want
25 to talk briefly about what constitutes an actual conflict

1 because those words sound easy, they sound simple, but it's not
2 defined in the Bankruptcy Code at all what an actual conflict
3 is.
4 The cases seem to indicate that it's on a case-by-case
5 basis and that each one has to be evaluated before it can be
6 concluded whether it is or not an actual conflict. And as the
7 Court said in BH&P, Inc.: "It is nonetheless sensible to
8 conclude that an alleged conflict of interest is actual and
9 warrants disqualification under Section 327(c) if there is
10 active competition between two interests in which one interest
11 can only be served at the expense of the other."
12 And I think that quote, as much as anything, and the
13 prior and continuing relationships between Milbank and Bank of
14 America, and Milbank and Goldman Sachs, those were the essence
15 of our concerns. And one of them, I think, in the last two
16 years, amounted to four percent of the total revenues of the
17 Milbank firm. I think the other one may be a little over one
18 percent.
19 But the conclusion was reached that, when trying to
20 make decisions concerning this case, that the law firm wouldn't
21 be able to pursue anything that would be adverse to either Bank
22 of America or Goldman Sachs. And they have already had them as
23 clients, they will continue to have them as clients, and that's
24 what the basic concern was.
25 Having been here today and having gotten to know Mr.

1 Fleck somewhat in the course of these proceedings, I'm glad
2 to --
3 THE COURT: You're not --
4 MR. VAN ARSDALE: I'm glad to be here.
5 THE COURT: -- jumping up and down and screaming;
6 you're just --
7 MR. VAN ARSDALE: I'm glad to be here.
8 THE COURT: Okay.
9 MR. VAN ARSDALE: Unless the Court wants something
10 more, I think that is the basis of our objection, and I take to
11 heart what Mr. Fleck said.
12 THE COURT: All right. Thank you, Mr. Van Arsdale.
13 Does anyone else wish to be heard in connection with
14 the Milbank retention application?
15 All right. Well, thank you for your comments. I
16 understand your position and the job you have to do to make
17 sure that the bankruptcy system is -- that the integrity of the
18 system is kept intact and that everyone's aware of what's going
19 on in the case.
20 I think in this case, as you indicated, there's no
21 problem with the disclosures that have been made by Milbank.
22 You referenced that Goldman may -- potentially would object if
23 there was a adverse situation. So I'm taking it at this point
24 that there is no adverse situation.
25 It does appear -- I think it was represented in the

1 pleadings -- that Goldman and the debtors are currently working
2 together to achieve the same objective insofar as the
3 successful outcome of this case is concerned.
4 I do think that the employment of Milbank, pursuant to
5 section 327(a), is appropriate. It's consistent with the
6 requirements of this district as set forth in In re: Johnson.
7 I would also observe that Milbank has conducted
8 itself, to date, in this case as I would expect it to do in
9 representing its client, the debtors, zealously, and in their
10 best interests.
11 I also am influenced, to some extent, by the same
12 factor that was raised with respect to Ernst & Young, and that
13 is that were there to be an elimination of Milbank in this
14 case, that would be significantly disruptive and burdensome to
15 the debtors and their estates.
16 That being said, and as Mr. Fleck has indicated,
17 should an actual conflict exist, and by that I mean one where
18 that it would be apparent that Milbank would not be able to
19 represent the debtor, then certainly we have the committee
20 present. But there's other alternatives, local counsel, and
21 potentially conflict counsel that would be available. And I
22 certainly expect that that will be brought to my attention
23 should that type of situation develop.
24 But for today's purposes, I am going to approve the
25 application.

1 MR. FLECK: Thank you very much, Your Honor. We
2 appreciate your time and we appreciate Mr. Van Arsdale's
3 comments, and we look forward to continuing to work with the
4 parties.
5 I think that brings us to the end of the agenda for
6 today.
7 Oh, I'm sorry. Too soon. Okay. I'll cede --
8 THE COURT: I think there's also the --
9 MR. FLECK: I see there's no objection.
10 THE COURT: Well, there was --
11 MR. FLECK: I'll cede the podium.
12 THE COURT: There was a Pan Pacific motion on the
13 agenda. And I know we heard from -- I think we heard from Pan
14 Pacific earlier, but --
15 MR. DONALDSON: Your Honor, Jed Donaldson on behalf of
16 Pan Pacific. And this, I guess, is the true main event that
17 everyone's been waiting for.
18 THE COURT: Okay. All right.
19 MR. DONALDSON: And --
20 THE COURT: Well, I wouldn't have left you out. I've
21 seen you sitting in the back of the courtroom patiently
22 waiting.
23 MR. DONALDSON: And I won't keep anyone in further
24 suspense. This is Pan Pacific's motion for adequate protection
25 and then related relief. We have an agreed order with the

***Robbins v. Dalafield (In re Williams)*, 2018 WL 832894 (Bankr. W.D. Va. Feb. 2, 2018).**

This case involved a "new car custody program" offered by Upright, a multi-jurisdictional, legal-services provider. Debtors who wished to surrender their vehicles would release them to a national towing company in exchange for its paying the debtor's bankruptcy fees and costs. The towing company would then place the cars in storage lots in other states that permit bailee fees that prime secured claims. The court levied over $250,000 in sanctions, including separate sanctions on its principles, and revoked Upright's ability to practice in the district for five years. It barred the two local attorneys for twelve and eighteen months, respectively. As stated in the opinion, the case represents a "collision between traditional methods of providing—and policing—legal services to consumers for bankruptcy matters and attempts by attorneys and creative online marketers to tap into that market on a high-volume, multi-jurisdictional basis." *Id*. at *1.

***In re Banks*, 2018 WL 735351 (Bankr. W.D. La. Feb 2, 2018).**

This case also resulted in sanctions against Upright and its local attorney, as well as their suspensions of practice. The opinion records a litany of negligence: counsel unnecessarily caused its client to file two bankruptcies; counsel failed to defend a judgment entered against the client; basic documents were never filed despite the client having timely produced them to counsel; both Upright and local counsel failed to correct mistakes and failed to communicate with the client. The court specifically found violations of state Rules of Professional Conduct by local counsel.

***In Wright et al.*, 591 B.R. 68 (N.D. Okla. 2017).**

The court consolidated its review of seventeen cases filed by the same counsel using the service of BK Billing LLC, "a finance company that provides factoring services to bankruptcy counsel in Chapter 7 cases." *Id*. at 72. The court held that counsel knew or should have known that BK Billing would begin collection activity prior to the debtor's court fees being paid in full. As such, the payment violated his clients' duties under Rule 1006. Additionally, counsel violated his own duty of candor under Rule 9011(b)(3) and section 526(a)(2) when he executed BK Billing's factoring agreement. He compounded his violation of section 526(a)(2) by advising his clients to sign the factoring agreements. The court did take notice of the fact that counsel had severed ties with BK Billing and cooperated with the United States Trustee. It nevertheless required that counsel disgorge the value of all fees collected by BK Billing from his clients after their petitions were filed, and reimburse them for those costs.

***In re Campbell*, 259 B.R. 615 (Bankr. N.D. Ohio 2001).**

In this 2001 opinion by Judge Pat E. Morgenstern-Clarren, the court considered the case of a bankruptcy counsel who was engaged by a previously-represented debtor in a confirmed chapter 13 case specifically to assist him in obtaining new financing. The court ordered the fee

agreement between the debtor and his new counsel cancelled, and ordered her to disgorge the undisclosed $700 she charged the debtor. The opinion lays out what counsel must do to preserve fees in the face of a challenge under section 329: (1) make a full disclosure under Fed. R. Bankr. P. 2016; (2) demonstrate knowledge regarding the Code and Rules; (3) enter an appearance shortly after retention; (4) maintain adequate records of work performed; (5) maintain records of fees paid by the debtor; and (6) have reasonable support for the fees obtained.

***In re Shelnut*, 577 B.R. 605 (Bankr. S.D. Ga. 2017).**

After the appointment of a chapter 11 trustee, parties discovered that debtor's counsel had received additional undisclosed fees by a third-party insider—in this case, the debtor's wholly-owned corporation. The parties argued that undisclosed compensation by an insider against whom the debtor had an approximately $4.4 million claim presented a conflict of interest that violated section 328(c). Counsel defended by arguing that the wholly-owned company was the debtor's alter ego. The Court found that the monies merely had passed through the corporation, and were in fact property of the estate. Nevertheless, the court partly reduced fees based on counsel's failure to supplement its fee disclosures in violation of Fed. R. Bankr. P. 2016 and section 329(a).

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

This is a follow-up to the interesting case *Sundquist v. Bank of America N.A.*, 566 B.R. 563 (Bankr E.D. Cal. 2017). In that case, the bankruptcy court awarded approximately $1 million in actual damages, $5 million in punitive damages, and an additional $40 million sanctions to be paid to public law schools and consumer law organizations for multiple and egregious automatic stay violations by Bank of America N.A. (The court's sanctions were subsequently modified by an agreed order). In this follow-up, the court took aim at counsel's asserted lien for a contingency fee. "With considerable regret at the necessity of being blunt in print, Ms. Henderson's performance in this adversary proceeding was… among the ten weakest performances by counsel for debtors that it has the misfortune to observe. It was as if she was in deep water, flailing with beginner strokes." *Id.* at 868. (The court goes on like this for nearly two pages). Here is the takeaway: under section 329(b), bankruptcy courts have enormous discretion to limit fees to the "reasonable" value of services rendered. That reasonable value need not be commensurate with the value ultimately obtained by the debtor—such as the court's award for damages, or presumably, the obtaining of a discharge—but must instead be commensurate with the quality of the services rendered.

***In re Grabanski*, 578 B.R. 458 (Bankr. D.N.D. 2017).**

In this case, creditors brought a motion to disgorge the fees of debtor's counsel under 329 after the court entered an order dismissing the case. Bankruptcy courts have authority under section 329 to order counsel to disgorge fees that exceed the amount previously approved by the court. The court retains its jurisdiction to require disgorgement of unapproved fees even after the entry of an order

dismissing the case. Creditors have standing to seek a disgorgement of attorney fees of debtor's counsel. In this case, the court ordered counsel to disgorge $44,887.74 of undisclosed and excessive fees, as well as pay reasonable attorney's fees to creditors.

***In re Carr*, 591 B.R. 474 (M.D. Fla. 2018).**

The court held that counsel's suspension from the practice of law in the state of Florida invalidated his privileges to file cases in the Middle District of Florida, which in turn required him (as a "Debt Relief Agency") to make disclosures to his clients in pending chapter 13 cases pursuant to section 526. Based on his failure to make these necessary disclosures, the court ordered sanctions of $12,000, or $1,000 for each pending chapter 13 case, and revoked counsel's privileges to practice before the court for six years.

***Cadwell v. Kaufman, Englett & Lynd, PLLC*, 886 F.3d 1153 (11th Cir. 2018).**

Reversing a lower court ruling, the Eleventh Circuit held that a law firm violated section 526(a)(4)'s prohibition on advising clients to incur new debt by indicating in its engagement letter that the client should pay the firm's retainer by credit card.

2018 WL 832894
Only the Westlaw citation is currently available.
United States Bankruptcy Court, W.D. Virginia,
Roanoke Division.

IN RE: Timothy James WILLIAMS, Jr., and Andrian Shannon Williams, Debtors.
Judy A. Robbins, United States Trustee For Region Four, Plaintiff,
v.
Darren Delafield, Upright Law LLC, Law Solutions Chicago LLC, Jason Royce Allen, Kevin W. Chern, Edmund Scanlan, and Sperro LLC, Defendants.
In re: Jessica Dawn Scott, Debtor.
Judy A. Robbins, United States Trustee For Region Four, Plaintiff,
v.
John C. Morgan, Jr., John C. Morgan, Jr., PLLC, Upright Law LLC, Law Solutions Chicago LLC, Jason Royce Allen, Kevin W. Chern, Edmund Scanlan, and Sperro LLC, Defendants.

Case No. 15–71767
Adversary Proceeding No. 16–07024
Case No. 16–50158
Adversary Proceeding No. 16–05014
Signed 02/12/2018

Attorneys and Law Firms

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William J. Charboneau, Margaret K. Garber, U.S. Trustee's Office, Roanoke, VA, for Plaintiff.

Darren Thomas Delafield, Upright Law LLC, Richard C. Maxwell, Christopher W. Stevens, Woods Rogers PLC, Roanoke, VA, for Defendants.

Sperro, LLC, pro se.

MEMORANDUM OPINION

Paul M. Black, UNITED STATES BANKRUPTCY JUDGE

***1** This matter comes before the Court on Complaints filed by the United States Trustee for Region Four ("UST") against Darren T. Delafield, John C. Morgan, Jr., Upright Law, LLC ("Upright"), Law Solutions Chicago, LLC, Jason Royce Allen, Kevin W. Chern, Edmund Scanlan, and Sperro, LLC on May 31, 2016 and June 30, 2016. Separate adversary proceedings were filed in the bankruptcy cases of Timothy and Andrian Williams, filed by Darren Delafield ("Delafield") as an Upright partner, and of Jessica D. Scott, filed by John Morgan ("Morgan") as an Upright partner. The two cases were consolidated for trial. Sperro, LLC did not file a response, nor has it appeared in this action. Default was entered against it on July 15, 2016 and August 17, 2016. The remaining defendants are collectively referred to as the "Upright Defendants." Extensive discovery took place and numerous motions were heard prior to trial. A four day trial was conducted September 25–28, 2017, during which multiple witnesses testified and thousands of pages of exhibits were submitted. All parties submitted post-trial briefing once the transcripts were prepared, which briefing was completed in late December 2017. This matter is now ripe for resolution.

FACTUAL BACKGROUND

This case involves yet another collision between traditional methods of providing—and policing—legal services to consumers for bankruptcy matters and attempts by attorneys and creative online marketers to tap into that market on a high-volume, multi-jurisdictional basis. On November 15, 2015, this Court issued an opinion in which it stated:

> [T]hese cases reflect the Pandora's Box of ethical issues opened by multi-jurisdictional practice [through] the "national law firm" business model, where law firms in distant locations around the country advertise on the internet, and then seek to retain a local attorney to become a local "member"—albeit one with limited, if any, rights other than in the cases they actually take.

Robbins v. Barbour (In re Futreal), Misc. Pro. No. 16-00701, 2016 Bankr. LEXIS 3974 (Bankr. W.D. Va. Nov. 15, 2016).

Little has changed.

The UST attempts to paint Upright and by association its local "partners" as money hungry "bankruptcy boiler room" operators that have stepped over—and will continue to step over—legal and ethical lines without hesitation in their inexorable quest for the next dollar. The Upright Defendants, in turn, attempt to portray themselves as cutting-edge advocates for the financially distressed consumer. They contend they have identified a void in the legal market for consumers that they are uniquely able to fill by using technology and the internet to match underserved areas of clients with attorneys who have the capacity and ability to fill their needs on a national basis, all while staying within the bounds of the law.

This case was aggressively litigated on both sides. The Court's findings of fact and conclusions of law follow below. [1]

FINDINGS OF FACT

I. Overview of the Genesis and Structure of "Upright Law"

***2** Upright Law, LLC is a d/b/a for Law Solutions Chicago, LLC ("LSC"), an Illinois limited liability company. LSC also operates under various other assumed names, including Jason Allen Law, LLC, Allen Chern Law, Allen Chern LLC, and Allen & Associates, LLC among others. In at least one instance, Upright Law is referred to as "a service of Allen Chern Law LLC." UST Ex. 3–7. According to Kevin Chern ("Chern"), the members of LSC are Chern, Jason Royce Allen ("Allen"), and David Leibowitz ("Leibowitz"), all members of the Illinois bar. [2] Tr. 60–61, Day 3. [3] The mangers of LSC are Chern and Allen. Chern is the managing partner of LSC, Allen is its chief operating officer, and Leibowitz is its chief legal officer.

Chern has a past business history with an individual named Edmund Scanlan ("Scanlan"), whose expertise is internet marketing, among other things. Scanlan is not an attorney. He holds the title of executive director of LSC, although he holds no actual ownership interest in LSC. Scanlan is paid a base salary of $200,000.00 by LSC for which he receives an IRS Form 1099, presumably as an independent contractor. LSC has very few actual employees—the ones it does have are in-house Chicago attorneys—instead leasing most of its employees from Mighty Legal, LLC. [4] Mighty Legal, LLC in turn is owned by Justiva, LLC, which is owned by Chern, Scanlan, Allen and some others not parties to this litigation. Justiva, LLC also owns Royce Marketing, LLC, which provides marketing services to LSC. [5] Scanlan does not share in the profits or losses of LSC. However, for all practical purposes, LSC is the only client of both Mighty Legal and Royce Marketing, and the arrangements with Mighty Legal, Royce Marketing—and ultimately Justiva—allow for significant funds generated by LSC to flow to Scanlan, Chern, and others. [6]

Chern testified that, while working with Scanlan to provide online marketing services to small law firms, he identified "that there was an enormous gap between the number of consumers who are actually reaching out and saying that they need legal assistance and the number of attorneys that are interested in proliferating information about their availability to provide services to those consumers." Tr. 55, Day 3. In 2013, Chern approached Allen, who at the time ran LSC, and discussed joining with him to attempt to match up on a multi-jurisdictional basis attorneys who were looking for work with consumers who needed bankruptcy assistance, but, for a variety of factors, were unable to obtain counsel. According to their research, clients overwhelmingly preferred not coming into "brick and mortar locations," instead they preferred receiving legal services without the burdens of travel. This led to the establishment of a "remote onboard process for clients," with LSC centralizing its operations in Chicago and abandoning the traditional client office-visit arrangement. Tr. 58–59, Day 3. Unless otherwise described in this Opinion, "Upright Law," "Upright" and "LSC" are generally referred to as one in the same.

A. The "Onboarding" Process

**3* The trial evidence reflected that when a prospective client searches the internet for a bankruptcy attorney and comes across Upright Law, the client generally reaches out one of two ways: they either call Upright Law or request information through an online request form. This reach out, in turn, prompts a call back from a "client consultant." In 2015, Upright had a bifurcated client intake process involving non-attorney personnel in Chicago called "client consultants" and "senior client consultants." Client consultants were junior employees whose job it was to gather basic information and probe whether the prospect was really interested in filing for bankruptcy, whether they had the ability to pay for services, and whether they were the decision maker for the family.[7] Chern, Tr. 88, Day 3. If those qualifications were met, the prospect was passed on to a senior client consultant.

Senior client consultants were usually former client consultants who had been promoted after a period of time. According to Chern, their job was to identify the consumer's motivations and desires, what goals they were trying to achieve, and whether there was a precipitating event that was driving them to file. *Id.* at 88–89. These individuals are not attorneys and are paid a base salary plus commission. Sales employees were also trained in a boot-camp type arrangement. They were provided with a "Playbook," which taught them a variety of methods to "close" the sale of bankruptcy services to individuals seeking relief.

For example, UST Exhibit 37 is an Upright Law "Sales Play Book," which provides at Chapter I "Sales Rules & Theory—Close or be Closed." It includes topics such as the "Pitch Outline," the "Pitch Script," "Moving to the Close," and "Objection Handling." It is replete with high pressure sales tactics, some of which recommended to "close" the sale are unsettling to the Court.[8] Under objection handling, senior client consultants are taught to respond as follows if a prospect says "I need to pray about it":

> I appreciate that. I pray about every decision I make myself. How are you most comfortable paying? Let's pray together. I trust God won't mislead either of us. I am willing to accept God's will for the both of us.

UST Ex. 37, p. 12. Moreover, if a prospect said, "I need to talk to my Wife/Husband," senior client consultants were advised to respond with responses including: "I agree, and you should, but if your husband/wife is anything like mine, he/she never tells me no when I really need or love something, and I never tell him/her no." *Id.* Or, "[b]etter to ask for forgiveness than ask for permission, so let's get you going right away[.]" *Id.* Under the Playbook's "Now or Never" pitch, Upright sales people were advised to state as follows:

> This is the offer I am making you for right this moment in time, and it is a now or never offer as I will not be able to make this available tonight, tomorrow, or event [sic] later today. Because we have an incentive available to us right now, I am able to offer this to you now but it expires when we get off the phone. Let's take advantage of the incentive.

UST Ex. 37, p. 7. If a prospect is already represented by counsel, sales personnel are directed to "[t]ell the client to fire their local attorney, they can send an email, then they can hire us." Upright Ex. J7, p. 11.[9]

**4* One of the senior client consultants, Brandon Fox ("Fox"), testified by deposition that he was paid a base pay of $40,000, plus a commission tied to how may "closes" he obtained. Tr. 289, Day 1. Another senior client consultant, Angelo Walsh ("Walsh"), testified by deposition that each client consultant had a minimum requirement to meet or no bonus would be paid, and each "salesman has a specific number or amount of fees collected they need to hit in order to remain employed." Tr. 304, Day 1. The sales numbers were tallied on a 45 day basis, and changed frequently. Tr. 289, 304–05, Day 1. Fox testified that he understood he was hired to "sell[ ] bankruptcy to people."[10] Tr. 287, Day 1.

The non-attorneys were instructed they could not provide legal advice. Chern, Tr. 169, Day 3. Fox and Walsh confirmed that instruction. However, in several instances in the matters before the Court, those instructions were not followed by Upright non-attorney personnel.[11] The conversations with the debtors involved in this action were recorded by Upright Law, and those transcripts were introduced into evidence by the UST. UST Exs. 3–1, 4–1. Among other things, prospects were told that they were a "perfect candidate for filing for

bankruptcy," and their filing chapter was pre-selected before they ever spoke to an attorney. UST Ex. 3–1, Tr. pp. 11–12, 43–45. A prospect was examined by a non-attorney to "see if you qualify to file," conceded by Allen to be unauthorized. UST Ex. 3–1, Tr. p. 4; UST Ex. 26, Tr. pp. 84–85. In addition, one client was advised, after asking about whether certain debts would be included in her case, that it would be up to the trustee to make that determination. UST Ex. 3–1, Tr. p. 21. In at least one instance in this case, a debtor was told she could leave a debt off her bankruptcy schedules to protect an ex-spouse.[12] UST Ex. 4–1, Tr. pp. 30–31. One prospect was given the advice to hide a vehicle from the lender, despite Allen's testimony that such a suggestion was "off-script." Chern confirmed such advice was outside the employee's authority. UST Ex. 3–1, Tr. pp. 75–77; Chern Tr. 252, Day 3; UST Ex. 26, Allen Dep. Tr. p. 219.[13] All of these discussions took place before a prospective client ever spoke with an attorney, either in Chicago or locally.

The sales personnel were supervised by a non-attorney sales director, and that sales director, in turn, reported to Allen. "Onboarding attorneys" in Chicago are supposed to confirm that the non-lawyers did not provide the client with any legal advice,[14] but as seen, this check appears less than effective based on the evidence at trial. Once a client was "closed" or sold on bankruptcy, and money was received or payment scheduled, an "oral retention" agreement was entered into and the client was then transferred to an attorney. No conflict check was run before a client was presented with the oral retention agreement.[15] Among other things, the oral retention agreement used in 2015 provided if the client is seeking to file bankruptcy under a certain chapter of the Bankruptcy Code, that the "firm does not represent you until you talk to you [sic] local attorney and they accept you as a client," and that until fees are paid in full, the firm will not take action to file the case. The oral retention agreement further advises that the client acknowledges that the firm will be performing work on the client's behalf, such as by fielding creditor calls, answering client questions, and preparing the petition. In addition, "[p]ayments made are direct compensation for that work on your case and are generally non-refundable as they are earned." UST Ex. 58. The oral retention agreement provides that an electronic retainer agreement will follow which the client is obligated to sign and return. *Id.* In the Western District of Virginia, forty-eight percent (48%) of all clients paying over time never complete their payment plans, and the cases are not filed. UST Ex. 1, p. 5. In general, the fees that are not refunded are not shared with the "local partners."

B. The Local Partners

5 In furtherance of its national marketing and business plan, Upright brings on local attorneys around the country as "partners," "local partners," or "limited partners." These attorneys generally have their own practices and have limited signage and advertising indicating they are affiliated with Upright. The attorneys get a different CM/ECF case filing password for their own practices, and a separate one for cases filed as an Upright partner. The local attorneys sign a limited partnership agreement that provides they have no rights in the management of the firm and only a marginal, non-voting interest in it. The attorneys are licensed in their home state.

Prior to September 2015, the senior client consultant would set up a recurring payment plan for a client to start paying his or her fee, and an engagement agreement would be generated and sent to the client. At that point, the local attorney or "limited partner" would get an email inviting the attorney to contact the client. The attorney would have forty-eight (48) hours to contact the client and do the initial welcome call.[16] Chern, Tr. 190–192, Day 3. Assuming the partner approved of the representation and did not have any modifications to the representation, whether in terms of fees or the relief sought by the client, they confirmed the representation back to Upright. *Id.* at 191.[17] At that point, Upright would take calls at the main office in Chicago. If they had a matter that required local participation, the client would be transferred or an email sent to the partner to contact the client. *Id.* at 191–92. Once the client paid in full, Upright had a team of "document collectors" who would "interface with the client and collect all of the documents remotely." *Id.* at 192. An associate attorney on staff in Chicago would prepare an initial draft of the petition and do an initial Skype interview with the client. A second interview and petition review would be scheduled with the local attorney, who would go over final changes to the petition, make any changes or corrections, and then file the petition. These meetings were by Skype or in person. The local attorney would attend the initial meeting of creditors. *Id.* After September 2015, the process was the same until the client paid in full. At that point, Chern testified Upright decided to pay the local partners more, but also shift to them the responsibility of collecting information and preparing the petitions. *Id.* at 192–93. That system prevails today.[18] Upright, however, has at all times

prepared in Chicago the Rule 2016 disclosures for the local partners and continues to do so. Chern, Tr. 197–98, Day 3.

In early 2014, LSC/Upright was advertising on the internet that it had local offices "nationwide." However, at that time, it only had local partners in fourteen (14) states. Chern, with assistance of another attorney, took the lead on recruiting local partners, targeting attorneys with approximately 20 years of experience or more in consumer bankruptcy. [19] Today, Upright has approximately 400 partners. Chern, Tr. 135–36, Day 3. Upright used to advertise that it had "local offices nationwide," but advertises now that it has "attorneys in offices nationwide," presumably to squelch any concerns that it does not have any office space actually leased anywhere but Chicago. The local partners are conducting Upright business locally out of their individual offices, according to Chern. Chern, Tr. 155–56, Day 3. Chern testified that Upright's website currently states that it has "attorneys in all 50 states across the nation." Chern, Tr. 156, Day 3. Upright holds the partners out to the public with the title, style, and attribute of "partner," which appears on the firm's website, letterhead, business cards, and in some cases, office signage. Chern, Tr. 187–88, Day 3. The local partners are to take reasonable steps to apprise potential clients of their affiliation with Upright. *Id.*

***6** In 2014, LSC/Upright was not authorized or qualified to do business in Virginia. An affidavit from the Virginia State Bar indicates Law Solutions Chicago, LLC is not registered with the State Bar. However, Upright Law, LLC, a Virginia limited liability company, was formed January 9, 2015, and Allen sent a document to the Virginia State Bar to qualify it with the Bar that same date. However, the bar qualification document was not signed by a member of the Virginia State Bar, as required. That deficiency was ultimately corrected, and Upright was qualified with the Virginia State Bar effective August 12, 2015. UST Ex. 57. The Virginia State Bar has taken no action against Upright for its tardy registration, despite beginning the provision of legal services in Virginia sometime after January 23, 2014 when it confirmed its arrangement with Morgan to provide services out of his office in Warrenton, Virginia. UST Ex. 41. [20] Upright began generating revenue from Virginia clients in late January or early February 2014.

1. The Partnership Agreements and "Partnership"

The UST contends that the LSC local partnership structure is nothing more than a "bankruptcy boiler room" and "telemarketing referral business," with the Chicago office as a "referral hub," and the partnership agreements just another way "to secure another person to attend 341 meetings and whitewash LSC's unauthorized practice of law, while [the local partner's] purpose was to receive additional revenue with minimum input." UST Initial Closing Argument ("UST Brief") at 3, 8, 15. The testimony and exhibits were voluminous on this point, both in terms of the UST's case and Upright's response, and the Court will attempt to summarize and condense them. Each local partner is required to sign a partnership agreement, which is revised and updated periodically. Pursuant to these agreements, local partners are entitled to a share of the revenue generated from that local partner's clients and a bonus pool formed from revenue generated in the local jurisdiction. These local partners receive Schedule K–1s to report their Upright-related income, as opposed to a Form 1099 or a W–2. Upright provides the local partners with access to its SalesForce software system, its case management system, so that they can log in and work on a client's file with Chicago personnel. They also have access to Upright's Best Case bankruptcy software system and an Upright credit card for the payment of filing fees. Upright also provides the local partners with malpractice insurance. Chern, Tr. 182–88, Day 3. [21]

The partnership agreements outline the allocation of certain rights and responsibilities between Chicago and the local partner, including the financial compensation, and Section 24 of the partnership agreement states that limited partners have "no right to participate in the management of the Firm." *See e.g.*, UST Ex. 43, Upright Ex. D8, Morgan Agreement, ¶ 24. From 2014 to March 2016, Virginia residents were given fee agreements which provided that money paid to LSC was earned on receipt. Chern contended, however, such language was not intended to restrict or curtail the limited partners in performance of the ethical duties or abilities to provide input into the firm's operations. During that same time frame, attorney's fees were placed directly into either LSC's Illinois general operating account or LSC's Virginia operating account.

***7** Limited/local partners are invited to attend bi-monthly "partner's meetings" by teleconference during which Chern solicits feedback about firm operations. In addition, during months when there is no partnership conference, Chern convenes a telephone conference of the Virginia limited partners so they have direct access to him. Chern, Tr. 183

–85, Day 3. There is also an annual partnership meeting in Chicago that limited partners are invited to attend, as well as a partner newsletter that goes out periodically.

2. Local Partner John C. Morgan, Jr.

Morgan is a member of the Virginia State Bar, with his office in Warrenton, Virginia. He is admitted to practice in the United States Bankruptcy Courts for the Eastern and Western Districts of Virginia. He has been disciplined twice by the Virginia State Bar, once for contacting the represented client of another attorney in a criminal matter, and the second time for the commission of a felony. He was suspended by the Bar for three years for the second matter. UST Ex. 24, Tr. pp. 126–27.[22] Morgan obtained electronic filing privileges in this Court in 2005 and has engaged primarily in consumer bankruptcy cases in this Court since then.

In early to mid-January 2014, Chern approached Morgan about joining Upright and establishing a Virginia presence. Prior to Morgan joining Upright, Upright had no presence in Virginia. Morgan took notes of his initial conversation with Chern. The notes reflect that "Kevin Chern and Ed Scanlon [sic] have started a new national law firm." UST Ex. 72. Among other things, the duties of the local partner were to do a 10–15 minute compliance call within 24–48 hours, the firm would take client calls and creditor calls, presumably at "headquarters" in Chicago. The firm would prepare the petition. Morgan would be required to obtain a separate ECF login for these cases and handle the petition signing and the Section 341 meeting of creditors. Chapter 7 cases are said to have a "25% margin" and Chapter 13 cases have a "40% margin."[23] *Id.* Morgan subsequently applied for and obtained a new ECF filing login for "UpRight Law LLC" on October 9, 2014. UST Ex. 50. He filed his first case in this Court for Upright on October 29, 2014.[24] Overall, at least nine (9) cases have been filed under Morgan's Upright ECF password—mainly Chapter 7 cases with one under Chapter 13. Stip. ¶ 17. Morgan's 2016 K–1 from LSC reflected $18,620.00 in self-employment earnings from LSC. Upright Ex. P5, pp. 85–86.[25]

3. Local Partner Darren T. Delafield

***8** Delafield has long appeared before this Court, and the Court is well familiar that his practice consists primarily of representing consumer debtors in Chapter 7 and Chapter 13 cases. Delafield first obtained ECF filing privileges in this Court in October 2004. As mentioned above, he has received prior admonition from this Court with instructions as to the future handling of cases, as well as a private reprimand from the Virginia State Bar. UST Ex. 63.

In early December 2014, Chern solicited Delafield to become a local partner of Upright. On December 3, 2014, Chern sent Delafield a pitch email, which provided, in part, as follows:

> Our goal at UpRight is to improve people's lives by providing the highest quality services, most effective legal strategies and world class customer service. I firmly believe that the only way to accomplish that end is to leverage both our incredible systems, technology and operations at our headquarters in Chicago and the intense subject matter expertise of local practitioners like you. We strive to be America's premier virtual consumer law firm that is geographically agnostic, representing clients in both rural and metropolitan areas, and allowing consumers to interact with their lawyer online, the same way they transact business with their banks and other professionals.

UST Ex. 45.[26] Delafield signed a partnership agreement with LSC/Upright shortly thereafter. UST Ex. 46.

Delafield applied for an ECF login for "UpRight Law LLC" by application dated January 9, 2015, which was promptly issued. He filed his first Upright case in this Court on January 10, 2015. In total, more than thirty (30) cases have been filed by Upright in this Court though Delafield's login, with seven (7) cases having been filed before Upright was properly registered with the Virginia State Bar. Stip. ¶ 19.[27] Delafield's 2016 K–1 from LSC reflected $21,741.00 in self-employment earnings from LSC. Upright Ex. P5, pp. 189–90.

C. The "New Car Custody Program" or "Sperro Program"

Chern testified he met an individual named Brian Fenner ("Fenner") as a result of both having attended the National Association of Consumer Bankruptcy Attorneys annual

conference in Chicago in 2015. Fenner was a sponsor and exhibitor, and he obtained Chern's name off a list of attendees. Prior to 2015, Fenner had long experience in the repossession industry. Fenner owned and ran multiple companies, including Collateral Services of Indiana, LLC, Sperro, LLC, and Fenner & Associates, LLC.

***9** Chern testified that Fenner described a service he provided called the "New Car Custody Program" or the "Sperro Program." As described by Chern, Fenner pitched this program as a service to consumer debtors who wanted to surrender their car in bankruptcy. Fenner explained that his service facilitated the return of collateral to the auto finance company by having the debtor turn the car over to Fenner, and Fenner would in turn notify the finance company that he has the car, and if desired, he would return the car to the finance company. Chern contends that Fenner advised him that Fenner would give the finance company the option of using Fenner's auction services, or they could pick the car up from Fenner.

Chern testified Fenner's program interested him because Fenner offered to pay the legal fees for consumers who were interested in participating in it.[28] As is the case in many bankruptcy cases, clients struggle to come up with the fees to pay their attorneys, as well as filing fees. One of the benefits of the program gleaned from Chern's testimony was that this would enable a consumer debtor who wanted to surrender his or her vehicle to have the attorney's fees paid by a third party such that the debtor did not have to go out of pocket, and it would eliminate the delay in filing precipitated by an installment payment plan that a debtor may or may not complete.

In May 2015, Chern told Fenner he would ask Leibowitz to contact Fenner and investigate the "risks/rewards" of participating in Fenner's program. Leibowitz did that, although he testified he only reviewed the "risks," and Chern advised Fenner that they would be moving forward. On May 11, 2015, Fenner emailed Chern, after being told he passed the "smell test," stating as follows:

> Wonderful, attached is a copy of our standard towing and storage agreement. Please advise if there is anything you would like changed. Depending on the region where the collateral is picked up, the only change we make is the lot location where the collateral is stored. *That being either Nevada, Mississippi, or Indiana.*

UST Ex. 35–10 (emphasis added).

This was the beginning of a scam.

Fenner sent another email to Chern on May 12, 2015, advising of their hookup fees, towing rates, and impound fees. Fenner advised Chern as follows:

> To perfect our lien process, we hold the car for 30 days. This is a state statute. At the 31st day the account would be in default status. This will generate the lien process. We then send both the consumer and the lien holder notification by certified letter via US post office. We follow the lien process accordingly to witch [sic] state we are storing the collateral. At this time, the lien holder will make their choice on how they wish to move forward.
>
> I believe that if you put in the BK petition that Fenner & Associates paid for the BK and that the collateral is stored at Collateral Services of Indiana LLC with our address, collaterals [sic] location. This should be more than enough notification to the lien holder and the court the intent, location and status of the collateral.
>
> ***10** We have to hold the vehicle so many days before we can perfect our lien by state law. We also need some time to generate a profit margin. I would prefer not to send notification to the lien holder from the existing attorney up front. The Lien holder would already be notified in the petition. Any attempts to speed the process would eliminate our perfection of the lien as well as cutting our profit.

UST Ex. 35–18.

On May 18, 2015, Chern asked Fenner for a copy of any correspondence that other attorneys in his program used to notify lenders that the collateral was in Sperro's possession, along with a copy of a petition to show how the compensation was disclosed to the bankruptcy court. UST Ex. 35–30. Fenner replied that no other attorneys sent such

correspondence to creditors and advised that the entity paying the fees should be disclosed as Fenner & Associates. *Id.* Fenner also asked that letters not go out to creditors until at least five days passed from pick up, in order to give the collateral time to reach his storage facility in Indiana. *Id.*

On June 18, 2015, Chern sent an email to all Upright partners advising “New Car Custody Program at UpRight Law—Read Carefully.” UST Ex. 35–53. Fenner was blind copied on the email. In that email, Chern advised his limited partners that Upright's senior client consultants had started offering a new program to clients to surrender a vehicle to a towing and storage facility and have the cost of their bankruptcy case fully subsidized. In order to qualify, Chern advised that the following conditions needed to be met: (i) the client wanted to file Chapter 7, (ii) the client has a vehicle he or she is willing to surrender, (iii) there is no equity in the vehicle, and (iv) the vehicle is worth greater than $5,000.00. *Id.* The client is advised to contact Fenner's company “Sperro,” and to arrange for Sperro to take custody of the vehicle. At the time of surrender to Sperro, the client signs a towing, storage and custody agreement with Sperro whereby the client contracts with Sperro to load the vehicle, tow it to a facility, store and maintain it until such time as the finance company picks up the vehicle. *Id.* Chern advised his colleagues that Sperro charges “customary and reasonable fees for these services (e.g. $75 loading fee, $1.50 per mile towing, $45/day storage, etc.).” *Id.* Chern advised that Upright—not Fenner—notices the finance company by certified mail “within a couple of days that Sperro has custody of the vehicle, the location of the storage facility, contact information for Sperro and instructions that they should recover the vehicle as soon as possible to avoid excessive storage fees.” *Id.*

The benefits to the clients were also described. Chern told his local partners that the client can immediately cancel the insurance. The client no longer has to maintain it or worry about the expense or inconvenience of plating or storing a vehicle. The client does not have to worry about the repossession agent showing up at home or at work. The creditor can be referred to Sperro as to the status of the vehicle. The client does not have to worry about finance companies who refuse to pick up a vehicle, and “[i]mmediately upon placing the vehicle in Sperro's custody, Sperro will remit the entire legal fee plus filing fee to UpRight Law on client's behalf.” *Id.*[29]

***11** An Upright limited partner named Mark Steinberg in Miami, Florida immediately questioned the program after it was rolled out, and on June 18, 2015, Chern told Steinberg as follows: “[t]hey hold the car in one of three states that allow for mechanic's liens that trump the 1st lien. 60% of the time, they pick up the car and satisfy the charges. 40% of the time they just abandon the vehicle. Sperro really makes its money when the finance company abandons and Sperro auctions it off.” UST Ex. 35–55.[30] So, at least as early as June 18, 2015, Upright senior management knew that Fenner and his companies were towing cars out of states like Florida (and as will ultimately be seen, Virginia) to Fenner-related storage lots in Nevada, Mississippi, or Indiana for the purpose of trying to prime secured lenders, or hold their collateral hostage, with excessive hookup, towing and storage fees that were completely unnecessary. But, Fenner and Sperro were willing to pay Upright's clients' attorney's fees and filing fees in order to get the referral from Upright to do it. Also significant to the Court is that all of this was offered to prospective clients by Upright using “senior client consultants” without the clients ever having spoken to their local attorney before being placed into the program,[31] and Chern was negotiating with Fenner for Sperro “to pay our marketing company $150 for each deal we generate from partners ....” UST Ex. 35–54, a June 18, 2015 email from Chern to Fenner.[32] As will be seen below, Chern further authorized the dissemination of letters to finance companies over the names of Upright's local partners from the Chicago office, and listing the local attorney's addresses as Chicago, without the knowledge of some of those attorneys.

Chern testified that he decided to terminate Upright's participation in the New Car Custody Program on or about November 19, 2015 due to a variety of factors, one of which was Chern learning from one of his limited partners that a lawsuit was filed by Ally Financial against Sperro and others alleging that the defendants in that case were complicit in converting its collateral. At that point, after reviewing the allegations in Ally's complaint, Chern decided that Upright should not refer any more clients to Sperro until the court ruled in that litigation. Chern, Tr. 86, 104–05, Day 3. In October, Chern was also getting concerned with Fenner and Sperro becoming increasingly tardy with the payment of Upright's attorney's fees, even though they had picked up client vehicles. *Id.* at 105–06. Finance companies also started complaining to Upright about Sperro's excessive towing and storage fees. *Id.* at 107–08.

D. Debtors Timothy and Andrian Williams

Timothy and Andrian Williams are “assisted persons” who filed a Chapter 7 bankruptcy petition in this Court on December 22, 2015.[33] Stip. ¶ 28. They are husband and wife, residing in Smyth County, Virginia.[34] In August 2015, the Williamses were experiencing financial trouble, and Ms. Williams began searching the internet for bankruptcy options. In a search, Upright Law came up, and she filled out an online information request form. Her husband was contacted by an Upright representative by telephone later the same day. The calls between Upright and their prospective clients were recorded, including the calls with the Williamses. The Williamses spoke to Upright, in part, because other attorneys they had spoken to in the past would not assist them unless they had money to pay their fees. Williams, Tr. 97–98, Day 1.

***12** The Williamses advised Upright they were being called by various creditors, in particular, GCB Acceptance Corp. (“GCB”), the secured lender on their Ford Taurus. Ms. Williams was becoming stressed about the calls. Mr. Williams spoke with Upright's client consultants and he was informed Delafield would be his local attorney. The total attorney's fees and filing fee quoted were $1,985.00. The Williamses wanted to return the Ford Taurus to GCB, but GCB only offered refinancing even though they were seriously delinquent. After going through their financial situation with a client consultant named Alexis Ball, Mr. Williams was told “you seem like the perfect candidate for filing for bankruptcy. We definitely want to help you get your financial independence back.... And I think filing bankruptcy would help you do that.” Stip. ¶ 29, UST Ex. 3–1, Tr. p. 11–12.

Mr. Williams had inquired about continuing to pay on several payday loans, and Upright's non-attorney consultant advised him “it's going to be up to the trustee whether or not they're going to include those into the bankruptcy ....” UST Ex. 3–1, Tr. p. 21. Later, when told by a senior client consultant that his credit score would go up by 85 to 135 points after he filed bankruptcy, Mr. Williams apparently decided to include the payday credit loans, stating that “I mean, now that I know that ... filing bankruptcy is going to help my credit, yeah.” *Id.* at 35, 40. The senior client consultant then advised “it just makes sense to just get rid of everything ... if you continue to hold on to that and you miss a payment, it's going to ruin your credit while we're trying to build it for you ....” *Id.* at 40.

Once the Williamses mentioned their issues with the Taurus, one of Upright's senior client consultants brought up the Sperro Program as a way to get GCB dealt with and to have their attorney's fees and filing fee paid at the same time. The Williamses, before they ever had a chance to consult with their local attorney, were asked to call Sperro directly and talk to them about surrendering their car and having their attorney's fees and filing fee paid. Once Sperro sold the car, and their fees were paid, the Williamses would be refunded any fees they had paid toward Upright in the interim.[35] In one conversation with senior client consultant Angelo Walsh at Upright, Mr. Williams advised he was being contacted by GCB about the car and indicated that GCB advised they would pick it up if a payment was not made. Walsh, in turn, reminded Mr. Williams that Sperro would be contacting him to pick up the car, and that if he turned it over to GCB he would likely get nothing for it. Walsh advised Mr. Williams, that although it was up to him, “in this situation, if I were you, I would keep it hidden and we come get it, and at least pay off some of your bankruptcy ....” UST Ex. 3–1, Tr. pp. 75–76.

Mr. Williams questioned the legality of the Sperro Program with a non-Virginia licensed Upright attorney named Ryan Galloway. Mr. Galloway told Mr. Williams the Sperro Program was legal. Stip. ¶ 32. Mr. Williams later spoke with an Upright onboarding attorney named Jacob Brown, and Brown explained the Sperro program was like parking a car in a fire lane. The car gets towed to a lot, then the finance company has to pay the towing company and lot owner to get it back. “And so that's like where Sperro makes all their money,” Brown told Mr. Williams. UST Ex. 3–1, Tr. pp. 87–88. “So, it's totally fine ...,” Brown said. *Id.* At no time in the recorded call transcripts does it appear that any Upright personnel told the Williamses the cars were being towed out of state.

Sperro sent the Williamses a transportation and storage agreement, and the Williamses signed an agreement with Sperro. Sperro had the vehicle picked up and transported it from the Williamses' residence in Smyth County, Virginia to Sperro's facility in Indianapolis, Indiana. The security agreement between the Williamses and GCB provided that the Williamses agreed, among other things, “not to sell, encumber or abandon the Collateral,” and “not to remove or attempt to remove said collateral from the county and state given above as my address without notifying you in writing ....” Stip. ¶ 37.

*13 Upright then emailed Delafield to approve the representation. On September 1, 2015, Delafield spoke with the Williamses and confirmed his representation to them as an Upright partner for their Chapter 7 bankruptcy case. However, on September 4, 2015, without ever having spoken to Delafield, Sperro picked up the Ford Taurus and towed it away. Sperro sold the car at auction on or about October 9, 2015. Stip. ¶ z. On September 8, 2015, someone at Upright mailed a letter to "General Acceptance Corporation" in Greenville, North Carolina, supposedly the lender for the Taurus, when the actual lender was GCB in Johnson City, Tennessee. UST Exs. 3–7, 3–9.[36] The letter advised the lender, albeit the wrong one, that, after identifying the Williamses, the collateral, and VIN on the Taurus,

> You are hereby notified that on September 1st, 2015 my client placed the above-captioned collateral, upon which you allege to hold a security interest, into the custody of Sperro Towing and Recovery, located at 2534 Bluff Road, Indianapolis, Indiana 46225. Please contact Sperro to arrange to recover the vehicle .... To avoid unnecessary storage and maintenance fees, please contact them immediately.

UST Ex. 3–7. A telephone number was provided. The letter was closed by the signature line Darren Delafield, 79 W Monroe, 5th Floor, Chicago, IL 60603. Delafield neither saw nor authorized this letter before it went out.[37]

On September 21, 2015, LSC deposited a $1,650.00 check from Fenner & Associates into LSC's operating account and deposited a $335.00 check from Fenner & Associates into an IOLTA account. Stip. ¶ 38. The October 16, 2015 engagement agreement with Upright described the fees charged to the Williamses as "Attorney's fees: $1600.00; Court Filing Fees: $335.00; and Report Fees: $50.00. Total Fees, $1985.00." Stip. ¶ 39. The Rule 2016 disclosure reflected the attorney's fees were paid by "Sperro." UST Ex. 3–15, p. 92. The Williamses met with Delafield several times by Skype and their petition was ultimately filed on December 22, 2015.

The Sperro Program came to light at the Williamses' 341 meeting, and Delafield denied knowing why Sperro paid the Williamses' fees in connection with their case. Stip. ¶ 40. However, Delafield admitted at trial he knew as early as December 2015, as the Williamses had told him, that the car had been used to pay their fees. Delafield, Tr. 143–44, Day 2. Delafield also admitted in his Answer to the Complaint that he received the June 18, 2015 email about the New Car Custody Program from Chern. UST Ex. 3–33; Delafield, Tr. 142 –43, Day 2. At the 341 meeting, Delafield attempted to deflect any questions regarding Sperro by the Trustee and GCB's counsel to an unidentified "senior attorney" at Upright for further explanation, professing ignorance as to the relationship between Sperro and Upright. UST Ex. 3–2. The Chapter 7 Trustee referred the matter to the UST, and a motion for a Rule 2004 examination was filed and granted by Order on March 15, 2016.[38] Treating joint debtors as a single client, not less than 219 clients of LSC participated in the Sperro Program, of which 7 resided in the Western District of Virginia. UST Ex. 62; Stip. ¶ 27. Nationally, Upright generated not less than $333,545.00 in fees from the Sperro Program, exclusive of filing fees, before it was terminated. Tr. 340–44, Day 2.

E. Debtor Jessica Dawn Scott

*14 Jessica Dawn Scott ("Scott") is an "assisted person" who filed a Chapter 7 petition with this Court on February 24, 2016. Stip. ¶ 41. Scott first learned of Upright through an internet search and understood it to be a law firm based in Chicago with partnerships throughout the United States. Scott searched the internet, and Upright came up early in her search. Like the Williamses, Scott told Upright that she was interested in surrendering a car, and Upright told her about the Sperro Program. Scott spoke with Brandon Fox, an Upright senior client consultant, on October 14, 2015. When asked if she knew what Chapter she wanted to file, Scott said "Whichever wipes out everything." Fox replied: "Okay. So Chapter 7 definitely." UST Ex. 4–1, Tr. p. 13. Scott had a 2005 Pontiac Sunfire she wanted to surrender financed with Credit Acceptance Corporation. Regarding the Sperro Program, Fox explained,

> "... so it's a partnership that we have with a repossession company. So they work out a deal with the bank ... they come and pick up the vehicle. Now rather than you having a repossession sitting on your—on your record, we're going to file a bankruptcy. So any debt that you have is removed off of your record.... And whatever the balance is of that vehicle that we get, the check, we refund you all of that money back.

UST Ex. 4–1, Tr. pp. 13–14. Later, on October 19, 2015, Scott spoke to Fox again and inquired about a debt she had co-signed with her ex-spouse. The exchange went as follows:

Scott: ... like my ex and I have a loan together. Like what happens with that?

Fox: Okay. So if you're both on a loan, you'll be taken off of all responsibility of the loan and he'll be fully responsible.

Scott: Oh, God, that sucks.

Fox: Now if you want to keep that loan though, we can keep it off and you can continue to pay on it ....

Scott: But I still don't want to screw him over.

Fox: Okay. Well I mean, we can leave that off, that's not a problem.

UST Ex. 4–1, Tr. pp. 30–31.

On October 20, 2015, Scott executed an engagement agreement with Upright. Scott's fee agreement stated that the total fee for her bankruptcy, including filing fees, was $1,835.00. Scott made a $100.00 payment to LSC as a partial payment toward its attorney's fees. On or about October 24, 2015, Scott spoke to Morgan over the telephone for an initial consultation and he approved her as a client. The first time Morgan ever met with Scott in person was when she was deposed in this case, although he did talk to her over the telephone. Scott met with Morgan's wife, Rhonda, who is his assistant in his law practice.[39] She is not an attorney. Morgan did not review Scott's petition or schedules with Scott, and Morgan did not witness Scott sign them either. This was delegated entirely to Rhonda Morgan.[40] The filings with the Court were replete with errors, including (1) the Rule 2016 disclosure failed to reflect the proper amount of fees paid to Upright, (2) the Rule 2016 disclosure failed to reflect that the fees were paid by Sperro and/or Fenner & Associates, (3) the Statement of Financial Affairs indicated that the 2005 Pontiac Sunfire was "attached, seized, or levied," and (4) the Statement of Financial Affairs indicated that she transferred no property to anyone within the two years of filing bankruptcy. UST Ex. 4–10.

***15** A former associate in Morgan's firm named James McMinn, who had no relationship to Upright other than working for Morgan in his separate private practice, attended the 341 meeting, and as in the Williamses' case, the Sperro Program came to light when questions were raised about what happened to the Sunfire and who paid the attorney's fees. Morgan said he had Scott's permission to have someone else appear on his behalf, but he has no confirmation of that fact. His own time records reflect he attended the 341 meeting, when clearly he did not. UST Exs. 4–3, 24, Tr. p. 95.

Scott's security agreement with Credit Acceptance on the Sunfire provided in part as follows:

> You promise that you will not remove the vehicle from the United States or Canada. You will not sell, rent, lease or otherwise transfer any interest in the vehicle or this contract without our written permission. You will not expose the vehicle to misuse or confiscation. You will not permit any other lien or security interest to be placed on the vehicle.

Stip. ¶ 45. Sperro towed the Sunfire from Virginia to Indiana, and by letter dated November 9, 2015, Sperro appears to have advised "Lien Holder" that Scott's car was towed to Indiana, and that "reasonable fees [are] still due and owing at this time in the amount of $3,258.80 for the towing, storage and related service expenses for the Vehicle ...." UST Ex. 4–2, p. 7. The lien holder was advised that if the foregoing charges were not paid in 15 days, the vehicle would be sold at public auction in Indiana on November 28, 2015 in furtherance of its mechanic's lien under Indiana law. *Id.*[41] On November 17, 2015, Fenner & Associates paid Upright $1,650.00 for Scott's attorney's fees plus $335.00 for the filing fee. Morgan's initial Rule 2016 disclosure filed with the Court reflected that Scott paid Upright $1,500.00 plus $335.00 for the filing fee. UST Ex. 4–10, p. 50. There was no reference to Sperro having paid any fees in that document.

McMinn discussed Scott's meeting of creditors, held on March 23, 2016, with Morgan when he returned to the office. More than two months passed before Morgan attempted to correct Scott's schedules, statements, and other papers filed in connection with the case. Stip. ¶ 53.

On June 7, 2016, Morgan filed an amended Rule 2016 disclosure, and he also filed an amended Statement of Financial Affairs ("SOFA"), which purports to bear Scott's signature under oath. Scott did not sign it and she did not know about it until she was deposed. In that SOFA, Morgan inserted that Sperro, LLC paid Upright Law LLC an attorney's fee of $1,650.00 and the filing fee of $335.00. Stip. ¶ 55, UST Ex. 4–11, 4–12. The amended SOFA does not disclose any of the funds LSC drafted from Scott's checking account, nor does it reflect that Sperro picked up the Sunfire. *Id.* Scott ultimately received a Chapter 7 discharge on July 1, 2016.

F. Assertion of the Attorney Client Privilege in Discovery

The Williamses and Scott are not parties to this litigation. There is no assertion by the UST that they did anything wrong, and there never has been. The Court finds both the Williamses and Ms. Scott to be caught up in this dispute through no fault of their own. None of the Debtors appears to have done anything more than seek out help due to severe financial distress, and rely on whoever was advising them what to do, be it an Upright sales person in Chicago or their local attorney. They did not know where else to turn, and it is truly unfortunate they have been drawn into this maelstrom.

***16** As part of the preparation for trial, subpoenas were served on the Williamses and on Scott by the UST. Discovery had previously been served on one or more of the Upright Defendants earlier in the case in which the attorney-client privilege was raised—not between Upright and its litigation counsel, but between the Upright Defendants and their bankruptcy clients. May 9, 2017 Transcript at pp. 4–5 (docket no. 76). According to counsel for the UST at a hearing on May 9, 2017, counsel for the litigants in this case agreed that since the Upright Defendants' counsel was not comfortable about asking the bankruptcy clients if they wanted to waive the attorney-client privilege, it was agreed that the UST would send Rule 45 subpoenas to the bankruptcy clients, and if those clients wanted to assert the attorney-client privilege, they could do so in response to those subpoenas. *Id.* Counsel for the Upright Defendants did not dispute this agreement.

Scott was served with the subpoena on April 10, 2017, and she produced documents to the UST on April 26, 2017. However, on April 27, 2017, with counsel for the Upright Defendants having represented they were uncomfortable discussing the attorney-client privilege with the bankruptcy clients, objections to the Scott subpoena asserting the attorney-client privilege were served on the UST by Morgan. This objection, however, was prepared behind the scenes by an attorney named David Menditto ("Menditto"), Upright's in-house litigation counsel.[42] Menditto apparently "mistakenly" put Morgan's name on the subpoena objection.

In addition, despite his own employer's actions being at issue, Upright, through Menditto, used heavy handed tactics, including text messages, to try and get the Williamses to sign conflict waivers, even though the UST informed the Court that Mr. Williams called the UST on April 27, 2017 and advised he did not want to sign one. UST Ex. 3–20; May 9, 2017 Tr. at 17. Menditto sent the Williamses a conflict waiver letter dated April 20, 2017, which suggested, among other things, that the Williamses' discharge might be at issue, despite telling them later by text message there was no allegation they did wrong. Compare UST Ex. 3–19 with UST Ex. 3–20, p. 11. While there is a suggestion that they could receive advice from other counsel, the proposed conflict letter was heavily tilted toward having the Williamses waive any conflicts and let Upright continue to represent them. Upright had to know, as a practical matter, the Williamses had limited resources to hire separate counsel.

Mr. Williams emailed Menditto on April 26, 2017, stating that:

> So, right now, I trust no one. I was told by "my lawyer" that if I did not sign the waiver that he would be solely looking out for himself only. He actually came out and said, "I will say what I have to, to save myself." [Referring to Darren Delafield].... I don't want to be defended by anyone like that, nor anyone who employs or goes into partnership with someone like that. If he is like that, then no wonder we are in the situation we are in with this case. We followed horrible advice when knowing nothing of legal matters. We were 21 and 20 when this started! I hope and pray that noone [sic] else comes to your firm for help. I don't believe that there is anyone at the firm or your partners that are truly in it to help people get out of financial trouble, but instead create more and at the same time, make money yourselves. Whether it is legal or not. *I am done speaking.*[43]

***17** UST Ex. 3–20, pp. 3–4 (emphasis added). Nevertheless, Menditto continued to persist in trying to get Mr. Williams to talk to him, clearly to lobby him to sign the conflict waiver so he could assert the attorney-client privilege on their behalf and attempt to shield their files and Upright's from discovery. *Id.*

CONCLUSIONS OF LAW

I. Jurisdiction and Venue

This Court has jurisdiction of this matter by virtue of the provisions of 28 U.S.C. §§ 1334(a) and 157(a) and (b) and the delegation made to this Court by Order from the District Court on December 6, 1994, and Rule 3 of the Local Rules of the United States District Court for the Western District of Virginia. This Court further concludes that these matters are "core" bankrupt#y proceedings within the meaning of 28 U.S.C. § 157(b)(2)(A). *See In the Matter of Kenneth W. Paciocco*, Misc. Pro. No. 15-00302-KRH, 2015 WL 5178036 (Bankr. E.D. Va. Sept. 3, 2015). A request for sanctions arising out of an attorney's conduct in a core proceeding is itself a core proceeding. *See, e.g., In re French Bourekas, Inc.,* 183 B.R. 695, 696 (Bankr. S.D. N.Y. 1995).

II. The UST's Requests for Relief

The UST has asserted six counts against the Upright Defendants and Sperro. Count I of the Complaints each asks the Court to order Delafield, Morgan, LSC, and Upright to disgorge fees under Section 329(a) and Section 105(a) of the Bankruptcy Code. Count II of the Complaints seek disgorgement of fees under 11 U.S.C. § 329(b) against Delafield, Upright, Morgan, and LSC. Count III of the Williams Complaint requests voiding of the fee agreement and disgorgement under 11 U.S.C. §§ 526(c)(1) and 105(a) against Delafield, Upright and LSC. Count III of the Scott Complaint and Count IV of the Williams Complaint seek an injunction against Delafield, Morgan, Upright and LSC, enjoining them from violating 11 U.S.C. § 526. Count V of Williams Complaint and Count IV of the Scott Complaint seek civil penalties under 11 U.S.C. § 526(c)(5)(B) against Delafield, Morgan, Upright Law LLC, and LSC, and Count VI of the Williams Complaint and Count V of the Scott Complaint seek sanctions against all Defendants under the Court's inherent powers. This last Count asks the Court to prohibit Delafield, Morgan, LSC, Upright Law, LLC, Allen, Chern, and Scanlan from practicing before this Court whether directly or indirectly through any companies in which they have ownership interests or management authority. The UST contends that cause also exists to sanction them monetarily. The Court is also asked to require Sperro and its affiliates to disgorge all funds received as a result of the Sperro Program, and to enjoin Sperro and its affiliates from remitting or providing any funds to LSC or Upright Law, LLC or to an affiliate, member, or agent of either of those entities. In both Complaints, the UST further requests that the Court "take such action as the court deems necessary to deter such misconduct and similar schemes in the future."

III. Williams and Scott Counts I and II and Williams Count III: 11 U.S.C. §§ 329(a), 329(b), 526(c)(1) and 105(a)

Section 329 of the Bankruptcy Code provides as follows:

> (a) Any attorney representing a debtor in a case under this title, or in connection with such a case, whether or not such attorney applies for compensation under this title, shall file with the court a statement of the compensation paid or agreed to be paid, if such payment or agreement was made after one year before the date of the filing of the petition, for services rendered or to be rendered in contemplation of or in connection with the case by such attorney, and the source of such compensation.
>
> ***18** (b) If such compensation exceeds the reasonable value of any such services, the court may cancel any such agreement, or order the return of any such payment, to the extent excessive, to—(1) the estate, if the property transferred—(A) would have been property of the estate; or (B) was to be paid by or on behalf of the debtor under a plan under chapter 11, 12, or 13 of this title; or (2) the entity that made such payment.

11 U.S.C. § 329. As stated in *In re Levin*, Case No. 97-15574DWS, 1998 WL 732878 (Bankr. E.D. Pa. Oct. 15, 1998), "[o]ne of the surest means for the bankruptcy system to come under public disrepute is for the perception to take hold that it allows attorneys to milk the last cent out of debtors while leaving creditors nothing. Also disturbing is the prospect that attorneys may be able to extract a premium from debtors who are desperate to file in order to save an asset that is on the brink of being lost. These concerns, among others, have led Congress and the Courts to enact and enforce strict regulations on the payment of attorney's fees in bankruptcy. One of the cornerstones of the regulatory structure is the necessity for attorneys to fully and honestly disclose their transactions with clients." *Levin*, 1998 WL 732878, at *2.

Section 329 reflects the Congressional concern that a debtor's payments to his attorney present a "serious potential for evasion of creditor protection provisions of the bankruptcy laws." H.R.Rep. No. 95–595, at 329 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6285.

> To that end, an attorney must "lay bare all [his] dealings" with the debtor concerning compensation. *In re Saturley,* 131 B.R. 509, 517 (Bankr. D. Me. 1991). The disclosures he makes must be "precise and complete." *Berg,* 356 B.R. at 381 (internal quotation omitted). "Coy or incomplete disclosures" that force the court "to ferret out pertinent information" will not do, *Saturley,* 131 B.R. at 517; *see also Neben & Starrett, Inc. v. Chartwell Fin. Corp. (In re Park–Helena Corp.),* 63 F.3d 877, 881 (9th Cir. 1995), even if they are merely the result of negligence or inadvertence, *Jensen v. U.S. Trustee (In re Smitty's Truck Stop, Inc.),* 210 B.R. 844, 848–49 (10th Cir. BAP 1997). Very simply, "[a]nything less than the full measure of disclosure" is unacceptable. *Saturley,* 131 B.R. at 517.

In re Jackson, 401 B.R. 333, 339–40 (Bankr. N.D. Ill. 2009).

Because disclosure under Section 329(a) and Rule 2016(b) is "central to the integrity of the bankruptcy process," failure to disclose is sanctionable. *In re Andreas,* 373 B.R. 864, 872 (Bankr. N.D. Ill. 2007). The sanctions can include partial or total denial of compensation as well as partial or total disgorgement of fees paid. *Id.* "Many courts, perhaps the majority, punish defective disclosure by denying all compensation." *Id.; see, e.g., Mapother & Mapother, P.S.C. v. Cooper (In re Downs)*, 103 F.3d 472, 477–78 (6th Cir. 1996). However, other courts consider the egregiousness of the conduct and the facts of a given case. *See Charity v. NC FinancialSolutions of Utah, LLC (In re Charity)*, No. 16–31974–KLP, 2017 WL 3580173, at *26 (Bankr. E.D. Va. Aug. 15, 2017).[44]

A. Mootness

***19** The Upright Defendants contend the UST's claims against them in Counts I, II, and III of the Williams Complaint, and Count I and II of the Scott Complaint are moot, because, prior to trial, they refunded to the Williamses and Scott all of the fees paid to LSC/Upright on both the Williamses' and Scott's behalf.[45] In Scott's case, Fenner & Associates sent extra funds on Scott's behalf, and the Upright Defendants advise they are prepared to deliver those additional funds, $100.00, to whomever the Court directs. Because they have already surrendered the funds to the Debtors, the Upright Defendants contend that any relief for disgorgement is moot. *See e.g., In re Bradley*, 495 B.R. 747, 792 (Bankr. S.D. Tex. 2013). The Upright Defendants, in effect, assert there is no case or controversy left for the Court to resolve as to the above referenced Counts, and there is no need to cancel any contracts, because the contracts are fully performed and the debtors have received their discharges. In essence, the Upright Defendants assert there is nothing left for Upright, Delafield, or Morgan to perform in their cases, and cancelling a fully performed contract is basically a useless act.

As stated in *Simmons v. United Mortg. & Loan Inv., LLC*, 634 F.3d 754 (4th Cir. 2011):

> "[T]he doctrine of mootness constitutes a part of the constitutional limits of federal court jurisdiction.... [A] case is moot when the issues presented are no longer 'live' or the parties lack a legally cognizable interest in the outcome." *United States v. Hardy,* 545 F.3d 280, 283 (4th Cir. 2008) (internal quotation marks and citations omitted). *See also Iron Arrow Honor Soc'y v. Heckler,* 464 U.S. 67, 70, 104 S.Ct. 373, 78 L.Ed.2d 58 (1983) ("Federal courts lack jurisdiction to decide moot cases because their constitutional authority extends only to actual cases or controversies."). "Mootness has been described as 'the doctrine of standing set in a time frame: The requisite personal interest that must exist at the commencement of the litigation (standing) must continue throughout its existence (mootness).' " *Arizonans for Official English v. Arizona,* 520 U.S. 43, 68 n. 22, 117 S.Ct. 1055, 137 L.Ed.2d 170 (1997) (quoting *U.S. Parole Comm'n v. Geraghty,* 445 U.S. 388, 397, 100 S.Ct. 1202, 63 L.Ed.2d 479 (1980)).

Id. at 763. The UST contends that the forgoing Counts are not moot, and that there is a live case or controversy.

First, as to Count I of each Complaint, brought under Section 329(a) and 105(a), the UST contends that the Upright Defendants failed to "disclose completely and accurately the compensation paid in this case, in particular both the ultimate source of the compensation and the sharing of compensation between the various entities involved." Williams Complaint, ¶ 84; Scott Complaint, ¶ 83. In both Complaints, the UST asks the Court to use its authority under Section 105(a) to require to LSC, Upright, Delafield and Morgan "to disgorge all fees."[46] This request is made in the body of Count I, whereas the requests for relief at the conclusion of all counts are much broader.

Part of what the UST is targeting in Count I of the Complaints is the allegation that LSC is not a law firm, and that the Rule 2016(b) disclosures are inaccurate and misleading under Section 329(a) and Rule 2016(b). Rule 2016(b) provides, in part, that "[t]he statement shall

include the particulars of any such sharing or agreement to share by the attorney, but the details of any agreement for the sharing of the compensation with a member or regular associate of the attorney's law firm shall not be required." Fed. R. Bankr. P. 2016(b). Count I of the Complaints asserts that the "precise nature of the fee arrangement must be disclosed, not merely the identity of the ultimate owner of the funds," and the Upright Defendants had an obligation to ensure the filing of an accurate statement under Section 329(a) and Rule 2016(b). "Despite this, they failed to disclose completely and accurately the compensation paid in this case, in particular both the ultimate source of the compensation and the sharing of compensation between the various entities involved." Complaints, Count I. Here, after this litigation commenced, the Upright Defendants contend that they paid the Williamses $1,650.00 and Ms. Scott the sum of $1,835.00. Thus, since the UST asks for disgorgement of those funds, the Upright Defendants assert there would be no point in the Court ordering them to do what they have already done, and there is no need to delve into the Rule 2016(b) disclosures.

***20** The Court disagrees. There are approximately 15 additional cases pending in this Court in which the UST has questioned the issue of fee sharing under LSC's business model and the adequacy and manner in which its Rule 2016(b) disclosures are prepared and filed with the Court.[47] In several of those cases, the UST alleges that her Office "has filed several other motions against[, among others,] LSC and Upright Law and alleged a pattern and practice of misrepresentations to the Court regarding the details concerning fees and fee sharing.". *See, e.g.,* Motion to Review Debtor's Transactions with Debt Relief Agencies and Order Disgorgement of Attorney Fees Paid, *In re Holtz*, No. 16–50742 (docket no. 11). In *Knox v. Service Emps. Int'l Union, Local 1000,* 567 U.S. 298, 132 S.Ct. 2277, 183 L.Ed.2d 281 (2012), the Supreme Court held that "[a] case becomes moot only when it is impossible for a court to grant ... any effectual relief whatever to the prevailing party.... [A]s long as the parties have a concrete interest, however small, in the outcome of the litigation, the case is not moot." (citations omitted). *Id.* at 2287. Moreover,

> There is a well-recognized exception to the mootness doctrine holding that "a defendant's voluntary cessation of a challenged practice does not deprive a federal court of its power to determine the legality of the practice." *City of Mesquite v. Aladdin's Castle, Inc.*, 455 U.S. 283, 289, 102 S.Ct. 1070, 71 L.Ed.2d 152 (1982); *see also* *United States v. W.T. Grant Co.*, 345 U.S. 629, 632, 73 S.Ct. 894, 97 L.Ed. 1303 (1953) ("[V]oluntary cessation of allegedly illegal conduct does not deprive the tribunal of power to hear and determine the case, *i.e.*, does not make the case moot.").
>
> The voluntary cessation exception "traces to the principle that a party should not be able to evade judicial review, or to defeat a judgment, by temporarily altering questionable behavior." *City News & Novelty, Inc. v. City of Waukesha*, 531 U.S. 278, 284 n.1, 121 S.Ct. 743, 148 L.Ed.2d 757 (2001). Accordingly, the exception seeks to prevent "a manipulative litigant immunizing itself from suit indefinitely, altering its behavior long enough to secure a dismissal and then reinstating it immediately after." *ACLU of Mass. v. U.S. Conference of Catholic Bishops*, 705 F.3d 44, 54–55 (1st Cir. 2013) (citing *Already, LLC v. Nike, Inc.*, 568 U.S. 85, 133 S.Ct. 721, 727, 184 L.Ed.2d 553 (2013)); *see also* *Knox v. Serv. Emps. Int'l Union, Local 1000*, 567 U.S. 298, 132 S.Ct. 2277, 2287, 183 L.Ed.2d 281 (2012) ("The voluntary cessation of challenged conduct does not ordinarily render a case moot because a dismissal for mootness would permit a resumption of the challenged conduct as soon as the case is dismissed."). To that end, "a defendant claiming that its voluntary compliance moots a case bears the formidable burden of showing that it is absolutely clear the allegedly wrongful behavior could not reasonably be expected to recur." *Laidlaw*, 528 U.S. at 190, 120 S.Ct. 693.

Porter v. Clarke, 852 F.3d 358, 363–64 (4th Cir. 2017).

The Upright Defendants continue to file cases in this Court under the existing business model, and the manner in which the Rule 2016(b) disclosures are prepared and filed is a recurring issue. To say that the Court cannot review their practices because in the two instances currently before the Court they paid the attorney's fees back to the debtors before the Court had a chance to rule on the adequacy of their disclosures would gut the "voluntary cessation" rule as described above. Moreover, in line with *Knox* above, the UST has asked the Court in each Complaint to take such other action as the Court deems necessary to deter such misconduct and similar schemes in the future," and the Court has that discretion under Section 105(a). There remains a "concrete interest ... in the outcome of this litigation," and the Court finds Counts I and II of both Complaints, and Count III of the Williams Complaint, are not moot.[48]

B. LSC as a law firm and the status of Delafield and Morgan as partners

**21* The UST contends that cancellation of the retention agreements and disgorgement of attorney's fees are appropriate in this case against Delafield, Morgan, Upright, and LSC because they each failed to satisfy their disclosure obligations under the Bankruptcy Code and Rules. UST Brief at 39. The UST contends that the Rule 2016 certifications in these cases are inaccurate and misleading.[49] The UST asserts that Rule 2016(b) requires the disclosure of the sharing of compensation between entities while not requiring the disclosure of sharing within a firm. Here, the UST argues that LSC does not fit the definition of a law firm and neither Morgan nor Delafield qualify as a bona fide partner of LSC for purposes of Rule 2016(b). Therefore, LSC's undisclosed sharing of fees with Morgan and Delafield is improper. *Id.* at 41. Bluntly stated, the UST characterizes the collective Upright entities, with Chern, Scanlan, and Allen at LSC's helm, as nothing more than a "boiler room and mere forwarder of legal business," and a "call center employing sales people and hard sell tactics to collect money" from, among others, Virginia residents. *Id.* at 42. The UST argues (1) that LSC is not properly registered with the Virginia State Bar, (2) that it is not organized to deliver legal services to Virginia residents, (3) that it encourages the unauthorized practice of law, (4) that there is an inability to perform meaningful conflicts checks, and (5) that a real law firm would have reasonable oversight procedures. *Id.* at 42–43. Further, the UST contends that Scanlan is a secret owner of the firm, disqualifying it as a law firm.

The UST then argues that even if LSC could be considered a law firm, Morgan, Delafield and Upright Law, LLC, the Virginia entity, are not *bona fide* partners in LSC. Even though Morgan and Delafield testified that they thought they were "partners" in LSC, the UST contends the evidence shows they were not. As examples of this lack of *bona fides*, Morgan and Delafield have no legal access to partnership documents that the law permits them to have, and the partnership agreements expressly provide that they have no right to participate in the management of the firm. The local partners are generally prohibited from collecting money from clients and the agreements attempt to prohibit local partners from soliciting clients upon disassociation from the firm. That the local partners receive no portion of the fees from files that were closed without a case being filed is another factor the UST relies upon. *Id.* at 44.

LSC, in turn, contends that LSC and Upright, with Delafield and Morgan as local partners, are very much a true law firm, both in form and substance. LSC contends that it is sufficient for an attorney to simply be a "member," "partner," or "regular associate," which are all terms Section 101 of the Bankruptcy Code leaves undefined. 11 U.S.C. § 101. Thus, LSC contends courts apply this section in a practical manner, recognizing that different law firms have varying types of structures and varying relationships with their attorneys. LSC contends that Delafield and Morgan have a true partnership relationship with Upright. It enters into partnership agreements with its local partners. They are provided with malpractice insurance. The local partners, albeit while maintaining their separate law practices, hold themselves out to the general public with the title, style and attribute of a "partner," and the partners are supposed to take reasonable steps to advise their clients of their affiliation with Upright. Moreover, Morgan and Delafield share in the firm's revenues and receive a Schedule K–1 to report their Upright-related income, not a W–2 nor a Form 1099.[50] Chern also testified that the local partners participate in partnership meetings with him, and they are invited to an annual partnership meeting in Chicago. They also receive regular newsletters and have direct communication with him to share concerns and to discuss issues with the firm and clients.

**22* In *Futreal*, this Court observed—addressing Prince Law's ill-fated foray into Virginia—that these multi-jurisdictional local partner arrangements "are often nothing more than disguised independent contractor arrangements designed to increase revenue streams by attempting to evade the fee splitting prohibitions in the Bankruptcy Code and Bankruptcy Rules." *Futreal*, 2016 Bankr. Lexis 3974, at *42.[51] Further, in *Banner*, addressing the Volks Anwalt firm and its managing partner Jessica McClean, Judge Beyer observed:

> While Volks Anwalt has "partners" other than McClean, they have no voting rights, own only nominal shares in the firm, and have no authority, control, or input over the operations and management of Volks Anwalt. The only authority that these "partners" may have is with respect to case management of their assigned cases in their localities. McClean controls all matters related to the business of Volks Anwalt, including overseeing all financial, marketing, and human resources activities.

Banner, at *3. The Court in *Banner* also observed that the Volks Anwalt local "partners," in her estimation, "were not legitimate partners" in the firm. *Id.* at *9, n.39.

While the Upright/LSC firm bears many similarities with that of Prince Law and Volks Anwalt, including the observations of Judge Beyer quoted above, it is a much more sophisticated and structured operation, perhaps because it is formed and operated by individuals, albeit self-described, experienced in law firm operations and internet marketing. Without limitation, efforts have been made to register the Virginia entity with the Virginia State Bar, as well as to qualify it to do business in Virginia and elsewhere.[52] The firm shares client information with its local partners through its SalesForce case management software system, such that Chicago and the local offices can work on files together, and the local partners are given significant involvement in the preparation, filing and management of the clients' cases, more so now than when Upright first started. LSC/Upright has a conflicts check system whereby it can run conflicts against its local partners' Upright clients, although it cannot run conflicts checks against those local partners' clients in their separate law practices. For example, neither LSC/Upright nor Morgan can check their client database against Delafield's non-Upright client database. The local partners can check their non-Upright client databases against the larger Upright client database, and based on Chern's testimony, this has not presented a problem in day-to-day operations, since the local partners rarely represent creditors. The Court is deeply disturbed by the lack of effective oversight of its sales people and methods used by LSC/Upright to sell its product, which will be addressed in more detail to follow, as well as the way it provides services and utilizes Virginia lawyers to do so in this District. However, it cannot say LSC is not a law firm.[53]

***23** Under the Virginia Rules of Professional Conduct, "firm," or "law firm" "denotes a professional entity, public or private, organized to deliver legal services, or a legal department of a corporation or other organization." Va. R. Prof'l Conduct, Preamble, Terminology. A comment to Rule 1.10 provides as follows:

> Whether two or more lawyers constitute a firm as defined in the Terminology section can depend on the specific facts. For example, two practitioners who share office space and occasionally consult or assist each other ordinarily would not be regarded as constituting a firm. *However, if they present themselves to the public in a way suggesting that they are a firm or conduct themselves as a firm, they should be regarded as a firm for the purposes of the Rules. The terms of any formal agreement between associated lawyers are relevant in determining whether they are a firm, as is the fact that they have mutual access to information concerning the clients they serve.* Furthermore, it is relevant in doubtful cases to consider the underlying purpose of the Rule that is involved. A group of lawyers could be regarded as a firm for purposes of the Rule that the same lawyer should not represent opposing parties in litigation, while it might not be so regarded for purposes of the Rule that information acquired by one lawyer is attributed to the other.

Va. R. Prof'l Conduct, 1.10 Cmt. [1] (emphasis added).

The Court recognizes that compliance with both Section 329 and Rule 2016(b) are questions of federal, not state, law. But, the comment above is not inconsistent with Federal Rules of Bankruptcy Procedure 9001(6) and (10). Those provisions find that for the purposes of the Bankruptcy Rules, "Firm" includes "a partnership or professional corporation of attorneys or accountants", and "Regular associate" means "any attorney regularly employed by, associated with, or counsel to an individual or firm." Fed. R. Bankr. P. 9001(6), (10). Although raised in a somewhat different context, the Court appreciates Judge Chapman's observation in *In re GSC Grp., Inc.*, 502 B.R. 673 (Bankr. S.D. N.Y. 2013), that:

> [m]uch has changed in the way law firms are organized since the founding of the earliest American firms in New York in the late eighteenth century. The complex, multinational structures of today's law firms would hardly be recognizable to the general partners of these early firms. Law firms today, as well as accounting and financial advisory firms, are comprised of partnerships, limited liability partnerships, professional corporations, limited liability companies—and combinations thereof.... Moreover, the titles and status afforded lawyers who practice in such firms have also evolved, along

> with the perquisites associated therewith; twenty-first century law firms include equity partners, non-equity partners, contract partners, shareholders, associates, contract associates, counsel, of counsel, senior counsel, and the list goes on.... Gone are the days of the professional universe being neatly divided into members and associates—and lawyers and accountants—as contemplated by the Code and the Rules.

Id. at 735, n.227.[54]

***24** Mindful of the above, the Court turns to Delafield's and Morgan's relationship with LSC/Upright. Although styled as "limited partners" with no rights to management of the firm, the Court takes a more holistic approach. Looking to substance over form with regard to the partnership agreements and the record in this case, including the method and manner of Delafield's and Morgan's interactions with LSC in Chicago, the Court is satisfied that both Morgan and Delafield are "regularly associated with" or "counsel to" the "firm," of which the local Virginia LLC in which Delafield and Morgan are limited partners is a component part. Thus, the Rule 2016(b) disclosures are not deficient on the basis that LSC/Upright is not a law firm and that Delafield's and Morgan's relationships with it are impermissible. The Court finds that the statements in the Rule 2016(b) disclosures by Delafield and Morgan that "I have not agreed to share the above-disclosed compensation with any other persons unless they are members and associates of my law firm" are not actionable in these cases. Disgorgement and cancellation of the retention agreements between LSC/Upright, the Williamses, and Scott will not be ordered on that basis.

C. Additional Rule 2016(b) and engagement deficiencies

Chern testified that the Rule 2016(b) disclosures were and still are prepared in Chicago. Chern, Tr. 197, Day 3.[55] The UST argues that from May 12, 2015, when Fenner sent Chern the email outlining the operation of the "New Car Custody Program," LSC knew that Fenner & Associates would be the source of payments for those clients participating in the Sperro Program. Even though Fenner & Associates was controlled by the same person as Sperro, Fenner & Associates actually wrote the checks to LSC/Upright. Nevertheless, when the Rule 2016(b) disclosures were filed for the Williamses and Scott, they failed to disclose that Fenner & Associates paid the fee instead of Sperro. To date, the UST points out no amended Rule 2016(b) disclosure has been filed in either case correcting the actual remitter of the fees.

The UST also complains that the engagement agreements between Upright and the Williamses and Scott contained misrepresentations and were also unclear or inaccurate.[56] Among the UST's contentions are that the engagement agreements misrepresented the local attorneys' true hourly rates. The Williamses' and Scott's retainer agreements appear to be form agreements used in the Western District of Virginia and elsewhere, and the hourly rate substantially exceeds the market rate for such services in this District. It appears the agreements specified rates of $395.00 per hour regardless of the fees the attorney actually charged, although Morgan's time records did specify $395.00 an hour in Scott's case.[57] Further, in violation of Virginia ethics rules, the engagement agreements contained provisions that funds paid were earned when paid.[58] The UST further contends that in Scott's case, the Rule 2016(b) disclosure reflects that Morgan and Upright agreed to accept $1,500.00 for legal services initially, but were paid $1,650.00 and the disclosure did not reflect the $100.00 that Scott paid.

***25** As to the Williamses, the UST contends that a "debt relief agency" is required to give an assisted person an executed written contract within 5 business days of first offering bankruptcy assistance to the assisted person. 11 U.S.C. § 528(a)(1). The written contract is required to explain "clearly and conspicuously—(A) the services such agency will provide to such assisted person; and (B) the fees or charges for such services, and the terms of payment." *Id.* The debt relief agency is also required to give the assisted person a "copy of the fully executed and completed contract." 11 U.S.C. § 528(a)(2). "Any contract for bankruptcy assistance between a debt relief agency and an assisted person that does not comply with the material requirements of this section, section 527, or section 528 shall be void...." 11 U.S.C. § 526(c)(1).[59]

LSC, Upright, Delafield and Morgan stipulated they are "debt relief agencies." Stip. ¶ 10. The Williamses and Scott are "assisted persons" as defined in the Code. LSC/Upright clearly provided "bankruptcy assistance" to the Williamses well before they received the written

contract from Upright.[60] In fact, and without limitation in terms of bankruptcy assistance, it appears their car was picked up on Upright's Sperro referral long before they ever saw a written contract that fell within the scope of Section 528(a).[61] Without addressing each and every UST alleged violation of Section 528(a) as to the Williamses, it is clear from the record that Upright violated Section 528(a) as to the Williamses based on the timing of the delivery of the written agreement. The contract between Upright and the Williamses is declared void pursuant to Count III of the Williams Complaint.

Further placing the Williamses and Ms. Scott into the Sperro Program is a sufficient basis to declare Upright's fee to be unreasonable in both the Williams and Scott cases under Section 329(b). What these individuals have had to endure as a result of the actions of LSC, Chern, Upright, Delafield and Morgan is unconscionable. Section 329(b) provides that the court “may cancel any such agreement, *or* order the return of any such payment to the extent excessive, to—(1) the estate, if the property transferred—(A) would have been property of the estate; or (B) was to be paid by or on behalf of the debtor under chapter 11, 12, or 13 of this title; or (2) the entity that made such payment.” 11 U.S.C. § 329(b) (emphasis added). Here, the Court sees little point in cancelling the agreements between Upright, the Williamses, and Scott. The Williamses' agreement has already been declared void under Section 526(c)(2) for violating Section 528(a). Scott and the Williamses have received their discharges and moved on with their lives. The pendency of these adversary proceedings is what is keeping their cases from being closed.

***26** The Court acknowledges that after this litigation ensued, Upright on its own paid the Williamses and Scott funds received on their behalf—for the most part. Upright is still holding approximately $100.00 in excess funds on Scott's behalf.[62] However, the Court believes that all funds received by Upright in these cases should be remitted back to the debtors' estates. The money Fenner & Associates paid to Upright on behalf of the Williamses and Scott in connection with the Sperro Program would not necessarily have been estate property, because it does not appear that the funds paid were traceable to proceeds of the sale of the debtors' vehicles. The funds were paid to Upright well before the vehicles were sold. Nevertheless, the legal fees were paid to Upright as a *quid pro quo* for the surrender of what would have been estate property, albeit property subject to a lien that the trustee would likely have abandoned (assuming perfection of the lender's security documents). This nexus to what would have been estate property is sufficient for the Court to conclude that the Chapter 7 trustees ought to have the opportunity to consider the disposition of the funds returned by Upright, as small as the dollar amounts may be, and who may be entitled to those funds. That Upright jumped the gun and paid funds to the Williamses and Scott voluntarily after litigation commenced is a loss Upright will have to bear. The Court will grant the UST's requests in both Counts I and II of the Scott and Williams Complaints that the fees received by Upright be delivered to the estates in those cases. The UST's request that fee agreements be cancelled is denied.

IV. Williams Count IV and Scott Count III—Injunction under 11 U.S.C. § 526(c)(5)(A)

In the above referenced Counts, the UST seeks injunctions against LSC, Upright, Delafield, and Morgan to enjoin them “from violating 11 U.S.C. § 526.” Williams, Complaint ¶ 100; Scott, Complaint, ¶ 96. The Court has already found that LSC is a law firm and that the Rule 2016(b) disclosures are not deficient on that basis alone.

The Court is aware of another recent decision, *In re Bishop*, involving Upright and the UST, where some, but not all, of the same issues in this case were raised.[63] *See In re Bishop*, 578 B.R. 158 (Bankr. W.D. N.Y. 2017). In that case, as here, the UST alleged the individual local attorney and the Upright Defendants “have engaged in a clear and consistent pattern of filing false and misleading disclosures of compensation in other Upright Cases.” *Id.* at 166. The UST also sought to have the Court enjoin the defendants “from violating 11 U.S.C. § 526.” *Id.*

The *Bishop* court observed that, while the injunction request tracked the language of 11 U.S.C. § 526(c)(5)(A), “ ‘when Congress authorizes injunctive relief, it implicitly requires that the traditional requirements for an injunction be met in addition to any elements explicitly specified in the statute.’ ” *Id.* at 166 (citing *Klay v. United Healthgroup, Inc.*, 376 F.3d 1092, 1098 (11th Cir. 2004)). The Court went on to observe that an order granting an injunction must meet the specific requirements of Federal Rule of Civil Procedure 65, and as the Second Circuit has noted, “ ‘an injunction must be more specific than a simple command that the defendant obey the law.’ ” *Bishop*, 578 B.R. at 199 (citing *Peregrine Myanmar v. Segal*, 89 F.3d 41, 51 (2d Cir. 1996)).[64] As stated in *Bishop*, an injunction simply to order

the defendants to obey the law and not violate Section 526 would be difficult to police and run afoul of Rule 65. Accordingly, Williams Count IV and Scott Count III will be dismissed.[65]

V. Williams Count VI and Scott Count V—Section 105(a) and the Court's Inherent Authority

*27 "A federal court has an inherent power 'to control admission to its bar and to discipline attorneys who appear before it.' " *Paciocco,* 2015 WL 5178036 (citing *In re Parker,* No. 3:14cv241, 2014 WL 4809844, at *5 (E.D. Va. Sept. 26, 2014) (quoting *Chambers v. NASCO, Inc.,* 501 U.S. 32, 43, 111 S.Ct. 2123, 115 L.Ed.2d 27 (1991))). "This inherent power extends to bankruptcy courts and 'includes the power to suspend or disbar attorneys from practicing before the court.' " *Paciocco,* at *1, (citing *Williams v. Lynch (In re Lewis),* No. 141881, 611 Fed.Appx. 134, 2015 WL 3561277, at *2 (4th Cir. Jun. 9, 2015) (citing *In re Snyder,* 472 U.S. 634, 643, 105 S.Ct. 2874, 86 L.Ed.2d 504 (1985))). Further, Section 105 (a) authorizes a bankruptcy court to "issue any order, process, or judgment that is necessary to carry out the provisions of [the Bankruptcy Code]." 11 U.S.C. § 105(a); *In re Circle T Pipeline*, No. 11-70556, 2011 WL 9688240, at *12 (Bankr. W.D. Va. April 27, 2011). Two years ago, discussing the "national law firm" business model and the use of local, limited partners, this Court made the following observation:

> These cases raise several questions as to who, if anybody, has oversight authority over these arrangements: Is it the state disciplinary authority where the law firm retains local counsel, or is it the authority where the law firm is physically located? If the former, when the ultimate sanction is to take a license, what power does that bar have to discipline attorneys who have no license to begin with? If the latter, does the bar have power to sanction local attorneys for actions that may have occurred in cases conducted in another state? Who has disciplinary and ethical authority over the client's fees and the attorney's trust account when the fees are paid out of state and the local attorney doing the work has no oversight or direct access to them? Do disciplinary authorities in multiple states have the ability to coordinate their efforts?

Futreal, 2016 Bankr. LEXIS 3974, at *41. As this case further demonstrates, the issues are complex, recurring, and multi-jurisdictional. It may well be that the federal courts in which the practices most often arise may be the most able and efficient places to draw lines.

As stated in *In re Burton*, 442 B.R. 421, 467 (Bankr. W.D. N.C. 2009), "[a] court exercises the authority to sanction attorneys with due restraint. When disciplining an attorney, the court must fashion an appropriate sanction without overreaching." (citing *Byrd v. Hopson,* 108 Fed.Appx. 749, 756 (4th Cir. 2004)). Further, *Burton* held that "[c]ourts should impose the minimum sanction necessary to both protect the public and deter future misconduct.... To this effect, courts are inclined to discipline a first offense with a lesser sanction and increase the severity of the discipline for any subsequent infractions, while taking into account previous failed attempts to discipline the attorney." *Burton,* at 467,. In this case, the Sperro/New Car Custody Program was a scam from the start. Despite Chern's protestations to the contrary, the Court believes he was well aware that cars were being towed out of state as early as June 18, 2015, or even earlier. UST Ex. 35–55; UST Ex. 35–37. The only purpose for doing so was to prime the secured lender's lien under more favorable state law towing and garagemen's liens, while running up exorbitant fees, and it benefitted Upright by getting their attorney's fees paid faster. As can be seen by a multitude of exhibits, including the Sales Playbook and scripts, the leadership of Upright constantly had its concerns on cash flow.[66] The fact that this Program was offered or suggested to debtors before they even had the chance to speak to an attorney makes it all the more egregious. Chern testified as follows:

> *28 Remember, we never made participating in the Sperro program a condition of working with Upright Law. In other words, we said to the debtor, "if you are interested in using this program, go ahead. But if you decide you don't want to use the program, that's fine too but you're responsible for the payment of your own legal fees."

Chern, Tr. 106, Day 3. Making this proposal to cash-strapped debtors was essentially offering them a Hobson's choice—one the debtors had to make without legal advice—all while Upright was offering its services under the guise of helping them make the proper decisions to reach their "financial independence." Upright preyed upon some of the most

vulnerable in our society—as the Williamses demonstrated—while they were under great stress. The Williamses were only 20 and 21 years old, with two children, when the Sperro New Car Custody Program was proposed to them. UST Ex. 3–20, pp. 3–4; UST Ex. 3–15, p. 72. Many of the debtors have had to take time off from work to either appear in Court or be deposed in this case, and the anxiety placed upon them permeates both the testimony and written communications. The debtors were left to question if they did anything wrong, as well as the consequences they might face, without proper guidance and assurance.

Of no lesser import is the impact upon an untold number of vehicle creditors.[67] The record reflects that 217 Upright clients participated in the New Car Custody Program nationally, but how many different creditors lost their collateral after being caught up in it is not readily clear, nor is the dollar value of collateral converted or the amount of funds Sperro and/or Fenner & Associates ultimately pocketed. The Court does know that Upright received an amount of not less than $333,545.00 in fees from Fenner/Sperro in payment of legal fees. This is exclusive of filing fees. As shown by the language of the security agreements with the Williamses' and Scott's lenders, hiding and intentionally removing their collateral from Virginia and facilitating the imposition of state law liens against it was contrary to the debtors' contractual obligations to their lenders.[68] There is no credible evidence that Chern or anybody at Upright gave serious thought or concern to this.

***29** Chern's testimony about being intrigued about Fenner's pitch that the New Car Custody Program could be a benefit to Upright's customers, taking the burdens of maintaining and surrendering the collateral off their shoulders, was not credible, nor was his belief that he was really trying to help his clients. Chern, Tr. 278, Day 3. On May 21, 2015, Chern even inquired if there was a way for a consumer to waive the 30–day hold requirement of Indiana law to see if the mechanic's lien could attach sooner. UST Ex. 35–37. Moreover, Chern was also angling for a separate $150.00 fee for his separate “marketing company.” UST Ex. 35–54. As the legal fees and filing fees were running on average between $1,800 to $2,000, Chern, clearly a financially astute businessman, had to know that Fenner and Sperro had to charge more than that to make a profit. Fenner's initial pitch email stated as much.[69] Two former Upright clients, Russell McGuire and Regina White, testified that their cars were sold with Sperro having incurred charges of between $4,500 and $5,000. McGuire, White Tr. 236, 249, Day 1. It was also not credible that Chern could have believed that the New Car Custody Program was some kind of a loss-leader for Fenner, or that Fenner could somehow make his auction services attractive to the vehicle lenders after Fenner towed their collateral hundreds of miles to states where their financing liens could be primed in violation of contractual covenants with their borrowers.[70] Despite red flags of being a “scam,” including one local partner questioning it as such on June 18, 2015,[71] Chern went forward with the rollout on June 18, 2015.[72]

***30** Considering (1) the hard sell tactics encouraged on its sales people, (2) the transcripts of the actual recordings of the calls with clients, (3) the lack of supervision and control over its salespeople in connection with the unauthorized practice of law, due in no small part to the commission and sales structure imposed upon them, (4) the focus on cash flow over professional responsibility, and (5) the participation in the Sperro Program and the record as a whole, including Upright's efforts to get the Williamses and Scott to assert the attorney-client privilege in a thinly-veiled attempt to cover its own tracks, this Court believes that the Upright Defendants have acted in bad faith and the privileges of LSC, Upright Law, Chern, and Allen to file or conduct cases, directly or indirectly, in the Western District of Virginia shall be revoked for a period of five (5) years.[73] This includes any firm that that LSC, Upright Law, Allen, or Chern, directly or indirectly, have an ownership interest in or control over. Further, LSC, Upright, Chern, Allen, Scanlan and Sperro shall be fined collectively the sum of $250,000.00.[74] Chern shall be separately and personally fined the sum of $50,000.00 for his participation in and leadership of the Sperro scheme. Given LSC's financial resources and revenues in particular, as reflected by its tax returns and evidence of receipts from residents of the Western District of Virginia, these sums are appropriate in an effort to deter future misconduct. A lesser sanction would not be more appropriate.[75] These fines are to be paid to the Office of the United States Trustee within thirty (30) days of the Court's Order becoming final and unappealable.

Delafield and Morgan bear responsibility for their actions as well. Delafield did do some things correctly: He met with his clients, he witnessed their signatures on the petition and schedules, and he went over the petition and schedules with them and explained things as an attorney should.[76] However, he also did some things incorrectly, like not acting

appropriately when it appeared he had a conflict of interest when the Sperro Program came to light, and also filing amendments to the petition without obtaining a wet signature, much less getting the clients' permission. Although not under oath, Delafield was an officer of the Court and less than forthcoming at the Williamses' 341 meeting.

At the 341 meeting, Delafield professed ignorance as to why Sperro paid the attorney's fees for the Williamses in their case. Clearly backpedaling, he said, “I don't know” and a “senior attorney at Upright can fill you in on the details. I can't.” UST Ex. 3–2. He knew full well what the Sperro Program was and how it worked.[77] Delafield knew as early as December 2015, as the Williamses had told him, that the car had been used to pay their fees. He also admitted in his Answer to the Complaint that he received the June 18, 2015 email about the New Car Custody Program from Chern.

***31** Delafield fumbled even more fundamental responsibilities. A lawyer with primary responsibility for a client's legal matter is under a duty to know how his client's file is being handled and cannot simply claim ignorance of another's misconduct. *Cf. Banner v. Cohen, Estis and Assoc., LLP* (*In re Balco Equities, Ltd., Inc.*), 345 B.R. 87 (Bankr. S.D. N.Y. 2006) (discussing New York Rules of Professional Responsibility). This was Delafield's case, and he was the responsible attorney before this Court. The actions leading up to its filing, the filing itself, and the conduct of the case fall to him. Moreover, Virginia Rule of Professional Conduct 5.1(c), applicable to attorneys practicing in this Court, provides as follows:

> (c) A lawyer shall be responsible for another lawyer's violation of the Rules of Professional Conduct if: (1) the lawyer orders or, with knowledge of the specific conduct, ratifies the conduct involved; or (2) the lawyer is a partner or has managerial authority in the law firm in which the other lawyer practices, or has direct supervisory authority over the other lawyer, and knows of the conduct at a time when its consequences can be avoided or mitigated but fails to take reasonable remedial action.

Pt. 6, § II, Rule 5.1, Rules of Supreme Ct. of Va.

Here, Delafield ratified participation in the Sperro Program when he took the case and filed it. He was also a partner with knowledge of the conduct in question.[78] He knew about the Sperro Program before he met with the Williamses, and Chern testified that Upright in Chicago prepared the Rule 2016(b) disclosures, which it still does, and sent them to the local partners. The Williamses' Rule 2016(b) disclosure came with the reference to Sperro already on it. Once Delafield saw that, he could have declined to take the case or to file it once the Sperro Program was disclosed to him. Instead, he decided to move forward. That it turned out to be a scam is laid equally at his feet. In addition, Rule 5.3 provides as follows:

> With respect to a nonlawyer employed or retained by or associated with a lawyer: (a) a partner or a lawyer who individually or together with other lawyers possesses managerial authority in a law firm shall make reasonable efforts to ensure that the firm has in effect measures giving reasonable assurance that the person's conduct is compatible with the professional obligations of the lawyer;
>
> (b) a lawyer having direct supervisory authority over the nonlawyer shall make reasonable efforts to ensure that the person's conduct is compatible with the professional obligations of the lawyer; and
>
> (c) a lawyer shall be responsible for conduct of such a person that would be a violation of the Rules of Professional Conduct if engaged in by a lawyer if: (1) the lawyer orders or, with the knowledge of the specific conduct, ratifies the conduct involved; or (2) the lawyer is a partner or has managerial authority in the law firm in which the person is employed, or has direct supervisory authority over the person, and knows or should have known of the conduct at a time when its consequences can be avoided or mitigated but fails to take reasonable remedial action.

Pt. 6, § II, Rule 5.3, Rules of Supreme Ct. of Va.

Delafield, a partner in the firm, also bears equal responsibility for the actions of the Upright sales staff touting and pushing the Sperro Program, as well as their unauthorized practice of law.[79] These are not trifling matters just requiring more sales staff education or training.[80] The “senior client consultants,” as outlined above in Part I(A), engaged in numerous

instances of providing impermissible legal advice to potential clients, albeit alleged violations of Upright's policies, and some of it was just outright wrong, such as advising clients to hide collateral or leave certain debts off their schedules. Coupled with the pressure to hit sales and commission targets, the fact that sales people engaged in overreaching conduct is not surprising. Chern testified that these are isolated instances and not illustrative of Upright's usual practices. However, that the instances of sales personnel exceeding their ethical boundaries just happen to be in the cases before this Court is a coincidence that cannot be ignored.[81] Delafield professed ignorance about much of what the sales people did and how the cases were handled in Chicago. He knew few in firm leadership other than Chern or their roles at Upright. He knew little about how his Upright clients' funds were handled in Chicago.[82] He should have known more about all of these matters. Delafield also has a past disciplinary history with this Court, specifically designed to correct past practice deficiencies in this Court. The Court believes lesser discipline would not be effective. Delafield's privileges to practice in this Court shall be revoked for a period of one (1) year, and Delafield will be sanctioned $5,000.00 to be paid to the Williamses, both to take effect within thirty (30) days of the Court's Order becoming final and unappealable.

***32** Morgan is another matter altogether. Morgan, more so than Delafield, was defiant in his testimony, taking little responsibility for anything. That he relied on his partners or his staff was a frequent Morgan refrain. He, too, bears responsibility for filing a case before this Court in which his client was put into the Sperro Program. He received Chern's Sperro rollout memo and knew Scott was in the program from the start. Morgan, Tr. 47–48, Day 4. Moreover, his actions in trying to advance the attorney-client privilege to shield his actions and that of Upright's were self-serving and in conflict with Scott's interests. The responsibility for Upright actions attributable to the salespeople are as equally applicable to Morgan as to Delafield.

However, one of Morgan's practices, which he had no qualms about, is that he often does not meet with his clients in person, much less meet with them to go over and witness schedules being signed. He often leaves that to his wife, a non-attorney, who he testified has “a superior knowledge of the law” in that area. In this case, the first time he laid eyes on Jessica Scott was at her deposition on June 2, 2017, nearly a year and a half after her case was filed.[83] As Judge Phillips stated in *In re Smith*, “[b]ankruptcy clients rely on their attorneys to explain an unfamiliar and complicated process so that they can make informed, appropriate decisions. *In re Alvarado,* 363 B.R. 484, 487 (Bankr. E.D. Va. 2007). An attorney has an affirmative duty to meet with and counsel his clients, answer any questions the client may have and explain the legal significance of their actions.” *In re Smith*, No. 13-31565-KLP, 2014 WL 128385, at *6 (Bankr. E.D. Va. Jan. 14, 2014). Judge Kenney in the Eastern District of Virginia echoed the same sentiment, advising that “despite these advances in technology that allow parties to communicate remotely and to file papers electronically with the Court, there is still a fundamental duty to meet with the client and to obtain the client's original signature on the petition. The filing of a bankruptcy petition is an important, life-altering decision. The client must consider the risks (the damage to one's credit, the transactional fees, and the possibility of a failed Chapter 13 plan after paying into the plan for some period of time) with the potential rewards (the automatic stay, a discharge and the possibility of a strip-off of wholly unsecured liens).” *In re Tran*, No. 14-11837-BFK, 2014 WL 5421575, at *7 (Bankr. E.D. Va. Oct. 17, 2014). Leaving it to a lay person to meet with the client, go over the petition and schedules, verify their accuracy, explain the ramifications, answer questions, and obtain the signature is beyond the pale in this Court.[84]

***33** This is unacceptable practice, and this practice shall stop. The Court also notes Morgan has a past disciplinary record with the Virginia State Bar more severe than that of Delafield, and it believes that lesser discipline would not be effective. Morgan's privileges to appear before this Court, directly or indirectly, including through his PLLC, shall be revoked for eighteen (18) months, and Morgan will be sanctioned $5,000.00 to be paid to Jessica Scott, both to take effect within thirty (30) days of the Court's Order becoming final and unappealable.[85]

Sperro, LLC is in default. Sperro is directed to disgorge immediately all funds received from (1) the sale or disposition of any property for which it remitted funds to LSC/Upright in connection with a case filed in this Court, and (2) any funds paid to it by or on behalf of a lender to recover that lender's collateral in connection with a case before this Court. Sperro shall provide full documentation to the UST of all such transactions. All such funds shall be paid to the Clerk of this Court, to be held in the Clerk's registry pending further order of this Court. Sperro shall also, to the extent it has not already done so, provide to the Office of the

United States Trustee a list of all clients referred to it from LSC/Upright nationally, as well as details pertaining to the recovery, sale, disposition and/or secured creditor redemption of any collateral in connection with the so-called New Car Custody Program.[86]

CONCLUSION

Bankruptcy courts have long recognized that Congress sought to enact certain provisions of the Bankruptcy Code so that lawyers would preserve the integrity of the bankruptcy process and not treat bankruptcy matters as "matters of traffic." *See In re Worldwide Direct*, 316 B.R. at 646 and cases cited therein (addressing Section 504 of the Bankruptcy Code). The Bankruptcy Code provisions and Rules in play here are part of a larger structure, all of which operate in their own way to support those same goals. The integrity of the bankruptcy process was a distant thought in these cases. The pursuit of the next dollar of compensation was the primary consideration here, by Sperro, LSC/Upright, its organizers, and its local partners.

Local attorneys joining multi-jurisdictional law firms as local or limited partners cannot be both tall and short. An attorney cannot claim to be a partner in the firm and file cases with the Court as lead counsel, but yet claim no responsibility for what happens in the main office on the files the attorney decides to take. Attorneys considering joining firms with this business model should understand that, in this Court, while an injury might be initiated elsewhere—there is a real possibility the pain is going to be felt at home.[87] An appropriate Order shall issue.

All Citations

Slip Copy, 2018 WL 832894

Footnotes

1 Where appropriate, findings of fact shall be construed as conclusions of law and conclusions of law shall be construed as findings of fact. *See* Fed. R. Bankr. P. 7052; 9014(c).

2 Leibowitz has a less than 1% interest in LSC. He is also a Chapter 7 panel trustee in the Northern District of Illinois. UST Ex. 25, pp. 30, 45.

3 References to the trial transcript are described as "Tr." and by day of testimony.

4 LSC pays Mighty Legal a factor of 1.1 times the actual payroll cost to Mighty Legal for its leased employees.

5 Justiva trademarked "Upright Law" and LSC pays licensing fees to Royce Marketing, as well as fees for the use of the domain name www.uprightlaw.com which Justiva also owns. UST Ex. 30, Scanlan Dep. Tr. at 15; Joint Stipulations of Fact ("Stip.") ¶ 12.

6 Allen testified by deposition that neither he, Chern, nor Scanlan took salaries from Mighty Legal or Royce Marketing. UST Ex. 26, Allen Dep. Tr. 36–38.

7 In 2017, Upright eliminated the title client consultant. All client consultants became "senior client consultants." Chern, Tr. 6, Day 4.

8 The word "close" is used 28 times in this 13–page document. Chern testified the Playbook was written by Allen, and that the versions of the Playbook were later revised from time to time. A number of these or similar sales techniques found their way into "Upright University" training materials. *See, e.g.*, Chern, Tr. 13–14, Day 4; UST Ex. 36.

9 Upright Exhibit J7 is an information tutorial with a quiz at the end for training purposes.

10 The UST, based in part on testimony from Chern, describes Upright as a "boiler room" operation. UST Brief, at 4–8; Chern, Tr. 33, Day 4. Upright vigorously disputes that characterization.

11 Upright's current system of live call monitors now listen for instances that might constitute the unauthorized practice of law. Violations are reported to the office of general counsel. Upright has a progressive discipline system that leads to

additional training and ultimately to a “three strikes” and “out” policy. Chern, Tr. 173–76, Day 3.

12 Because Brandon Fox's testimony was presented by deposition, the Court had little opportunity to weigh his credibility, but when asked if instructing debtors they could leave debts off their schedules was part of his training, he said “From what I recall, yes.” UST Ex. 21, Tr. pp. 46, 59. Kevin Chern denied that. Tr. 179, Day 3. The simple fact is Fox did give this advice to Jessica Scott.

13 This suggestion was made in connection with the “New Car Custody Program,” discussed *infra.*

14 Chern, Tr. 169–70, Day 3.

15 Conflicts checks are done at the local attorney level, and Chern testified that the local attorneys check for client conflicts among their own client databases. No conflicts check is run by local attorneys against other local attorney's non-Upright clients. Thus, if a local attorney has his own practice and also works for Upright, no other Upright attorney can check for conflicts against that attorney's private client database. Delafield, Tr. 195–96, 206–07, Day 2. Chern contends that, practically, this is not a problem, since their local partner attorneys “generally speaking” do not represent creditors. Chern, Tr. 165–66, Day 3. The “onboarding associate,” an employee in Chicago, runs conflicts checks against Upright's master database. Chern, Tr. 166–67, Day 3.

16 The attorney is supposed to key the completion of this call into a quality control program. Chern, Tr. 139–40, Day 3.

17 Presumably, this was also when a conflicts check was run by the local attorney.

18 The prior system, with the petition being prepared in Chicago, was clearly susceptible to errors, as one petition was filed by Delafield as a member of Law Solutions Chicago, LLC d/b/a Jason Allen Law LLC, not Upright. UST Ex. 20. According to Delafield, all he could see prior to the petition being filed was the space for his name. He could not see how the field below that was populated, yet it was still filed on his behalf under his CM/ECF password.

19 Chern's testimony rings hollow and is contradicted by his December 3, 2014 email to Delafield. UST Ex. 45. Under “[r]equirements of becoming a partner” Chern advised Upright was looking for attorneys with at least five years' experience in both Chapter 7 and 13. Moreover, Upright's alleged vetting of its local partners appears to have been minimal, if not non-existent. The email advises that the “requirements” include a “clean disciplinary record.” In this case, it appears that meant nothing more than a certificate of good standing from the Virginia State Bar. Morgan and Delafield both had disciplinary histories with the Virginia State Bar before joining forces with Upright, and Delafield has received prior instruction from this Court on the proper performance of his duties due to failures to meet his expectations before the Court. UST Ex. 63. Morgan is also a convicted felon who was once suspended by the Bar. Chern testified that these matters were known to Upright. UST Ex. 28, pp. 13–14.

20 The VSB registration is on a form for a professional limited liability company. The registration form discloses the Virginia members and managers of Upright Virginia as “John Morgan, Edrie Pfeiffer, and Darren Deerfield [sic].” Delafield's name is misspelled each time it appears. UST Ex. 57. Chern testified that Upright Virginia was formed after consulting with Bernard DiMuro, LSC's Virginia ethics counsel. Further muddying the organizational waters, Chern testified that: “After Mr. DiMuro did his research, he could not provide with a degree of certainty a definitive opinion to us as to what was required. In other words, his feeling was that Virginia state law was somewhat ambiguous as to whether or not a foreign LLC could register to practice law in Virginia. As a result of that, out of an abundance of caution, we thought it was prudent to go ahead and set up a Virginia professional limited liability company called Upright Law, LLC, which is a d/b/a for Upright Law, PLLC.” Tr. 64–65, Day 3. As previously shown, Upright Law, LLC, an Illinois limited liability company, is a d/b/a of LSC. Upright Law, PLLC does not appear in LSC's 2016 federal tax

return as a company owned or controlled by LSC. Despite their separate existences, the separate Upright entities are practically referred to and treated by the Chicago managers as a single entity.

21 LSC pays agency fees to Mighty Legal for use of the Best Case software.

22 The Court takes judicial notice of the length of the suspension in the Bar's order of suspension. http://www.vsb.org/disciplinary_orders/morgan_opinion.html.

23 Chern followed up with an email dated January 15, 2014. UST Ex. 41. The email provided, in part, that "[a]s a partner of the firm you will receive the following compensation: 1. Chapter 7—8% of the gross fee for the retention, plus 17% of the gross fee for filing the case under the ECF you obtain for Firm filings and for attending the 341 meeting and making sure the debtor's case is completed. 2. Chapter 13—10% of the gross fee for the retention, plus 30% of the gross fee for filing the case under the ECF you obtain for Firm filings and for attending the 341 meeting and making sure the debtor's case is confirmed, plus 40% of any supplemental fees attributable to post-confirmation work. 3. Pro rata share of a pool of 10% of any revenue generated from ancillary services including litigation on FDCPA and FCRA matters the firm generates. 4. 1% pro rata non-voting profit share with other state members of all law firm business transacted in the state." *Id.*

24 As the UST points out, Upright was not qualified to do business in Virginia or registered with the Virginia State Bar at this time.

25 Upright Ex. P5 is LSC's 2016 Federal Tax Return, which is currently under seal. Redacted versions of the K–1's of Morgan and Delafield will be unsealed. The remainder of the return will remain under seal, absent further order of the Court. While the Court sees no need to disclose the total gross revenues of LSC as reflected on the return, they are substantial. The Court further notes that through June 30, 2017, Upright had filed 190 cases in the Western District of Virginia, and it had received payments from 757 people (joint representation of spouses is treated as one person). Total fees paid to Upright, including filing fees, were $821,156.52 in this district. Total fees paid in cases actually filed equaled $409,650.22, including filing fees, all through June 30, 2017. UST Ex. 1, p. 5.

26 The January 2015 Chern email also reflected the change in compensation from 2014, providing that the new compensation structure was as follows: "1. Chapter 7—25% of the gross fee. 2. Chapter 13—40% of the gross 'no look' fee, plus 40% of any supplemental fees attributable to post-confirmation work. 3. Pro rata share of a pool of 10% of any revenue generated from ancillary services including litigation on FDCPA and FCRA matters the firm generates. 4. 1% pro rata non-voting profit share with other state members of all law firm business transacted in the state." UST Ex. 45.

27 From October 24, 2014 to September 30, 2015, Delafield was affiliated with another high volume consumer bankruptcy law firm, known generally as "Prince Law," that was based in Florida, advertised over the internet, and referred prospects to a local "member" for filing. Prince Law and a different local member were held in civil contempt and barred from filing cases in this Court after the Court found they engaged in a variety of ethical and rule violations. *See In re Futreal*, No. 15-70886, 2016 WL 2609644 (Bankr. W.D. Va. May 5, 2016), and *In re Futreal,* 2016 Bankr. LEXIS 3974. Curiously, the Court recognizes Edrie Pfeiffer, footnote 20, as another Virginia based Prince Law alumni now affiliated with Upright.

28 Before Fenner made his pitch, Chern testified he had heard of a "vehicle recovery program" being run by an attorney named Max Gardiner while attending a "bankruptcy boot camp" run by Gardiner in North Carolina. Chern testified that through Gardiner's boot camp, he also met other lawyers who had vehicle recovery programs. Chern testified he thought, "hey, there are other lawyers who are doing this legitimately in other parts of the country. This is something that I should seriously consider." Chern, Tr. 81–82, Day 3. Chern acknowledged that the Sperro Program was unlike the Gardiner program, in

that Gardiner did not tow cars out of state and he gave lenders a date in the future after which charges would start to accrue if the vehicle was not picked up. Chern, Tr. 15–16, Day 4.

29 The June 18, 2015 email stated, under “Due Diligence,” that “Kevin Chern reviewed the program in detail with Felicia Burda, our UST Counsel, Mary Robinson, or [sic] Professional Responsibility Counsel, and David Leibowitz, General Counsel of UpRight Law and Head of Litigation.” UST Ex. 35–53. Chern testified Ms. Burda was a former attorne9 with the U.S. Trustee's Office, and that Ms. Robinson was a former disciplinary attorney with the State of Illinois. Chern, Tr. 76–77, Day 3.

30 Steinberg's response was, in part, “I guess it just seems like it is cheating the unsecured [sic] creditor. And I need to add that it pains me to type that sentence because I have a general disdain for most of my clients' creditors. But you have clearly presented the scenerio [sic] to people who are well positioned to give a recommendation, so I am not going to object.” *Id.*

31 Regina White, a former Upright client, who was ultimately represented by Delafield outside of the Upright relationship, participated in the Sperro Program before being dropped by Upright as a client. White testified that she “kept asking them are you sure this is legitimate because I don't want to go to jail.... But you know, they assured me it was legal and legitimate and I trusted them to know what they were talking about.” White, Tr. 241–42, Day 1.

32 It is unclear to the Court who “our” is in this email, but it appears to be one of the entities Chern and Scanlan own together, as opposed to LSC/Upright. It is also not clear whether these funds were ever paid, but the effort was clearly made by Chern to squeeze what he could out of the Sperro Program.

33 Mrs. Williams' legal name is “Andrian,” not “Adrian,” which caused some confusion in the proper filing of her petition.

34 Both Mr. and Mrs. Williams testified at trial, and both were earnest, forthcoming, and credible witnesses. They were, unfortunately, caught in the crossfire between the UST and Upright through no demonstrable fault of their own.

35 Upright sought an immediate credit card payment to confirm the representation. UST Ex. 3–1, Tr. pp. 33, 47–48.

36 This was not a one-time event. On September 15, 2015, Upright sent a virtually identical letter, this one to “Ally,” regarding a Delafield client named Shannon Chapman. UST Ex. 64. A template document was admitted by which Upright could plug in any local partner's name. UST Ex. 35–29.

37 Chern's explanation as to the letters sent out over Delafield's name without his knowledge or permission referenced back to the June 18, 2015 roll out email for the Sperro Program. “So, I believed, at the time, that my June 18th memo to my partners notified the [sic] that we were going to be sending a letter out to the finance companies notifying them that Sperro was in custody of the vehicle, notifying them to pick up the vehicle, you know, quickly to avoid excessive charges, etcetera. It didn't have Mr. Delafield's signature on it. It has his name on it as the attorney who was going to be representing the debtor throughout Upright Law. I regret that I didn't do a better job of communicating to the partners that their names would be placed on those letters. That was a mistake on my part.” Chern, Tr. 110–11, Day 3.

38 On March 14, 2016, Chern emailed Delafield and advised “Please set up a time for the client to be prepped by you and me in advance of the hearing and advise him not to talk to anyone until then about the circumstances surrounding the placement of the car with Sperro.” UST Ex. 3–18.

39 Morgan's deposition testimony was frank: “Q. Who sat down physically and reviewed these petition and schedules with Jessica Scott? A: [Morgan] My wife, Rhonda. Q. So, you did not review the petition and schedules with the debtor, correct? A. [Morgan]: Not with the debtor, correct.” UST Ex. 24, Tr. pp. 49–50.

40 As a witness, the Court found Morgan to be defiant, unremorseful and wholly lacking in credibility. When questioned by the Court why Morgan and his associate attorney allow his wife to go over petitions and schedules with consumer debtors, and also obtain their signatures, Morgan testified: "Between the three of us, I would say that my wife has a superior knowledge of the law and the conduct of the signing and the elements of the bankruptcy petition. We often ask for her advice." Morgan, Tr. 66, Day 4.

41 The address to which this letter was mailed, if it was mailed, is unclear. Brian Fenner was never deposed in connection with this litigation. What the car actually sold for, when, and to whom are unknown.

42 Menditto attempted to appear *pro hac vice* on behalf of the Williamses and Scott at the May 9, 2017 hearing on the UST's motion to compel. The UST objected, and the Court sustained that objection. At the hearing on May 9, 2017, counsel for the Upright Defendants stated "... Mr. Menditto was brought in to assist in responding to the subpoenas ...." May 9, 2017 Tr. at p. 28. However, when pressed by the Court, counsel could not say who brought him in.

43 At trial, Delafield denied the comments attributed to him.

44 "...[T]he Bankruptcy Code and Rules impose no requirement on debtor's counsel in a chapter 7 case to obtain court *approval* of his or her fees.... Rather, the duty is simply one of *disclosure*, with the court having the power to disapprove fees to the extent they are determined to be excessive *if* the reasonableness of the fees is raised either by the debtor or the United States Trustee, or by the court on its own motion. *See Burd v. Walters (In re Walters),* 868 F.2d 665 (4th Cir. 1989) (bankruptcy court had power to reduce fees of attorney hired by debtor to litigate against creditor in another forum from $29,000 to $15,000 even though the fees were being paid from exempt funds rather than estate assets)." *In re Hooper,* No. 93-11599-AB, 2001 WL 34054526, at *9 (Bankr. E.D. Va. Oct. 29, 2001).

45 The Court denied a motion to dismiss to that effect shortly before trial. Docket Nos. 162, 173, 189.

46 In the Williams Complaint, the UST also asked that the Defendants be required to provide "restitution of the full value of the converted property," but this request was withdrawn prior to trial at the hearing on the motion to dismiss.

47 The Court takes judicial notice of its own docket. The additional cases are set for a status conference on March 19, 2018.

48 As to Count II of the Complaints, the additional question arises as to whom should the funds should be disgorged? Section 329(b) provides that the court may order the return of any such payment to "(1) the estate, if the property transferred—(A) would have been property of the estate; or (B) was to be paid by or on behalf of the debtor under a plan under chapter 11, 12, or 13 of this title; or (2) the entity that made such payment." 11 U.S.C. § 329(b). This is an open question for the Court, not the Upright Defendants, to decide.

49 Fed. R. Bankr. P. 2016(b) provides as follows: "... (b) Disclosure of Compensation Paid or Promised to Attorney for Debtor. Every attorney for a debtor, whether or not the attorney applies for compensation, shall file and transmit to the United States trustee within 14 days after the order for relief, or at another time as the court may direct, the statement required by § 329 of the Code including whether the attorney has shared or agreed to share the compensation with any other entity. The statement shall include the particulars of any such sharing or agreement to share by the attorney, but the details of any agreement for the sharing of the compensation with a member or regular associate of the attorney's law firm shall not be required. A supplemental statement shall be filed and transmitted to the United States trustee within 14 days after any payment or agreement not previously disclosed."

50 In 2016, LSC filed a composite tax return in Virginia, and the record reflects the Schedule K–1's received by Morgan and Delafield were from LSC, not

Upright Law, LLC, a Virginia limited liability company. Upright Ex. P5, p. 39. No Schedule K–1 was provided from the Virginia entity, which is the entity with which Morgan and Delafield had partnership agreements.

51 Another "multi-jurisdictional" firm using a local attorney arrangement, Volks Anwalt, was barred from practicing in the Western District of Virginia under an agreement with the UST for a period of three years. *In re Glover*, No. 15 –61476 (Bankr. W.D. Va. Dec. 15, 2015). Volks Anwalt was also sanctioned by the Western District of North Carolina and disbarred from that court for a period of five years. *In re Banner*, No. 15-31761, 2016 WL 3251886 (Bankr. W.D. N.C. June 2, 2016). The firm was also sanctioned in Hawaii, as was its local counsel. *In re Hanawahine*, 577 B.R. 573 (Bankr. D. Hawaii 2017) (disciplining Volks Anwalt and its local partner for abandoning client).

52 The Court acknowledges that, for a period of time, Upright was providing legal services in Virginia and in this Court without being properly qualified to do so. The Court further understands and appreciates the UST's position that the registration was both improperly prepared and untimely filed, and that the registration on file is for Upright Law, the Virginia entity, and not LSC. The Virginia State Bar has taken no action against any of the collective Upright entities for their registration deficiencies. Chern, Tr. 206, Day 3. At this point, the Court will leave the consequences of those deficiencies, if any, to the proper State authorities.

53 Scanlan's role in LSC is concerning to the Court as well. It is clear to the Court from the undercurrents at trial that while Scanlan is not one of the technical, legal owners of LSC, his hand is never far from the wheel. Moreover, the federal tax return admitted as Upright Ex. P5 reflects substantial portions of LSC's legal services revenues are channeled to both Royce Marketing and Mighty Legal for marketing and employee leasing services, which flow down to Justiva and ultimately to Scanlan.

54 The Court wrestled with this conclusion, especially given the admonition against treating bankruptcy cases as a "matter of traffic." *See In re Worldwide Direct, Inc.*, 316 B.R. 637, 646 (D. Del. 2004).

55 Delafield at one point testified he prepared the Williamses' 2016(b) disclosure. That does not appear to have been the case. UST Ex. 23, Tr. p. 208.

56 For example, the Williamses' engagement agreement indicated amendments to schedules were included in the flat fee, while in another portion of the same agreement, those services were excluded. UST Ex. 3–24, ¶¶ 8(f), 9(h).

57 Delafield's true local rate on the Williamses' file appears to have been $200.00 per hour. UST Ex. 3–23. In Scott's case, every attorney involved appears to have billed $395.00 per hour, regardless of whether they were an associate or partner. The veracity of Upright's time records for Scott's case are questionable to the Court. See pp. 27–28, *supra.*

58 It appears that from 2014 through March 2016, attorney's fees were placed directly into LSC's Illinois general operating account or LSC's Virginia operating account. In response to an Interrogatory, LSC stated, in part, as follows: "LSC states the following that it is currently in compliance with Virginia's IOLTA rules. However, LSC and Upright initially misinterpreted the Virginia IOLTA Rules and found out this was the case in March 2016. At that time, they immediately began depositing all new Virginia client funds into its Virginia, IOLTA account and began an audit of payments received and earned from its Virginia clients. After completion of the audit and determining the proper amounts that should be in (and or replenished into) the Virginia IOLTA account, the IOLTA account was properly replenished. This process was completed in October 2016...." UST Ex. 2, p. 4.

59 These are but a fraction of the UST's complaints about Upright's engagement agreements and retention procedures in these cases. *Cf. Lyda v. City of Detroit (In re City of Detroit)*, No. 13-53846, 2014 WL 6474081, at *7 (Bankr. E.D. Mich. Nov. 19, 2014) ("These allegations have an 'everything but the kitchen sink' quality that makes them challenging to parse through."). In the

future, the Court trusts the UST will take a more focused approach on such matters.

60 "The term 'bankruptcy assistance' means any goods or services sold or otherwise provided to an assisted person with the express or implied purpose of providing information, advice, counsel, document preparation, or filing, or attendance at a creditors' meeting or appearing in a case or proceeding on behalf of another or providing legal representation with respect to a case or proceeding under this title." 11 U.S.C. § 101(4A).

61 UST Ex. 3–5, p. 6 reflects the written retainer agreement was "completed" for the Williamses on September 30, 2015. The agreement was signed October 16, 2015. UST Ex. 3–24. No fully executed contract signed by Upright or Delafield was introduced. The Williamses' first contact with Upright at which time "bankruptcy assistance" was provided was on August 27, 2015.

62 It appears that Upright received $1,750.00 in attorney's fees on Scott's case. Apart from filing fees, Upright received $1,650.00 from Fenner & Associates for the Sperro Program, and $100.00 from Scott. Upright refunded Scott $100.00 on her debit card on June 8, 2016, then it sent her an additional $1,550.00 on July 28, 2016. UST Ex. 4–14.

63 Neither the New Car Custody Program, Sperro, nor Fenner & Associates appeared to be implicated in *Bishop*.

64 The Fourth Circuit acknowledged this argument in *U.S. S.E.C. v. Pirate Inv'r LLC*, 580 F.3d 233, 255 (4th Cir. 2009), observing that "Federal Rule of Civil Procedure 65(d) requires that injunctions 'describe in reasonable detail ... the act or acts restrained or required,' and several circuits have relied on Rule 65 (d) to require that injunctions do more than instruct a defendant to 'obey the law.' *See, e.g., Burton v. City of Belle Glade,* 178 F.3d 1175, 1201 (11th Cir. 1999); *Payne v. Travenol Labs., Inc.,* 565 F.2d 895, 897–98 (5th Cir.1978)." The Fourth Circuit did not take up this issue, however, as it was raised for the first time on appeal.

65 The UST should know that this Court also agrees with the caution in *Bishop* about the use of "shotgun" pleadings. In *Bishop*, Judge Warren referred to *Weiland v. Palm Beach Cnty. Sheriff's Office*, 792 F.3d 1313, 1318–26 (11th Cir. 2015), which categorized the 4 types of shotgun pleadings. "[T]he most common type—by a long shot—is a complaint containing multiple counts where each count adopts the allegations of all preceding counts, causing each successive count to carry all that came before and the last count to be a combination of the entire complaint)." *Bishop*, 578 B.R. at 167–68. The Complaints in this case suffer from a virtually identical affliction.

66 Chern testified in part that, with regard to Upright's usage of the Playbook and its aggressive sales techniques, "... we train our client consultants to compete against other lawyers for the representation of the clients. Why they should use our services verses another attorney's services." Chern Tr. 12–13, Day 4. Further, these techniques are to "motivate a consumer to take an action to actually start advancing their own best interest which sometimes they just don't act in the best self-interest." *Id.* at 14. The Court found Chern's overall emphasis on sales and profit to be far more credible than his goals of helping consumers execute on decisions they had already made in their own minds.

67 Chern testified that he felt remorse for the Sperro Program, that it was a "horrible" mistake, and that he felt "horrible" that he put his partners and their professional reputations at risk, acknowledging that there were "red flags that I should have given more credence to." Chern, Tr. 119–120, 278, Day 3.

68 In Virginia, it may also be a crime. Va. Code § 18.2–115 provides, in part, as follows: "Whenever any person is in possession of any personal property, including motor vehicles or farm products, in any capacity, the title or ownership of which he has agreed in writing shall be or remain in another, or on which he has given a lien, and such person so in possession shall fraudulently sell, pledge, pawn or remove such property from the premises where it has been agreed that it shall remain, and refuse to disclose the location thereof, or otherwise dispose of the property or fraudulently remove

the same from the Commonwealth, without the written consent of the owner or lienor or the person in whom the title is, or, if such writing be a deed of trust, without the written consent of the trustee or beneficiary in such deed of trust, he shall be deemed guilty of the larceny thereof."

69 See quoted language in UST Ex. 35–18, *supra* p. 18.

70 This point is borne out by a recent opinion of the Indiana Court Appeals, after Sperro was sued by Ford Motor Credit Company over the "Sperro Plan." In *Sperro LLC v. Ford Motor Credit Co., LLC*, 64 N.E.3d 235 (Ind. App. 2016), the Court observed that "[u]nder the Sperro Plan, Sperro established contacts with numerous consumer bankruptcy attorneys throughout the United States, who would notify Sperro when a prospective bankruptcy client had a financed vehicle that he or she could no longer afford to make the payments on. Although such vehicles would normally be voluntarily surrendered to the secured creditor, Sperro would offer to pay the client's bankruptcy legal fees in exchange for the client's agreement to have the vehicle towed to Indiana and stored pursuant to a Transporting and Storage Authorization Agreement ('TSAA')." *Id.* at 239–240. Further, "Sperro transported the Vehicles from New Mexico, California, Louisiana, and Arizona to its Storage Yards in Indianapolis." *Id.* The Indiana Court of Appeals upheld, among other things, a trial court injunction finding in that "Sperro's business was to transport and store collateral, and therefore Fenner had to know that all the vehicles surrendered to Sperro pursuant to the TSSA's have been financed and are subject to the liens. Fenner's business experience supports the trial court's conclusions that he had or should have had general knowledge that the Borrowers purchased the Vehicles pursuant to retail installment contracts and the provisions generally included therein. Accordingly, the trial court did not err in concluding that Sperro and Fenner intentionally induced the breach of the Installment Contracts between the Borrowers and FMCC or proceeded with reckless disregard of the contractual relationship between the Borrowers and FMCC. Therefore, we affirm the trial court in all respects." *Id.* at 250.

71 In a June 8, 2015 email from Allen to Chern, Allen stated: "It might be time to send an email to the partners about the program. We just had a client who surrendered his car, then talked to the partner for the compliance call, where the partner attorney told our client it sounded like a scam. Then of course the client calls in freaking out." UST Ex. 35–47.

72 Chern testified that he tried to send notices to secured lenders earlier than Fenner wanted, but in the Williams case, that was sent to the wrong creditor at the wrong address. That was effectively no notice at all, as GCB's attorney showed up at the Williamses' 341 meeting to inquire as to the status of the car. Moreover, by the time the notices in the record were sent, the vehicles were well on their way to, if not already in, Indiana at $1.50 a mile, plus a $75 loading fee, and $45 per day storage. UST Ex. 35–53. The distance from the Williamses' residence in Saltville, Virginia to the Sperro lot in Indiana is approximately 420 miles one way per Google driving directions.

73 The Court uses the word "revoked" instead of "suspended" for a reason. Any person or entity whose privileges are revoked by this Court's Order will have to reapply for privileges to practice at the end of the revocation period, at which time the Court will consider their application as well as their compliance with this Opinion and the Order of revocation. Readmission will not be automatic.

74 UST Ex. 35–33 is a direct reach out from Scanlan to Fenner in connection with the Sperro Program, and the Court believes that Scanlan was well aware of the Sperro Program. Further, as LSC's internet marketing expert, his fingerprints appear to be all over the hard sell tactics used by LSC/Upright. Scanlan, Tr. 102–103, Day 4. In harmony with *Bishop*, whether the structure of LSC/Upright and Scanlan's role in it pass muster under Illinois law is a question the Court will leave to appropriate Illinois authorities.

75 In 2016, LSC paid over 68% of its substantial gross revenues to Royce Marketing (Advertising) and Mighty Legal (Leased Payroll), captive companies of Justiva, for which it took deductions on Schedule 4 of its federal tax return. Upright Ex. P5; Scanlan, Tr. 114–16, Day 4. The Court also considered

Chern's testimony that through trial LSC has refunded approximately $100,000.00 in legal fees earned from Sperro and incurred over $1,000,000.00 in legal expenses related to its involvement in the Sperro Program. Chern, Tr. 275, Day 3. Even considering that testimony, the Court believes its sanction to be appropriate. Chern, Tr. 275–76, Day 3. LSC is well able to handle this payment.

76 The Court has no qualms about Delafield meeting with clients or witnessing signatures over Skype. This district is approximately 400 miles long from Winchester to the Cumberland Gap. Appropriate accommodations can be made with the proper use of technology. However, simple telephone calls are unacceptable.

77 Delafield's December 11, 2015 time entry stated, “Darren called Chicago and asked for additional information regarding Sperro.” UST Ex. 3–23, p. 4.

78 The Court has considered both Delafield's and Morgan's experience before this Court, as well as their roles as primary counsel in the cases before the Court. This is not the circumstance of a junior attorney early in his career inheriting a matter brought in by a senior partner. *Cf. Blue v. U.S. Dep't of Army*, 914 F.2d 525 (4th Cir. 1990).

79 “Any lawyer who aids a non-lawyer in the unauthorized practice of law is subject to discipline and disbarment. A lawyer has an affirmative duty to report unprivileged knowledge of such misconduct by another lawyer to the appropriate District Committee, and to discontinue his representation of a client when he discovers that his employment furthers the unauthorized practice of law by the client.” Pt. 6, § I, Rules of Supreme Ct. of Va.

80 According to the Rules of the Supreme Court of Virginia, no non-lawyer shall engage in the practice of law in Virginia. The Rules define the practice of law as follows:

> (B) *Definition of the Practice of Law.*—...
>
> Generally, the relation of attorney and client exists, and one is deemed to be practicing law whenever he furnishes to another advice or service under circumstances which imply his possession and use of legal knowledge or skill.
>
> Specifically, the relation of attorney and client exists, and one is deemed to be practicing law whenever—
>
> > (1) One undertakes for compensation, direct or indirect, to advise another, not his regular employer, in any matter involving the application of legal principles to facts or purposes or desires.
> >
> > (2) One, other than as a regular employee acting for his employer, undertakes, with or without compensation, to prepare for another legal instruments of any character other than notices or contracts incident to the regular course of conducting a licensed business....
> >
> > (4) One holds himself or herself out to another as qualified or authorized to practice law in the Commonwealth of Virginia.

Pt. 6, § I, Rules of Supreme Ct. of Va.

81 In response to the argument that Upright facilitates the unauthorized practice of law, Upright asserts “[t]hat notion is both over simplified and unproven. While admittedly in these two cases senior client consultants violated protocols and arguably gave consumers legal advice, the Trustee has presented no evidence of their actions being widespread.” Upright Defendants' Post-Trial Brief at 72. The sampling of the client consultants' actions in this case, combined with evidence as a whole, was enough to satisfy the Court that Upright has serious oversight issues.

82 *Cf.* Delafield, Tr. 167–68, Day 2.

83 This brings up Morgan's use of appearance attorneys. James McMinn, Morgan's former associate, was sent to the 341 meeting for Scott. He never

met her prior to that meeting, and he spoke to her for the first time "in the moments before the 341." UST Ex. 31, Tr. p. 110. In addition, she was a client of Upright Law, not one of Morgan's separate law firm where McMinn was employed. Lines of separation between the two firms appear to have been blurred, if non-existent. This too is unacceptable and shall stop.

84 Delafield and Morgan are both further reminded of their obligations under 11 U.S.C. §§ 707(b)(4)(C) and (D), as well as Fed. R. Bankr. P. 9011 and Local Rule 5005–4(B). *See First State Bank of Newport v. Beshears (In re Beshears*), 196 B.R. 468, 472, n.2 (Bankr. E.D. Ark. 1996) ("At least one of the signatures purporting to be [the debtor's] was executed by his attorney. This is a violation of Rule 9011 which requires pleadings, *except a list, schedule, or statement, or amendments thereto,* to be signed by an attorney. The petition and schedules are required to be signed, under oath by the debtors themselves."). The cavalier manner in which such matters were handled in these cases will also stop.

85 The Williamses and Ms. Scott have been put through much stress, anxiety, and inconvenience in this case, including having to take time to appear for depositions and/or court. The Court believes directing Delafield and Morgan to pay them the sum indicated is an appropriate sanction in combination with their revocation of privileges to practice before this Court. The Court's Order will also impose continuing legal education requirements in both fundamentals of bankruptcy law and ethics on Delafield and Morgan.

86 Section 526(c)(5)(B) provides, in part, that "... if the court ... finds that a person intentionally violated this section, or engaged in a clear and consistent pattern or practice of violating this section, the court *may* ...—(B) impose an appropriate civil penalty against such person." 11 U.S.C. § 526(c)(5)(B) (emphasis added). Because the Court has already imposed sanctions against LSC, Upright, Delafield and Morgan, including fining LSC and Upright, and sanctioning Delafield and Morgan $5,000.00 each, the Court elects to exercise its discretion and not award a separate civil penalty against LSC, Upright, Delafield and Morgan under Section 526(c)(5)(B). Williams Count V and Scott Count IV are dismissed.

87 This was a difficult and vigorously contested case, and trial counsel on both sides are commended for their efforts. As a suggestion to the UST, if in the future deposition testimony is to be used at trial—and that deposition testimony refers to an exhibit—it would be helpful to the Court and anyone else reading the transcript to have the court reporter mark the exhibit for identification so everybody knows what document the witness is talking about. Tr. 261–64, Day 2.

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2018 WL 735351
Only the Westlaw citation is currently available.
United States Bankruptcy Court, W.D. Louisiana,
Shreveport Division.

IN RE: Lillie Mae **BANKS**, Debtor

Case Number: **17–10456**
Signed February 2, 2018
Entered February 6, 2018

Attorneys and Law Firms

Andrea Augustus, The Augustus Law Firm LLC, New Orleans, LA, for Debtor.

MEMORANDUM OPINION

JEFFREY P. NORMAN, UNITED STATES BANKRUPTCY JUDGE

***1** The Court held a hearing on the Acting United States Trustee's Motion to Disgorge Fees and for Other Appropriate Relief (ECF No. 16) in the above captioned bankruptcy proceeding on January 9, 2018. This opinion constitutes this Court's findings of fact and conclusions of law. To the extent any of the findings of fact are considered conclusions of law, they are adopted as such. To the extent any of the conclusions of law are considered findings of fact, they are adopted as such.

STATEMENT OF JURISDICTION

The United States District Court for the Western District of Louisiana has issued a General Order of Reference of Bankruptcy Cases and Proceedings dated June 1, 2012. This Court has subject matter jurisdiction over this action pursuant to 28 U.S.C. § 1334. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2)(A). This United States Bankruptcy Court has the authority to issue final orders pursuant to 28 U.S.C. § 157(b). The Court also has inherent authority to "to discipline attorneys who appear before it." *Chambers v. NASCO Inc.*, 501 U.S. 32, 43 (1991). The Court's inherent authority is further bolstered by 11 U.S.C. § 105.

FACTUAL AND PROCEDURAL BACKGROUND

This case is an unfortunate tale of attorney delay, promises to a client made by counsel but not kept, deception, and professional negligence. On December 29, 2015, the debtor, Lillie Mae **Banks** (hereinafter "**Banks**"), contacted UpRight Law LLC (hereinafter "UpRight") by telephone. After a series of calls this opinion discusses later, **Banks** ultimately retained UpRight on February 16, 2016, to file a Chapter 7 bankruptcy case. After unnecessary delay and several errors, UpRight finally filed a Chapter 7 for **Banks** on June 10, 2016, some four months later. This first bankruptcy case was dismissed on June 13, 2016, three days after it was filed, when UpRight failed to file **Bank's** credit counseling certificate. UpRight committed additional errors in attempting to reinstate [1] **Banks**' case, failing to properly file and prosecute said motion; therefore that case remained dismissed. **Banks**' second bankruptcy case (the instant case) was filed on March 28, 2017. Unfortunately, this case was subsequently dismissed on May 11, 2017, again due to UpRight's negligent failure to file required documents. [2] Thereafter, UpRight did not seek to vacate the dismissal order, which it easily could have done. But for the actions of the United States Trustee (hereinafter "UST"), the debtor would have been on her own to deal with the legal mess and entanglements created by UpRight. On May 18, 2016, the UST sought to vacate the dismissal order in this case, which the Court granted. The UST then filed a Motion to Disgorge Fees and for Other Appropriate Relief. The Court's findings of fact derive from the hearing conducted on the UST's motion, which was held on January 9, 2018.

FINDINGS OF FACT

***2** By stipulation, the parties introduced 38 exhibits into evidence. Some of these exhibits consist of telephone transcripts, emails, and text messages. These exhibits, together with witness testimony, give a clear picture of the interactions between UpRight and **Banks**. The Court will provide a chronological review of the events in this case.

On December 29, 2015, after discovering UpRight on the internet, **Banks** called UpRight for the first time. First, **Banks** spoke to an employee named David, who placed notes from their conversation into UpRight's computer system. David ultimately routed her to Brian, who is

described as a "senior consultant" and is not an attorney. **Banks** disclosed she had between $15,000 and $18,000 in debt that she could not pay. She told Brian her problems stemmed from a broken $10,000 heating and air conditioning system that Sears refused to fix. She indicated that, given her fixed income, she could not afford to pay Sears. The Court considers Brian a salesperson, as it is obvious he was following a sales script. He made the following promises in this initial conversation, nearly all of which turned out to be false:

a. He indicated he would set **Banks** up on a payment plan to pay for her bankruptcy.

b. He stated he would provide her a number for the immediate referral of creditor calls. He promised creditors would be sued if they continued to call. The following is a direct quote from David during the call:

> "I mean, because what I would do is I'd get you the number that you can start referring your creditor calls to us, and basically what you're going to tell them is say, look, I've retained a law firm that's handling my finances. Here's the number and don't call me again. And if they do call you up, you let us know. We'll go after them, we'll sue them, and whatever funds we collect we put back into your pocket as well, so I mean, it's a win win situation. That way...if they do contact you, again we'll go after them and...we'll make sure that, you know, we collect the funds and then we'll put those funds back into your pocket as well. So that's...what we'd be able to do for you, and you know, the relief would—**it would definitely be able to start today** as opposed to, you know, at some other time as well [emphasis supplied]." UST Ex. 1, pgs. 7–8.

c. He promised **Banks** that her bankruptcy would only take a couple of months. The Court notes that **Banks**' bankruptcy has not concluded as of this date, which is more than two years after this promise was made.

d. He promised her "[t]his will be a very simple case." The Court agrees that this should have been a simple bankruptcy case. However, this is "the rest of the story,"[3] as UpRight failed to represent **Banks** adequately in the case.

e. He quoted **Banks** a fee of $1,685.00 for filing her Chapter 7, which covers filing fees, court costs and all attorney's fees.

f. He represented that UpRight is one of "the biggest and best bankruptcy law firms in the country."

g. He indicated UpRight is a nationwide law firm that delivers services seamlessly to clients regardless of the location using the internet, email, and telephone. He stated this UpRight provided these services as a convenience to clients The Court notes UpRight's legal services were not seamless with respect to **Banks**, and that the internet, email, and telephone options appear to mainly benefit UpRight itself.

***3** h. Brian promised **Banks** would be represented by a local lawyer and that she could travel to that lawyer's office if she desired. As discussed later, **Banks** was not appointed a local lawyer. Instead, UpRight appointed a lawyer located 350 miles from **Banks**' home.

i. Brian concluded by stating that **Banks** was "all set" and that "the attorneys will be reaching out to you very soon." The Court notes that **Banks**' local attorney waited almost 45 days to contact her after this conversation. At the end of this initial conversation, Brian read a scripted disclaimer. This disclaimer expressly contradicted some of the promises Brian had just made to **Banks**. The disclaimer stated the following, in part:

1. "Our firm does not offer services for non-bankruptcy alternatives." Brian had offered to sue **Banks**' creditors if they call her. This promise is a reference to the Fair Debt Collection Practice Act.[4] However, if UpRight does not offer these services, why were they offered as an inducement to get **Banks** to retain the firm for a bankruptcy?

2. "You acknowledge that you've asked—that the firm does not represent you until you talk to your local attorney." Brian had promised immediate relief, yet the disclaimer indicated that relief would not be immediate. In fact, **Banks** did not speak to her "local" attorney for almost 45 days after this conversation.

3. "You understand and accept for your video conference you will not meet face to face with your attorney at your hearing date unless you want to travel to their office." This disclaimer is confusing. Typically, the only "hearing" in a no-asset Chapter 7 case is the § 341 first meeting of creditors. In this division, this meeting occurs at the courthouse and the attorney would not participate by video conference. Perhaps Brian was

> indicating that future attorney client meetings would be conducted by video conference. However, this disclaimer contradicts Brian's earlier promise that **Banks** could meet with the local attorney at the attorney's office.

Banks received another telephone call from UpRight the same day (December 29, 2015). This time she spoke to an individual named Josh Laker, who identified himself as an attorney with UpRight. Mr. Laker is an attorney admitted to the Illinois State Bar on November 5, 2015, and who lists his registered business address at UpRight Law at 79 W. Monroe St., Chicago, IL 60603–4901. Mr. Laker is based in Chicago, and is not licensed to practice law in Louisiana. He advised **Banks** that she would be getting a retainer agreement via email. He also stated the following:

> "We are a virtual multijurisdictional law firm, so all that means is what lawyers and legal assistants in Louisiana and outside Louisiana helping you with your case, so while I'm in Chicago in our main office and, you know, we'll have a team here that will be helping you through the process and working on your case, you'll also have a local partner/attorney, and that's Ms. Cynthia Tanner, [5] and Ms. Tanner is going to be reaching out to you soon." UST Ex. 2, pg. 6.

***4** Cynthia Tannert electronically signed **Banks**' Attorney Client Base Retainer Agreement for Chapter 7 Bankruptcy Related Services (hereinafter the "retainer agreement") the next day. Ms. Tannert is located in Greenville, Tennessee and is licensed to practice law in Tennessee and Georgia. She has never been licensed to practice law in Louisiana. Ms. Tannert never contacted **Banks**. Further, **Banks** never received a retainer agreement signed by an attorney licensed in Louisiana. Josh finished the call by giving **Banks** a number for creditor referrals and confirmed **Banks**' payment arrangement for her Chapter 7 bankruptcy.

Banks signed the retainer agreement for Chapter 7 Bankruptcy on December 30, 2015. **Banks** signed electronically using DocuSign. Cynthia Tannert's signature is affixed to the document using the /s/ notation, but she did not physically sign the retainer agreement or even see it. Tannert, a partner attorney with UpRight, has signed a contract giving UpRight permission to sign her name to these contracts without notice. The retainer agreement specifically provides that "[t]he undersigned Partner of Firm has authorized Firm to affix Partner's digital signature upon this Agreement."

The Court finds the retainer agreement problematic. Some of its terms violate the Louisiana Code of Professional Responsibility, specifically Rule 1.5. However, as **Banks** never received a signed copy of the agreement signed by an attorney licensed to practice law in Louisiana, the agreement is not binding. Still further, the retainer agreement contains terms that are contrary to the oral representations made by UpRight and contains "unbundling" provisions this Court has not and will not allow. [6] For example, UpRight had previously quoted **Banks** a onetime fee of $1,685.00 for filing her Chapter 7, which covered filing fees, court costs, and all attorney's fees. However, the retainer agreement signed by **Banks** allows for additional attorney fees for the negotiation, review, and execution of reaffirmation agreements with creditors. This Court does not allow such unbundling. In the Fifth Circuit, a debtor must reaffirm, redeem, or surrender all secured debts. *Johnson v. Sun Finance Co. (In re Johnson)*, 89 F.3d 249 (5th Cir. 1996) (holding chapter 7 debtors cannot retain collateral securing their consumer debt without either redeeming the property or reaffirming the debt). If a debtor mistakenly does not reaffirm or redeem collateral, a debtor can be forced to surrender that collateral. Therefore, this Court considers reaffirmation or redemption an integral part of representation in a Chapter 7 case. An attorney cannot unbundle such services. Also, this Court will not allow UpRight's attempt to disclaim or resolve this issue by stating the following in its retainer agreement:

> In various jurisdictions, services for reaffirmation agreements may not be excluded in Firm's limited scope retainer agreement, in which case the Firm will waive the $150.00 fee.

Such language is confusing. It also contradicts to the oral representations UpRight made to **Banks** that all legal services are included in her quoted fee. Any future retainer agreements between UpRight and its clients in the Western District of Louisiana must specifically include all services integral to a Chapter 7 filing. It also must conform to the Louisiana Rules of Professional Conduct.

*5 On January 5, 2016, Brian returned **Banks**' telephone call. She had called UpRight earlier and left a message. She was worried about UpRight's legal representation. Brian replied as follows:

> "Yeah, yeah, well, we're—we're definitely going to be working on your case as I mentioned to you last time, and, you know, we're definitely moving things forward in the right direction, so, I mean what you're going to be doing in the meantime is like I mentioned to you previously just refer your creditor calls to us, and—and, you know while you're paying off your bankruptcy. Certainly, you know, as I just mentioned to you last time, if you do have some funds due in tax season, which is right around now, you can certainly put that toward your bankruptcy and it will be—you'll pay if off that much more sooner, so—" UST Ex. 5, pgs. 3–4.

Banks was worried as she had been approached by one of her creditors. Brian responded as follows:

> "Yeah, you're—we're—we're moving forward with your—with your case. That—that's what we're doing, we're definitely going to be moving forward with—with getting you started with your bankruptcy. Absolutely." UST Ex. 5, pg. 4.

Banks was stalling because he was aware there really was no action taking place on **Banks**' case. UpRight was not going to file her case until she had paid the retainer. To his partial credit, he did effectively communicate to **Banks** that her case would not be filed until she finished what he called "a great payment plan." However, the Court is troubled by this conversation because it completely contradicted his prior promise that relief would be immediate.

No later than January 18, 2016, UpRight's partner attorney Andrea Augustus[7] (hereinafter "Augustus") was aware that UpRight had assigned her **Banks**' Chapter 7 case. On that day, Augustus received an email from Joe Liang at UpRight regarding why she had not called or contacted **Banks**. He stated the following in that email:

> "Secondly, I wanted to see if there's anything I can do to assist with the 9 clients awaiting the first compliance call. Let me know if you are having difficulty getting ahold of them." Respondent Ex. 3.

Banks was one of the nine clients she had not contacted. Augustus responded two days later, on January 20, 2018. She apologized and stated that she would be emailing those nine clients, including **Banks**, later that day.

On February 1, 2016, some 12 days later, **Banks** calls UpRight. She was concerned that her local lawyer had not contacted her. **Banks** was apparently aware that Augusts was her local attorney, but the record is unclear about how she knew this. **Banks** spoke with an individual at UpRight named Sola, who was not an attorney. **Banks** indicated she was worried because Augustus lives in New Orleans and she wanted to get a Chapter 7 hearing date. She was advised that her Court date would be about three weeks after she filed her bankruptcy case. Sola also stated that **Banks**' case had not been filed yet due to her not having paid her retainer. **Banks** was worried she would have to go to court in New Orleans, but Sola advised her that she would go to court in her county.[8] **Banks** stated "I'm just trying to get my mind settled." She indicated she wanted to pay her fees off early so that her case could be filed. Sola advised that she could pay off her case in full and her bankruptcy case would be filed.

*6 On February 10, 2016, Augustus emailed **Banks**. This email was brief and merely contained documents Augustus was requesting **Banks** complete. Respondent Ex. 4. Before this email, it had been 43 days since **Banks** initially contacted UpRight. This email was the first time she had been contacted by a lawyer licensed to practice law in Louisiana and admitted to practice in the Western District of Louisiana federal courts. Any legal advice given to **Banks** from December 29, 2015, to February 10, 2016, had been given by staff of UpRight or by an UpRight lawyer not licensed in Louisiana. This Court has concerns about the unauthorized practice of law during this substantial period of time.

On February 16, 2016, **Banks** called UpRight. She indicated she had been unable to get in touch with Augustus. She was confused and believed that Augustus was a paralegal. She stated:

> "**Banks**: My name is Lillie **Banks**, and I've been trying to get in touch with the paralegal that they assigned me to which is Andrea Augustus."

UpRight: OK

Banks: I'd like to be able to reach anyone at that number.

UpRight: What number do you have for her?

Banks: (504) 264–1167

UpRight: Oh, okay. Do you leave messages for her when you call?

Banks: Yes, I have left several messages and I haven't had a return call." UST Ex. 7, pg. 2.

By this point, **Banks** had received certified letters from a creditor. She had yet to speak to Augustus or any attorney licensed in Louisiana, and had only received a brief email from Augustus. UpRight advised **Banks** again to give creditors UpRight's contact information. UpRight further advised **Banks** to complete her documents so that she could file bankruptcy.

UpRight attempted to call Augustus on another line, but they only reached Augustus's voice mail. UpRight left the following message on Augustus's voicemail:

"Hi, message for Attorney Augustus: This is Scott calling from UpRight Law. I have a client that's been trying to reach you. She got your email address to documents and information you're going to need from her. Has a few questions. Client's name is Lillie **Banks**, B–A–N–K–S. She's out of Homer, Louisiana" UST Ex. 7, pg. 6.

Banks was still worried about Augustus's location. UpRight attempted to allay **Banks**' fears. UpRight stated the following:

"So the nice thing is that if her office is too far away from you, she travels to you for the only thing you actually need to appear for which is the 341 meeting with the trustee after you're filed. If her office is too far away, at the time of the review you'd do it as a video conference call via Skype or Facetime. We have these options too. So her location shouldn't be an issue. We do want to get you at least with somebody who covers that district." UST Ex. 7, pg. 8.

It is clear UpRight had little or no knowledge that its partner attorney (Augustus) and the client (**Banks**) are 350 miles apart, which would be a 12 hour round trip by car. Given the distance between them, **Banks** never personally met with Augustus, nor anyone from UpRight. **Banks** expressed concern that her Chapter 7 payment plan would not end until April, but she wanted to pay it off early and get her case filed. In response, UpRight stated the following:

"Yeah, take care of the fees quicker, get those types of judgments or those letters that the courts are sending you, take care of those, absolutely, yeah, just give us a call here. We can schedule payments ahead of time and run those while we have you on the line. UST Ex. 7, pg. 10.

That same day **Banks** finished her bankruptcy payment plan earlier than scheduled. UpRight then provided Augustus a paid in full summary via email showing **Banks**' legal fees had been fully paid.

Later that same day, February 16, 2016, **Banks** again called UpRight. She spoke to Josh, who confirmed she had paid her case in full. He stated the following: "[w]hat I'm going to do for you today is start prepping your petition which is what gets filed with the bankruptcy court." UST Ex. 8, pg. 2. This is contrary to Augustus's testimony. She testified she alone was responsible for the typing and filing of **Banks**' petition. **Banks** had yet to speak to Augustus or any other lawyer licensed in Louisiana and had borrowed money from a family member to pay the bankruptcy legal fees in full. Josh promised **Banks** "[s]o you're going to be filed relatively soon here." However, the case would be unnecessarily delayed, and would not be filed for nearly another four months.

***7** On February 19, 2016, **Banks** spoke to Augustus for the first time. This was the first time she had spoken to a lawyer licensed in Louisiana. Any legal services provided by UpRight to this date had come from UpRight's staff. The attorneys she had spoken to were located in Chicago, and those attorneys were not licensed to practice law in Louisiana. That same day, Augustus emailed **Banks** a bankruptcy document request letter. On March 4, 2016, **Banks** completed her credit counseling and forwarded the certificate to Augustus. Augustus's negligent failure to timely file this document caused the dismissal of **Banks**' first bankruptcy case.

On March 17, 2016, **Banks** called UpRight to indicate she was still having difficulty reaching Augusts. The following day, she called UpRight once again. In that call, she stated the following:

Banks: I'm having a hard time trying to catch up with (incomprehensible) lady that's been assigned to me in my area.

UpRight: Yeah, Ms. **Banks**, I see you called in yesterday morning about it. When you called the number, you were unable to reach her?

Banks: Well, I called yesterday and say I'll call you this time, and I still can't never get her. UST Ex. 11, pg. 2.

The UpRight representative then promised to get managers involved and assured **Banks** that Augustus or someone else would get in touch with her soon. The representative ended the conversation by saying the following:

> UpRight: Yeah, but you understand that we're legit, because obviously if we weren't, we wouldn't have taken you out with the payment that you agreed to. We would have probably like emptied your **bank** account and disappeared in the night. I mean, we're here to help you, and we still want to file your Chapter 7. I can't speak for why Attorney Augustus is not returning your calls, but what I can do is get my managers involved so we can fix that. UST Ex. 11, pg. 4.

Despite UpRight's continued promises, there was an amazing lack of oversight of August by UpRight. Scott Hogan, who holds the title of Client Advocate with UpRight, sent an internal email to a Joe Liange that same day (March 18, 2019) stating the following:

"Ms. **Banks** called in yesterday and not being able to reach the PA.[9] She has left VM's and gotten no calls. Crystal called yesterday too and left a message. Told Ms. **Banks** I'd get you involved since she can't get an answer." Respondents Ex. 7.

Joe Liange forwarded the email to Augustus and asked her to "[p]lease reach out to the below referenced claim before the end of the day." Augustus responded by stating the following:

"I've spoken to Ms. **Banks** on several occasions and sent an email. However, I will contact her today. I believe clients are unfamiliar with my voicemail and hand up when it asks their name." *Id.*

Her response was forwarded to Scott Hogan, who took no further action.

Irrespective of Augustus's assurances, **Banks** called six days later UpRight on March 24, 2016. She had been served a civil citation and was very upset. She did not feel like anything was being done on her case. She stated the following:

"Because I don't feel like anything is being done. I have paid my money, and I just got issued a civil citation due March (incomprehensible) in my house in (incomprehensible) by creditors, and y'all had told me not to pay anything, stop paying everybody, so I did that, but now I'm being sued, and I have ten days with this—all these papers they just sent me." UST. Ex. 12, pg. 2.

UpRight responded that they needed more documents from **Banks**. She responded that she could not reach her attorney. She stated the following:

Banks: I called her. I talked to her (incomprehensible) and she told me—and said they need some more information on the stuff that she says she didn't receive from me, so I've been checking my e-mail, and I haven't received anything (incomprehensible).

***8** UpRight: Have—have you tried to contact her today just to see if she sent it.

Banks: I just tried and I told you I never can get her on this number that she gave me. UST Ex. 12, pg. 2–3.

That same day, **Banks** emailed Augustus and stated in all caps "DID YOU RECEIVE MY E –MAIL? PLEASE CALL ME AT YOUR EARLIEST." Augustus did not call **Banks**, but instead emailed a reply of "[n]o ma'am I haven't seen an email from you. I'll contact you as soon as I

am able." UST Ex. 13. In response, **Banks** emailed Augustus from an email address not associated with her and carbon copied herself. This email contained a copy of the civil citation the sheriff's department had issued that morning. **Banks** also gave Augustus two phone numbers to reach her.

Four days later, on March 28, 2016, Augustus emailed **Banks** with a request for updated documents. One day later, she provided a fax number so that **Banks** could forward the documents. Apparently, the notice of a civil citation had still not caused Augustus to take more immediate action and it would still be over two months before she would file **Banks**' first Chapter 7 case.

On April 10, 2017, **Banks** again emailed Augustus in all caps. That email stated the following:

> "ANDREA WILL YOU PLEASE GIVE ME CHECK UP CALL SO I WILL KNOW IF I HAVE EVERYTHING BEFORE COURT DAY, IF YOU ARE NOT HANDLING MY CASE PLEASE LET ME KNOW. THANKS FOR EVERYTHING YOU HAVE DONE IN THIS MATTER." UST Ex. 14.

The next day, April 11, 2016, Augustus sent **Banks** an updated list of items required to be submitted before the case could be filed. The following day, **Banks** faxed over 64 pages of documents to Augustus. One day later, on April 13, 2016, a judgment is taken against **Banks** by Republic Finance for $2,133.71 plus interest accruing at the rate of 18%, together with attorney fees at 25%.

On April 15, 2016, **Banks** sent a text message to Augustus asking if she had received the 64 pages faxed to her. Augustus did not respond. That same day, she called UpRight yet again. She was angry about the judgment. She stated that "she has done what they asked me" and "today I was—I have been issued a judgment against one of my creditors that I have because there was no response." She continues:

> "I've been in touch with her (Augustus), and I have sent her all kind of information. I gave her information about when they first sent me a letter from the—the sheriff's department came by her, and they issued them a letter from the—from the creditors that I owe. I told her about this. They gave me ten days. And I gave her that information, and nothing has been done, no response. They haven't contacted them, I guess, or whatever because the people kept calling me and say I was lying that I had bankruptcy, and—because I don't' have a court number so today I get a notice of judgment, and..." UST Ex. 16, pgs. 3–4.

At this point, UpRight cut **Banks** off and told her she needed to provide more documents to Augustus. In response, Ms. **Banks** stated the following:

> "**Banks**: She got everything. I have—as she explained what she need, I get it right back to her, so she got everything, and she's sitting there e-mailing to me she had received all my documents, so she got it. Now my, (incomprehensible) when I first filed, this guy name—well, I forgetted his name. Anyway, he tells me he's (incomprehensible) UpRight Law (Incomprehensible). He was the one advised me not to pay anything else on the bills—
>
> ***9** UpRight: Right, no, I get that—
>
> **Banks**: —and just give them this 1–800 number—
>
> UpRight:— I totally get that and—
>
> Ms. **Banks**: —to call—
>
> UpRight: —and that's correct—that's correct, but—
>
> **Banks**: —which I have, but—
>
> UpRight: That's correct, but the key is to get you filed as soon as possible.
>
> **Banks**: Yeah, but it been there since February, and I have to keep calling back and forth to you all, and then—you know, because sometime Andrea is so hard to get in touch with, you know, and then I have to call your office and say I cannot get her, but lately she has been responding to me, but I'm saying now that—now I got this judgment so if (incomprehensible) I don't see no need to (incomprehensible). Because this here will have added me that I got to pay this amount—I got to pay two thousand something dollars in

> (incomprehensible), so I'm trying to see if what—you know, why is my case taking so long." *Id.* at pgs. 5–6.

The conversation continues:

> "I say she have all the documents, and I have give her everything that she asked for. It burns me. She came back and said she needed some more, so I made sure I got everything that she asked for. I go my whole (incomprehensible). Everything that I gave her, I keep it with dates on it...and I feel like, you know, if—if she (incomprehensible) take the money and I'm telling her that these people here is pressuring me, that they putting up a judgment and stuff against me, that seems though that (incomprehensible) you could at least call the people and say, well, yes, okay (incomprehensible) or something to keep them from going to the four—I know they taken for action on me now. (incomprehensible) you know, (incomprehensible). So it's frustrating, because like I told her, I said, I'm on a fixed income. I can't afford to pay out of (incomprehensible). We're trying to hire a lawyer to help me out, but (incomprehensible) because my case not being handled." *Id.* at pg. 6 –8

The UpRight representative responded that "I'll call her and see what's going on, and then I'll have her to give you a call back, because we need to get your case filed." *Id.* at pgs. 8–9. It would still be another twenty days before any further action is taken on **Banks'** case.

On May 4, 2016, August emailed **Banks** a draft copy of her bankruptcy petition. **Banks** reviewed this petition, made corrections, and returned it to Augustus. Two weeks later, on May 18, 2016, Augustus forwarded a second draft of the petition, which **Banks** then corrected and returned. Thirteen days later, August sent **Banks** a tracking number for the package containing the bankruptcy petition that must be signed. **Banks** signed the petition and schedules and returned them to Augustus. Finally, Augustus filed **Banks**' first Chapter 7 bankruptcy (Case No. 16–10979). The case was filed 164 days after **Banks** originally contacted UpRight. The case was then dismissed three days later.

The docket in that first case reflects that the case was dismissed due to **Banks**' failure to comply with 11 U.S.C. § 109(h), which contains the credit counseling requirement. Augustus failed to file the credit counseling certificate **Banks** obtained on March 4, 2016, and that she had previously received. In response to the dismissal order, which Augustus received electronically, Augustus emailed **Banks** requesting another copy of the credit counseling certificate. Her email stated the following:

> ***10** "I hope this finds you well. If you would forward me the email with your credit counseling certificate it would be greatly appreciated. I do recall you sending it, unfortunately my email account is bursting and cannot be located via a search." Respondents Ex. 18.

She did not inform **Banks** that her case had been dismissed. **Banks** complied and emailed the credit counseling certificate. On June 22, 2016, Augustus filed the credit counseling certificate. She also filed the Declaration of Electronic Filing and an Ex–Parte Motion to Reconsider Dismissal. The PDF attached to the Ex–Parte Motion to Reconsider was incomplete and the clerk's office instructed Augustus to refile it. However, Augustus did not refile the document. Augustus took no further action in the case, so the case remained dismissed and was subsequent closed in February of 2017.

Augustus was negligent in allowing **Banks**' case to be dismissed and remain dismissed. Augusts could have easily vacated the dismissal order had she properly served all parties and set the motion to vacate for hearing. She negligently failed to take these actions. UpRight is also negligent in failing to appropriately supervise Augustus. UpRight's failure to supervise Augustus continued over the entire course of UpRight's representation of **Banks**.

On June 20, 2016, **Banks** called UpRight and spoke to an individual named Teeter. **Banks** explained she had received a letter notifying her that her bankruptcy case had been dismissed. The conversation proceeded as follows:

> Teeter: Here in that case do me a favor. Call Attorney Augustus. Do you want me to give her—her phone number.
>
> **Banks**: I've done called her—I got her number, and I'm not pleased with the way that I—that the feedback that I am getting, because when I got this letter, I was very upset about it, and I've been texting her so she—and I would ask her was she trying to reject my case and my phone call. She text back and just said, no. Ms. **Banks**, but I'am out of town.

> Okay, I'm having a issue. I have given you—this shouldn't have taken six months to file bankruptcy. It's been over six months. And then when I get this letter, then you can't even talk to me enough to say, okay Ms. **Banks**, that was a misprint or something. Let me know at least what is going on. UST Ex. 23, pgs. 4–5.

Teeter promised that **Banks** would get a call from someone named Orlando, who is a lawyer at UpRight.

That same day an individual named Matthew, not Orlando, called **Banks**. Matthew explained that he was an "enhanced service manager." The record is unclear whether Matthew is a lawyer. He was calling her because of her earlier telephone call and because her first Chapter 7 case had been dismissed. He did not know why the case has been dismissed, even though this information could easily be obtained from the Court's electronic docket. **Banks**, who was confused by the terminology, advised him the case was dismissed because a "cash (sic) certificate and debt repayment plan wasn't provided." She stated that she had taken the class but could take the second financial management class until her case was filed. She stated the following:

> "But, I had sent her everything she asked for. I had taken the class online, the counsel class for the certification right after—when I first filed and then I couldn't file—I couldn't take the next class until they gave me a court number." UST Ex. 22, pg. 3.

***11** **Banks** complained that she did not understand why it had taken six months for her case to be filed and that "it shouldn't take that long to file bankruptcy." She wanted to know why her creditors were still calling her. Matthew advised her to give them her case number. **Banks** explained that she had not given her creditors her case number because her case had been dismissed. **Banks** was clearly frustrated, as was Matthew. The conversation continued:

> **Banks**: I feel like I may have lost $1,600.00 that I paid you all up front in February. I paid the $1600.00 in February, and here it is June.—
>
> Matthew: Correct.
>
> **Banks**: —and I'm still having to pay for it to have me get through this in a painless manner, but I haven't had nothing but paid since I've been through this because I—
>
> Matthew: If—if you—if you have creditors calling you, you have to give them your case number and then they know to stop. *Id.* at pg. 7.

Matthew clearly was not taking into consideration the fact that **Banks**' case was dismissed. Due to the dismissal of the case, the automatic stay [10] was no longer in effect. Therefore, Matthew's advice had little value. The conversation continued:

> **Banks**: But how can I give them a case when I didn't have a case number?
>
> Matthew: You—I—I—I don't know why this is not making sense.
>
> **Banks**: I did not get some up until later—
>
> Matthew: Okay, you're—you're filed—you're filed on June 10. Okay?
>
> Matthew: So prior to June 10th there was no case number because your case was not filed up until June 10th. Now that June 10th came around, you have a case number, so anybody calling you cannot call you so—as long as you provide them this case number. *Id.* at pgs. 7–8.

The Court again stresses that **Banks**' bankruptcy case had been dismissed for seven days. Matthew had no basis for stating that "anybody calling you cannot call you so—as long as you provide them this case number." This representation was false as there was no automatic stay in effect. The conversation continued:

> Matthew: Now, to keep your case going the way it needs to, it sounds like the certificate of completion for the debtor's education course would be needed on the court's end, so what we're going to have to have you do is contact Ms. Augustus, because on our end everything—everything's completed. *Id.*

Given **Banks**' repeated difficulty communicating with Augustus, Matthew's advice was problematic. Further, by stating that everything on their end had been completed, Matthew confirms this Court's suspicion that UpRight is merely a referral service. **Banks** responded as follows:

> **Banks**: Okay, can you call (incomprehensible)? She's still not answering my phone calls. She not answering my text. *Id.*

Banks was clearly frustrated. She later asked if this was the first case Augustus had handled. Matthew responded as follows:

> Matthew: No, not at all. When—she's a partner of ours, okay, so she's not someone that we just say, hey you know, here's—here's someone that needs their bankruptcy filed. She's literally a partner of UpRight Law and a player of UpRight Law. Not, to become a partner of UpRight Law, we're not going to hire any Tom and Sally fresh out of law school. They have to be doing bankruptcy for a very long time. This is not her first case. If something is going to be dismissed, it's generally because, unfortunately, something was not submitted by the client, so it—it's not something on the attorney end that she might have done, as right now it sounds like there might be some sort of documentation missing. So again, you sent the documents directly to her office, not here, otherwise I would pull up everything, you—sent it to her office, so that—that's why I—I don't want to sound redundant, but we are going to have to have you speak with her, now if you can reach her yourself, I will even step in there and say, hey Andrea, please—
>
> **Banks**: Yeah, I want you to step in because she is not responding to me. UST Ex. 22, pgs. 11–12.

***12** As previously stated, **Banks**' case was dismissed due to Augustus's failure to file the credit counseling certificate that **Banks** had previously provided. **Banks** is not at fault for the dismissal; however, Matthew ignorantly attempted to blame her for not providing documents. He then attempted to intimidate her regarding a refund of the fees she had paid. He stated:

> Matthew: And I'll—and I'll do that, because Lillie, on our end—on our end as far as, you now, refunds go, which is what I think you're about to (incomprehensible), the work's completed, like the case is filed, the attorney fees are done, credit counseling all that so we couldn't offer a refund. *Id.* at pg. 12.

First, the Court must comment on the ignorance of Matthew's comments. **Banks**' bankruptcy case had been dismissed—the work was far from complete. In fact, **Banks**' case is still not complete to date. Second, the retainer agreement signed by UpRight specifically provides a guaranteed refund policy, so Matthew's comments are totally without justification. The retainer agreement states the following:

> 5. Guarantee—Refund Policy. Firm offers a 100% Money Back Guarantee that if the courts do not accept your bankruptcy filing because of an error on our part**,** we will refund 100% of your money, including the filing fee.

UpRight had repeatedly promised **Banks** that it would take specific actions, and that she was protected from her creditors. UpRight had also enticed her with the full refund policy. UpRight had promised that **Banks**' case would be competently handled until discharge. As the Court will discuss, these misstatements and broken promises are not isolated incidents, and UpRight's negligent representation actually continued.

Matthew later agreed to step in and help **Banks**. He stated "I'll step in and help with that, I really will because I know you're going through a lot." *Id.* Unfortunately, there is no evidence that Matthew followed up on any of his promises. **Banks**' case remains dismissed, and it would take nine more months for her second case to be filed.

On the morning of June 20, 2016, Augustus emailed **Banks** with a draft motion to reconsider the dismissal of her first case. The record is unclear whether **Banks** received or read the email prior to her telephone calls to UpRight. This motion was filed in Case No. 16–10979

(ECF No. 6), but it was filed incorrectly. The Clerk of the Court requested the motion be refiled; however, Augustus failed to ever refile the motion to reconsider.

On July 12, 2016, Augustus emailed **Banks**. She stated the following:

> "That letter is the result of our previous conversation. I have been in contact with the law clerk of the judge your case is in front of to resolve the issue." Respondents Ex. 21.

Augustus had not been in contact with the law clerk of this Court. This Court's Courtroom Procedures, which are available on the Court's website, specifically states that "[c]ontact with Judge Norman and his law clerks, other than by pleadings, is strictly prohibited. Letters and telephone calls to chambers are prohibited." Augustus intentionally misled her client.

On July 25, 2016, an individual named Julian at UpRight contacted **Banks** to advise her that there was a court date the following day that Augustus should be attending to reconsider the dismissal of her case. This statement was false as there was no hearing scheduled.

***13** On August 18, 2016, **Banks** called UpRight once again. She wanted more information regarding the next step in her case. She assumed the dismissal of her case had been vacated. However, she was still having difficulty communicating with Augustus. She stated the following:

> **Banks**: Yeah, but—okay, what is my next step, because it been filed for I guess maybe a month or a couple of months, I can't ever get in touch with my lawyer. She's never returned my call.
>
> UpRight: You're—you're waiting—you're waiting on a discharge, so a discharge takes, excuse me, sixty to ninety days.
>
> **Banks**: Okay, so my question is can we open my case, because I never had dismissed my—they have dismissed my case at one time because something about Andrea (incomprehensible) or something.
>
> UpRight: Let's see.
>
> **Banks**: So I'm just on pins and needles, and I never—I can never get in touch with her any time. Her mailbox is full and can't accept message, and the last time I (incomprehensible) was someone from your office when they told me that you probably going to court the next day, and I haven't heard from her to know how the court date went. I've been texting her trying to find, and I still haven't got a response. Hello?
>
> UpRight: Give me one second.
>
> **Banks**: Okay, I thought you had hung up on me.
>
> UpRight: Everything looks fine from—from what happened in June so looks like you are waiting to be discharged.
>
> **Banks**: Okay, Is there any way you (incomprehensible) in touch with Andrea and have her just give me a call—
>
> UpRight: Yeah, I'll—I'll
>
> **Banks**: —and let me know what's going on?
>
> UpRight: I'll call her and—and see if I can get in touch with her, and I'll shoot her over an e-mail. All right?
>
> **Banks**: Okay.
>
> UpRight: All right, have a good—
>
> **Banks**: Okay.
>
> UpRight: Have a good day.
>
> **Banks**: Thank you. UST Ex. 27, pgs. 2–4.

UpRight never followed up on this call, and Augustus never contacted **Banks**. **Banks**' bankruptcy case remained dismissed and no discharge would be forthcoming. Again, UpRight misrepresented the facts of **Banks**' case to her.

On October 4, 2016, **Banks** again called UpRight. She complained that she had filed bankruptcy, that her case was not yet closed, and that she was getting creditor correspondence. She was not aware that her case remained dismissed. **Banks** again complained that Augustus was unresponsive. UpRight promised to escalate her case to a manager. **Banks** replied that this had been promised before and that nothing had happened. UpRight promised the following:

> UpRight: Right, so they'll look into all that that they'll reach out to Ms. Augustus and get the details from her and then at that point we'll reach out to you. Hopefully Ms. Augustus will reach out to you and we can get this moving forward and any steps need to get this case filed and whatever else it needed at that point. UST Ex. 28, pg. 8.

On October 7, 2016, **Banks** again called UpRight. UpRight indicated that Augustus would call **Banks** that day. **Banks** was frustrated as she knew her case had been dismissed. UpRight advised that the matter had been escalated to partner relations and promised they would reach out to her with an update soon. However, as usual, UpRight never followed up. Again, the Court stresses the repeated broken promises made by UpRight to **Banks** and UpRight's continued failure to monitor and oversee its partner attorney Augustus.

***14** On October 12, 2016, **Banks** again called UpRight. August had not called her, and no one from partner relations had called her. **Banks** expressed her frustration with the fact that no one would ever follow up with her. UpRight simply had no answer. A representative merely promised to get in touch with partner relations. In this conversation, **Banks** stated the following:

> **Banks**: You should at least give me someone that know how to handle the business. (Incomprehensible) I have to start back in—receiving letters from all these collection agent. You know, where is my money then, you know. They tell me they can't reimburse me my money but you haven't given—you haven't satisfied me yet. So do I need to get a lawyer to make sure this company's legit, or what do I need to do? Because I'm tired—my—I don't feel like—
>
> UpRight: No, the—the legitimacy is—isn't really the issue. Listen, I cannot argue that—that this is an issue Okay? Again, I wish I could give you an answer—
>
> **Banks**: It's an issue of—
>
> UpRight: What was that?
>
> **Banks**: It's an issue to me because it's all have—almost a year. I haven't yet been (incomprehensible) before the judge or anything. You know, you—you've given me all these broken promises maybe about five or six months ago. Okay, two—two—it's been at least two months ago, and I—every time I call you, you never return my call, and they telling me that if I call, they are responsible to me within seventy-two hours. I never got a phone call yet. I always have to call this—I have to call my lawyer. My lawyer do not recall... UST Ex. 30, pgs. 5–6.

On October 13, 2016, **Banks** received an email from Augustus. UST Ex. 31. This was the first time in three months Augustus had followed up with **Banks**. Augustus indicated that she was preparing to file **Banks**' second bankruptcy case. However, **Banks**' credit counseling certificate had expired.[11] Therefore, Augustus advised **Banks** to retake the credit counseling course, which **Banks** does on October 17, 2016.

On October 19, 2016, August once again emailed **Banks**. Respondents Ex. 24. She states that she will print **Banks**' first bankruptcy petition to determine if there are any changes that need to be made, after which **Banks** would need to sign it. On October 25, 2016, Augustus emailed **Banks** promising that the bankruptcy case would filed the second week of November. However, the second case would not be filed until some four months later, on March 28, 2017.

On November 8, 2016, **Banks** called UpRight yet again to complain. The UpRight representative stated the following:

> UpRight: Yeah, okay, you just need to contact Andrea Augustus if you have any questions about your case. I do see that you're all filed. That's obviously

> a good thing, but if you have any questions, you have to contact the attorney that filed your case. UST Ex. 34, pgs. 2–3.

The Court again notes that, at that time, **Banks** did not have an active bankruptcy case. UpRight promised to email Augustus and have her contact **Banks**. The UpRight representative stated that the dismissal of the first case was because "there were some issues with not being able to sign electronic filing in a timely manner." As usual, this was a gross misrepresentation of why **Banks'** first case was dismissed.

On January 3, 2017, **Banks** again called UpRight. She continues to complain to UpRight. The UpRight representative assured **Banks** that the case had been filed:

> ***15** UpRight: Yeah, your case was filed already in September, ma'am. You had your court date on—your case was filed already. It was filed in June. You had your Court date in September, so right now you're just waiting for your discharge, ma'am. You'll get the discharge—UST Ex. 35, pg. 3.

Given what had already occurred, UpRight's ignorance here is astonishing. **Banks** attempted to explain that the first case had been dismissed and a new case had not been filed. The representative stated "[w]ell, she did refile it, ma'am." The representative later retracted this assertion. Again, UpRight promised to email Augustus and "include a manager from our partner relations department." Not surprisingly, the phone call generated no response from UpRight.

On January 13, 2017, **Banks** sent a text message to Augustus stating "[p]lease call me ASP (sic), need to know where you are with my case." Augustus failed to respond. On January 24, 2017, **Banks** again called UpRight and spoke to an individual named Karen. **Banks** again complains about the status of her case and the fact that Augustus did not respond to her text message. Karen indicated she could see reports of **Banks'** previous calls to UpRight. Karen stated the following:

> UpRight: Right, yeah, we have spoken before. This is—yeah, I see notes every—you know, like all through October and November, so I know this—this has been like a long, big issue. So, Lillie, again I—you know, because—you know, there's nothing that can be resolved with this conversation alone, so let me go ahead and—and send the email to partner relations, and I'll be following back up with you with more information on Thursday. I'm putting you on my—my calendar if not before then. UST Ex. 36, pgs. 8–9.

Based on the information in the record, the Court can only conclude that the "partner relations" department does very little, and is negligent at the very least. There are multiple instances when UpRight representatives have promised to involve "partner relations." However, there were never any results.

On March 6, 2017, Denise Alcauther (hereinafter "Alcauther") at UpRight emailed Augustus about **Banks**. That email stated the following:

> Client listed below called in this morning stating that her case was supposed to be refiled. Can you please reach out to her at your earliest convenience. Please let me know if you need anything on my end. Respondents Ex. 28.

The record does not show that August responded to this email. There are no documented conversations or emails between **Banks** and Augustus from the date of the Alcauther email until **Banks'** second case was filed.

Banks' second bankruptcy case (the instant case) was filed on March 28, 2017. However, the Court notes that the petition in this case is identical to the first petition. **Banks** did not review it or sign it. The petition falsely represents that it has been signed by **Banks**. It is clear Augustus filed the exact same case without determining whether there were any changed circumstances. By filing the petition and schedules without **Banks'** actual "wet" signatures, Augustus violated the rules for the electronic filing of documents and pleadings

in this district pursuant to the Administrative Procedures for the U.S. Bankruptcy Court for the Western District of Louisiana ("Administrative Procedures"), last amended March 18, 2014. Augustus falsely indicated **Banks** had signed the documents by indicating a signature with a "/s/" before **Banks**' name. This representation was false.

***16** On April 3, 2017, **Banks** completed her personal financial management course required for a discharge. She forwarded the certificate to Augustus, who never filed it. On May 5, 2017, **Banks** appeared for her first § 341 meeting of creditors. Augustus failed to attend that meeting.

The CM/ECF docket for this case at the time of the hearing in this matter showed Andrea Augustus as the attorney of record. UpRight was not listed on the docket. Augustus's physical address at all times pertinent to this matter was her residence. Augustus testified that she did not meet with clients in her home, instead meeting with them in offices she maintained. However, she could not provide the Court with the address of any office she claimed to maintain during time when **Banks**' bankruptcy cases were pending. The Court finds that she did not maintain an office during this time, and UpRight misrepresented this fact to **Banks**. Even if Augustus had maintained an office, her location in New Orleans made it all but impossible for **Banks** to meet with her.

These facts lead the Court to conclude that Augustus never had any intention of attending **Banks**' meeting of creditors. Augustus was clearly aware of the meeting date and time as she had sent an email to UpRight confirming it. On May 5, 2017, Augustus emailed UpRight and **Banks** at 2:57 p.m. that she was unable to attend the first meeting of creditors, even though that meeting had already taken place at 10:00 a.m. She stated that a "proper motion requesting an extension arising from extenuating circumstance will be filed before end by end (sic) of day Monday." Respondents Ex. 31. No such motion was filed. The Court finds that Augustus never intended to attend the meeting given her distance from Shreveport and the travel time that would have been required.

The Partnership Agreement between Augustus and UpRight set the rate of compensation for **Banks**' Chapter 7 case. Augustus was to receive 20% of all earned fees, assuming she performed certain work, plus 13% for attending the first meeting of creditors. **Banks** paid UpRight $1350, so Augustus could have earned $175.50 for traveling from New Orleans to Shreveport for the meeting of creditors. Assuming she performed certain work and attended the meeting of creditors, Augustus could have earned a total of $445.50 for representing **Banks**. The round trip drive time between New Orleans and Shreveport is at least 10 hours. Further, there are no direct flights between the cities. Augustus's excuse that she was ill and could not attend the first meeting of creditors is not credible. The Court finds that she did not plan to attend the meeting given the low rate of compensation compared with the time and cost it would have taken to attend.

On May 11, 2017, **Banks**' second Chapter 7 case was dismissed for failure to comply with 11 U.S.C. § 521. Augustus had failed to file required employee income records, a declaration of electronic filing, a picture ID card, and **Banks**' Social Security card.[12] Augustus and UpRight took no further action on behalf of **Banks** to vacate the dismissal order or correct the Augustus's failure to file the required documents. On May 17, 2017, the UST sought to vacate the dismissal order and to take the Rule 2004 examination of **Banks**. Both motions were granted. Thereafter, on September 26, 2017, the UST filed the instant motion. The UST is seeking UpRight and Augustus disgorge all fees collected from **Banks**. The UST also requests this Court grant such other relief appropriate to deter this conduct in the future. In response, UpRight issued **Banks** a refund of $1,685.00, representing the attorney's fees and filing fee **Banks** had paid.

***17** Upright Law, LLC is not a typical law firm. It consists of Chicago based Law Solutions Chicago, LLC, (hereinafter "Law Solutions"), an Illinois limited liability company licensed to do business in Louisiana as UpRight Law LLC. The firm engages "partner" attorneys located throughout the country. The nature of UpRight's consumer bankruptcy practice was outside the scope of the hearing in this matter. However, the evidence shows UpRight refers to itself as a national law firm. UpRight does not maintain an office in the Western District of Louisiana. Instead, it engages "partners" licensed to practice law in the jurisdiction and then solicits consumer bankruptcy business over the internet.

UpRight appears to be nothing more than a referral service. It solicits clients and then refers them to local attorneys. The local attorneys, who UpRight calls "partners," file consumer bankruptcy cases for those clients after they are referred. In many instances, these "partner"

attorneys maintain their own independent practices in which they often engage in consumer bankruptcy work. It appears "partners" are not full time UpRight employees.

Augustus, who "partnered" with UpRight to handle **Banks**' consumer bankruptcy, entered into her Partnership Agreement with Law Solutions on December 17, 2015. However, as the Court has already discussed, this partnership appears to be for the purpose of client referral only. This agreement allows Law Solutions to collect a referral fee for signing up bankruptcy clients and then referring them to so called "partner" attorneys such as Augustus.

LEGAL ANALYSIS

The scope of the professional negligence on the part of Augustus and UpRight in the handling of **Banks**' Chapter 7 case is substantial. Over a period of more than two years, they have continuously violated the Louisiana Rules of Professional Conduct. These violations are noted below:

Rule 1.1 Competence:

> (a) A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.

Augustus and UpRight have failed to competently represent **Banks** in her Chapter 7 case. **Banks**' case should have been simple; in fact, UpRight has admitted as much. However, in the two years **Banks** has interacted with Augustus and UpRight, all she has achieved is two dismissed bankruptcy cases. Due to lack of legal knowledge, skill, thoroughness, preparation, and general negligence on the part of Augustus and UpRight, **Banks** has still not received a discharge.

Rule 1.3 Diligence:

A lawyer shall act with reasonable diligence and promptness in representing a client. **Banks**' Chapter 7 case should have taken no more than five months. However, over two years later, her case remains unresolved. This is due entirely to UpRight and Augustus. The Court has never seen such a lack of diligence in any Chapter 7 proceeding. Phone calls were constantly not returned. There was unnecessary delay. There were false promises. All fairly describe Upright's and Augustus's representation of **Banks**.

Rule 1.4 Communication:

(a) A lawyer shall:

(1) promptly inform the client of any decision or circumstance with respect to which the client's informed consent, as defined in Rule 1.0(e), is required by these Rules;

(2) reasonably consult with the client about the means by which the client's objectives are to be accomplished;

(3) keep the client reasonably informed about the status of the matter;

(4) promptly comply with reasonable requests for information; and

UpRight and Augustus never kept **Banks** appropriately informed of the status of her case. Augustus repeatedly failed to communicate with **Banks** in violation of the Louisiana Rules of Professional Conduct. **Banks** was often unaware of what was happening in her bankruptcy cases. Further, UpRight representative had an appalling lack of knowledge regarding what was occurring in these two bankruptcy cases. While **Banks** was always able to communicate with representatives in Chicago, those representatives either negligently or intentionally gave her the wrong information about her cases consistently. Still further, UpRight's failure to take corrective action as promised, including returning **Banks**' phone calls, as well as giving her false information, leads the Court to conclude that they failed to reasonably consult with their client.

***18** Rule 1.5 Fees:

(f) Payment of fees in advance of services shall be subject to the following rules:

(5) When the client pays the lawyer a fixed fee, a minimum fee or a fee drawn from an advanced deposit, and a fee dispute arises between the lawyer and the client, either

during the course of the representation or at the termination of the representation, the lawyer shall immediately refund to the client the unearned portion of such fee, if any. If the lawyer and the client disagree on the unearned portion of such fee, the lawyer shall immediately refund to the client the amount, if any, that they agree has not been earned, and the lawyer shall deposit into a trust account an amount representing the portion reasonably in dispute. The lawyer shall hold such disputed funds in trust until the dispute is resolved, but the lawyer shall not do so to coerce the client into accepting the lawyer's contentions. As to any fee dispute, the lawyer should suggest a means for prompt resolution such as mediation or arbitration, including arbitration with the Louisiana State Bar Association Fee Dispute Program.

Banks often came close to requesting UpRight provide a refund of her fixed fee; however, the Court notes **Banks** never explicitly requested a refund. She did frequently reference the fees she had paid. If **Banks** had overtly requested a refund, then the Louisiana Rules of Professional Conduct would have required UpRight to immediately refund the unearned portion of such fee. Regardless, the Court finds that UpRight did violate this rule. An UpRight representative said the following to **Banks**: “on our end—on our end as far as, you know, refunds go, which is what I think you're about to (incomprehensible), the work's completed, like the case is filed, the attorney fees are done, credit counseling all that so we couldn't offer a refund.” The representative was clearly attempting to avoid a refund request. Rule 1.5 would have required UpRight to immediately refund **Banks** the unearned portion of the fixed fee if a fee dispute had arisen. The UpRight representative was obviously misrepresenting UpRight's obligations under the Louisiana Rules of Professional Conduct. UpRight misrepresented its professional obligation to provide a refund. The Court holds that any future fixed fee agreement between UpRight and any Louisiana client must include a disclosure of its requirement to provide a refund under the Rules of Professional Conduct. Further, UpRight may not make statements that lead clients or potential clients to believe that that have no right to a refund.

RULE 5.1. Responsibilities of Partners

(a) A partner in a law firm, and a lawyer who individually or together with other lawyers possesses comparable managerial authority in a law firm, shall make reasonable efforts to ensure that the firm has in effect measures giving reasonable assurance that all lawyers in the firm conform to the Rules of Professional Conduct.

(b) A lawyer having direct supervisory authority over another lawyer shall make reasonable efforts to ensure that the other lawyer conforms to the Rules of Professional Conduct.

***19** (c) A lawyer shall be responsible for another lawyer's violation of the Rules of Professional Conduct if:

(1) the lawyer orders or, with knowledge of the specific conduct, ratifies the conduct involved; or

(2) the lawyer is a partner or has comparable managerial authority in the law firm in which the other lawyer practices, or has direct supervisory authority over the other lawyer, and knows of the conduct at a time when its consequences can be avoided or mitigated but fails to take reasonable remedial action.

UpRight's supervision of Augustus was totally inadequate. UpRight has various supervisory lawyers who were expected to ensure client satisfaction. On multiple occasions, UpRight representatives promised **Banks** that her complaints would be escalated. The supervisory lawyers were either unable or unwilling to address the issues in **Banks**' case. By their lack of action, the managing attorneys in the Chicago office ratified Augustus's conduct. Still further, with regard to Augustus, the managing partners had supervisory authority over her practice. Many of the errors and negligence in this case could have been avoided if they had taken action.

11 U.S.C. § 528 requires bankruptcy attorneys execute a written contract and to provide such contract to their clients. This Court has already noted that **Banks**' retainer agreement with UpRight was signed by a lawyer not licensed in Louisiana. In fact, the lawyer did not even see it or physically sign it. Cynthia Tannert's electronic signature is affixed to the retainer agreement by the notation of a /s/Cynthia Tannert. Tannert a “partner” with UpRight, has given permission for UpRight to sign her name to these contracts without notice. This does not comply with the requirements of the Bankruptcy Code. **Banks** never had a written contract with UpRight executed by a Louisiana licensed lawyer.

Pursuant to 11 U.S.C. § 329 and Fed. R. Bankr. P. Rule 2017, disgorgement in this case is appropriate. Section 329(b)(2) of the Bankruptcy Code provides that a court may order disgorgement of fees if attorney compensation exceeds the reasonable value of the services provided. Further, Bankruptcy Rule 2017 provides the following: "[o]n motion by any party in interest or on the court's own initiative, the court after notice and a hearing may determine whether any payment of money or any transfer of property by the debtor, made directly or indirectly and in contemplation of the filing of a petition under the Code...to an attorney for services rendered or to be rendered is excessive." The Court finds no value in the services UpRight provided to **Banks**. To the contrary, UpRight's actions harmed **Banks** by causing her to file two bankruptcies instead of one, and allowing a judgment to be entered against **Banks** when such judgment could have been avoided. In both bankruptcy cases, Augustus failed to submit basic required documents t, despite **Banks** having provided her those same documents. When the proceedings were dismissed, Augustus and UpRight failed to correct the mistakes in either proceeding and failed to communicate with **Banks** for months at a time. In this case, Augustus filed identical schedules and statements to those filed in the first case, with no updated financial information and without **Banks** having reviewed or signed them.

***20** While Augustus bears responsibility for her failures, UpRight took no effective action to aid **Banks**. UpRight took no action even though **Banks** had apprised them constantly of the issues in her case. The contract UpRight provided **Banks** stated that "[c]lient retains Firm, (and not any specific attorney/staff member) to represent Client for Chapter 7 Bankruptcy Services." This contract indicates that UpRight should have been responsible for proper representation.

Disgorgement is appropriate under 11 U.S.C. § 526(c)(1). That section provides that "any contract for bankruptcy assistance between a debt relief agency and an assisted person that does not comply with the material requirements of [11 U.S.C. §§ 526, 527, or 528] shall be void and may not be enforced...other than [by] such assisted person." Under 11 U.S.C. § 528, a debt relief agency must "execute a written contract" with a client not less than five days after first providing bankruptcy assistance services and provide the assisted person with a copy of the fully executed and completed contract. Here, **Banks**' contract bears the electronic signature of Cynthia Tannert. Ms. Tannert is a Tennessee attorney who is not licensed to practice in Louisiana and and has never had any contact with **Banks** and never physically signed any contract with her. Thus, the signature on the **Banks** contract is false, and the contract is fraudulent. Even assuming Ms. Tannert had actually signed the contract, she is not licensed to practice law in Louisiana and had no ability to ensure UpRight followed through on its agreement to serve **Banks**. Moreover, UpRight and Augustus never executed a contract with **Banks**, despite Augustus having filed her two bankruptcy cases. As a result, no one from UpRight ever executed a contract with **Banks**. UpRight failed to provide **Banks** a properly executed copy of a written contract between them. This is in violation of 11 U.S.C. §§ 528(a)(1) and (2), so the contract is void and UpRight must disgorge all fees collected as provided by 11 U.S.C. § 526(c)(1).

Relief pursuant to 11 U.S.C. §§ 526(c)(5) and 105 is also appropriate. Section 526(c)(5) provides that upon a finding that "a person intentionally violated this section, or engaged in a clear and consistent pattern or practice of violating this section, the court may...enjoin the violation of such section;...or...impose an appropriate civil penalty against such person." Section 526(a)(1) provides the following:

> (a) A debt relief agency shall not—
>
> (1) fail to perform any service that such agency informed an assisted person or prospective assisted person it would provide in connection with a case or proceeding under this title: ...
>
> (2) make any statement, or counsel or advise any assisted person or prospective assisted person to make a statement in a document filed in a case or proceeding under this title, that is untrue or misleading or that upon the exercise of reasonable care, should have been known by such agency to be untrue or misleading;
>
> (3) misrepresent to any assisted person or prospective assisted person, directly, or indirectly, affirmatively or by material omission, with respect to—
>
> (A) the services that such agency will provide to such person: or
>
> (B) the benefits and risks that may result if such person becomes a debtor in a case under this title...

In this case, UpRight promised to provide **Banks** an array of bankruptcy services. UpRight has repeatedly failed to provide those services or misrepresented those services. UpRight's continued failure to provide **Banks** with bankruptcy services after numerous requests for help amounts to an intentional violation of 11 U.S.C. § 526(a)(1). UpRight's apparent disregard seems to reflect a business model in which this Chicago based corporation is primarily a marketer of legal services, not a provider of them. UpRight has never provided **Banks** any real service, beyond the detrimental step of referring her to Augustus. Violations of 11 U.S.C. § 526(a) are actionable under 11 U.S.C. § 526(c)(5), which provides that the Court may enjoin the violation of such section or impose an appropriate civil penalty.

**21* The UST and UpRight have agreed to the following sanctions for UpRight:

(a.) Disgorging of all fees paid by **Banks**.

(b.) Refunding $30 representing sums **Banks** paid for credit counseling.

(c.) A civil penalty in the amount of $5,000.00 paid to the United States Treasury.

CONCLUSION

The Court approves the sanctions agreement between the UST and UpRight. The Court finds that UpRight has previously disgorged to **Banks** all fees that she paid. However, the Court will also impose the following sanctions and requirements.

IT IS ORDERED that UpRight refund to **Banks** the sum of $30.00 no later than 14 days after this order is entered. This represents the sums **Banks** paid for credit counseling.

IT IS FURTHER ORDERED that UpRight pay a civil penalty of $5,000.00 payable to the United States Treasury c/o Richard H. Drew, Office of the United States Trustee, 300 Fannin St. Suite 3196, Shreveport, Louisiana 71101. UpRight shall make this payment no later than 14 days after this order is entered.

IT IS FURTHER ORDERED that, pursuant to Local Civil Rule LR83.2.10, the Court suspends attorney Andrea Augustus from the practice of law in the United States Bankruptcy Court for the Western District of Louisiana effective on the date this order is entered for a period of 90 days. The Court stresses this suspension is appropriate due to her negligent handling of **Banks**' case and her violations of the Louisiana Code of Professional Responsibility.

IT IS FURTHER ORDERED that, pursuant to Local Civil Rule LR83.2.10, the Court suspends UpRight Law, LLC from filing any bankruptcy case in the Western District of Louisiana effective on the date this order is entered for a period of 90 days. This suspension includes any of UpRight's partner attorneys. The Court stresses this suspension is appropriate due to UpRight's negligence in representing **Banks**, its failure to adequately supervise Augustus, and its violations of the Louisiana Code of Professional Responsibility. However, partner attorneys who maintain separate legal practices may continue to file bankruptcy cases for those clients not contracted with or represented by UpRight. Partner attorneys may also participate in any bankruptcy cases filed by UpRight prior to the entry of this order.

IT IS FURTHER ORDERED that Andrea Augustus's electronic filing privileges are suspended in all divisions of the United States Bankruptcy Court for the Western District of Louisiana. This suspension is due to her violations of the rules for the electronic filing of documents and pleadings in this district pursuant to the Administrative Procedures for the U.S. Bankruptcy Court for the Western District of Louisiana (“Administrative Procedures”), last amended March 18, 2014. By signing **Banks**' name to a bankruptcy petition and schedules she did not sign, Augustus is in violation of these rules. Augustus may petition this Court for reinstatement of her electronic filing privileges after she completes fifteen hours of bankruptcy specific continuing legal education.

IT IS FURTHER ORDERED that UpRight Law, LLC may not accept any payment from any Western District of Louisiana residents who have not had a thorough and adequate consultation with an attorney that is licensed to practice in this District and is able to represent them.

22* **IT IS FURTHER ORDERED that UpRight Law, LLC contracts or retainer agreements must conform to Louisiana Rule of Professional Conduct 1.5(f)(5). All contracts between UpRight and residents of the Western District of Louisiana must contain the following language in bold, 12 point type:

> **The Louisiana Rules of Professional Conduct require that when a client pays a lawyer a fixed fee, a minimum fee or a fee drawn from an advanced deposit, and a fee dispute arises between the lawyer and the client, either during the course of the representation or at the termination of the representation, the lawyer shall immediately refund to the client the unearned portion of such fee, if any. If the lawyer and the client disagree on the unearned portion of such fee, the lawyer shall immediately refund to the client the amount, if any, that they agree has not been earned, and the lawyer shall deposit into a trust account an amount representing the portion reasonably in dispute. The lawyer shall hold such disputed funds in trust until the dispute is resolved, but the lawyer shall not do so to coerce the client into accepting the lawyer's contentions. As to any fee dispute, the lawyer should suggest a means for prompt resolution such as mediation or arbitration, including arbitration with the Louisiana State Bar Association Fee Dispute Program.**

IT IS FURTHER ORDERED that the interim relief this Court previously entered (ECF No. 35) is made permanent. **ACCORDINGLY, IT IS ORDERED** that attorneys acting on behalf of UpRight Law LLC and its affiliates are immediately prohibited from filing any document electronically signed by a client (i.e., using the /s/ notation for a signature). All documents UpRight Law LLC and its partner attorney's file in the Western District of Louisiana containing a client signature must have a scanned original signature. This order applies to all bankruptcy cases filed by UpRight Law LLC and its affiliates in the Western District of Louisiana.

IT IS FURTHER ORDERED that every employment contract for debt relief services between UpRight Law LLC and its clients must contain the original "wet" signatures of both the client and the UpRight Law LLC attorney licensed in the Western District of Louisiana. The attorney who executes that contract shall be designated as the attorney in charge of that case. Further, UpRight Law LLC and its affiliates may not accept a retainer from any client before an employment contract is executed. This order applies with respect to UpRight Law LLC and its affiliates and any of their prospective clients residing in or anticipating filing bankruptcy in the Western District of Louisiana.

IT IS FURTHER ORDERED that every attorney affiliated with UpRight Law LLC and its affiliates filing a pleading within the Western District of Louisiana on behalf of those entities must contact the clerk of court and update their CM/ECF account or create a duplicate account so that the docket in each case accurately reflects their firm's name as UpRight Law LLC.

SO ORDERED.

All Citations

Slip Copy, 2018 WL 735351

Footnotes

1 The Court treats a Motion to Reinstate as a Motion to Vacate the Dismissal Order. Technically, there is no such motion as a Motion to Reinstate a dismissed bankruptcy case.

2 The case was dismissed *sua sponte* for failure to comply with 11 U.S.C. § 521.

3 The "rest of the story" is a quote from a radio program hosted by Paul Harvey. The broadcasts always concluded with the tag line "and now you know the rest of the story."

4 The Fair Debt Collection Practice Act (FDCPA) 15 U.S.C. § 1692. Aggrieved consumers may also file a private lawsuit in a state or federal court to collect damages (actual, statutory, attorney's fees, and court costs) from third-party debt collectors.

5 The Court notes that the individual mentioned here is named Cynthia Tannert, even though the transcript indicates her name is Cynthia Tanner.

6 Unbundled legal services, also known as limited scope representation and discrete task representation, is a practice in bankruptcy cases in which an attorney attempts to limit the scope of the attorney's involvement in the case. This Court permits "unbundling" for legal services in Chapter 7 cases for adversary proceedings; however, it requires debtor's counsel must represent the debtor, without exception, for all legal services from case filing to discharge, **or** the date a discharge order would have been entered if a complaint under 11 U.S.C. § 727 is filed in the main bankruptcy case.

7 As of June 1, 2017, Ms. Augustus was ineligible to practice law in Louisiana for failure to fulfill continuing legal education requirements and failure to pay bar dues. She has since restored her eligibility.

8 The Court notes that Louisiana does not have counties, but rather parishes.

9 This appears to be an abbreviation for "Partner Attorney."

10 The automatic stay is an injunction that halts actions by creditors, with certain exceptions, to collect debts from a debtor who has declared bankruptcy. Under Section 362 of the United States Bankruptcy Code, the stay begins at the moment the bankruptcy petition is filed. In a Chapter 7, the stay terminates at dismissal, when a case is closed, or the time a discharge is granted or denied.

11 Credit counseling certificates expire after 180 days. 11 U.S.C. § 109(h).

12 The picture ID and Social Security card are required by Local Bankruptcy Rule 1002–1.

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extravagant or disproportionate to the damages Jesmer would suffer from a default triggering the liquidated damages provision that it functions as a punishment rather than compensation. However, facts not in material dispute fail to establish whether Jesmer is entitled to the attorneys' fees component of her claim. The Court will, therefore, deny summary judgment with respect to the attorneys' fees included in Jesmer's claim. The Court will enter a separate order consistent with this Memorandum Opinion.

IN RE: Roberta Ellarae WRIGHT, Debtor.

In re: Ian Gomes and Stephanie Ann Gomes, Debtors.

In re: Brittany Marie Dirkswager, Debtor.

In re: Ryan Michael Brown, Debtor.

In re: Tommy Lenard Guthrie and Debra Denise Guthrie, Debtors.

In re: Kiley Gene Lawrence, Debtor.

In re: Michael Joe Lawson and Sara Lynne Lawson, Debtors.

In re: Karen Dawn Inman, Debtor.

In re: David Charles Williams, Debtor.

In re: Daphne Leannette Robitaille, Debtor.

In re: Kimberly Leann Sullivan, Debtor.

In re: Brett Wayne Murphy and April Irene Conder, Debtors.

In re: Daniel Bruce Bowers and Janie Mae Bowers, Debtors.

In re: Dale Daniel Burris, Jr. and Sheila Mae Burris, Debtors.

In re: Darin Dwane Miller and Kathy Jo Miller, Debtors.

In re: Kenneth Charles Burton, Debtor.

In re: Kirby Dwayne Smith and Rebecca Leann Smith, Debtors.

Case No. 17-11936-M, Case No. 17-11172-M, Case No. 17-11410-M, Case No. 17-11411-M, Case No. 17-11555-M, Case No. 17-11557-M, Case No. 17-11558-M, Case No. 17-11559-M, Case No. 17-11688-M, Case No. 17-11689-M, Case

No. 17-11690-M, Case No. 17-11930-M, Case No. 17-11932-M, Case No. 17-11933-M, Case No. 17-12027-M, Case No. 17-12028-M, Case No. 17-12029-M

United States Bankruptcy Court,
N.D. Oklahoma.

Signed September 4, 2018.

Background: United States Trustee filed motion for review of transactions between debtors and attorney who had agreed to represent them and for imposition of possible sanctions against attorney, inter alia, for violating his fee disclosure obligations.

Holdings: The Bankruptcy Court, Terrence L. Michael, Chief Judge, held that:

(1) attorney violated his fee disclosure obligations under bankruptcy statute and rule;

(2) attorney not only violated fee disclosure requirements, but committed a fraud on his clients and on court; and

(3) as sanction, bankruptcy court would require disgorgement of all postpetition fees.

Ordered accordingly.

1. Bankruptcy ⚷3179

Fee disclosure obligations imposed on debtor's attorney by bankruptcy statute and rule apply regardless of whether the attorney applies for compensation from bankruptcy estate. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

2. Bankruptcy ⚷3179

Fee disclosure obligations imposed on debtor's attorney are mandatory, not permissive. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

3. Bankruptcy ⚷3179

Fee disclosure obligations imposed on debtor's attorney are designed to prevent bankruptcy attorneys from extracting more than their fair share from prospective debtors willing to do whatever is necessary to obtain their counsel of choice and avoid unfavorable bankruptcy proceedings. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

4. Bankruptcy ⚷3179

Bankruptcy counsel's fee revelations must be direct and comprehensive; coy or incomplete disclosures which leave the court to ferret out pertinent information from other sources are insufficient. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

5. Bankruptcy ⚷3179

Absent complete disclosure, bankruptcy court is unable to make an informed judgment regarding the nature and amount of compensation paid or promised by debtor for legal services in contemplation of bankruptcy. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

6. Bankruptcy ⚷3179

Consequences of failure on part of debtor's attorney to comply with his or her fee disclosure obligations can be severe, including forfeiture of right to receive any compensation for services rendered to debtor. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

7. Bankruptcy ⚷3179

Disgorgement of fees due to inadequate fee disclosure by debtor's counsel is a matter left to sound discretion of bankruptcy court. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

8. Bankruptcy ⚷3179

Entry of fee disgorgement order due to attorney's violation of fee disclosure obligations should be commensurate with the egregiousness of the violation and will depend on the particular facts of each case. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

9. Bankruptcy ⚷3179

Court may sanction attorney's failure to make proper fee disclosure regardless of actual harm to the estate. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

10. Bankruptcy ⚷3179

That debtor's attorney acted with a pure heart, and without any subjective intent to violate his fee disclosure obligations under bankruptcy statute and rule, is no defense to his failure to make the proper disclosures. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

11. Bankruptcy ⚷3179

Negligent or inadvertent omissions do not vitiate a failure on part of debtor's attorney to properly disclose his or her fees. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

12. Bankruptcy ⚷3179

Debtors' attorney violated his fee disclosure obligations under bankruptcy statute and rule by sloppily disclosing in inaccurate amounts the fees which he had collected, by treating fees that his clients had agreed to pay as the fees that he had agreed to accept despite fact that, based on attorney's factoring agreement with collection agency that would retain a portion of any fee, he had actually agreed to accept hundreds of dollars less from each client, and by not disclosing this fee sharing arrangement with collection agency. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

13. Bankruptcy ⚷3179

Debtors' attorney had duties of competence to his clients that transcended bankruptcy law, and he could not lay the blame for his inaccurate fee disclosures on the loss of his long-time assistant and his difficulties in training a new one. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

14. Bankruptcy ⚷3179

Conduct of debtors' attorney in offering to make available upon request the factoring agreement pursuant to which he shared fees with collection agency did not satisfy his obligation pursuant to Bankruptcy Rule to disclose "the particulars of any such sharing or agreement to share." Fed. R. Bankr. P. 2016(b).

15. Attorney and Client ⚷14, 32(14)

Attorney becomes officer of the court upon taking an oath and meeting other requirements imposed by state law, and as officer of court, has duty to show complete candor toward that tribunal. 5 Okla. Stat. Ann. § 2.

16. Attorney and Client ⚷114

Bankruptcy ⚷3179

By adopting bifurcated approach to fees, pursuant to which attorney had his clients enter into two separate retainer agreements, one for preparing and filing bare bones petition to which he would allocate whatever portion of agreed fee his clients could afford to pay up front, and a second postpetition agreement for continuing his representation after petition was filed, thereby rendering whatever fees could not be paid up front nondischargeable and collectable by agency that factored attorney's accounts, as well as by his failure to disclose payments that he received from agency pursuant to this factoring arrangement, attorney not only violated fee disclosure requirements, but committed a fraud on his clients and on court. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

17. Bankruptcy ⚷3022

Bankruptcy system is a fragile one, built on the principles of full and candid disclosure.

18. Bankruptcy ⚷3179

As sanction for attorney's violation of his fee disclosure obligations in connection with undisclosed factoring arrangement with agency from which he secretly received a large portion of his fees, and whose collection of fees from clients he facilitated by employing a bifurcated retention/billing system that had the effect of rendering, as postpetition fees not dischargeable in bankruptcy, whatever fees his clients could not afford to pay up front, bankruptcy court would require disgorgement of all such postpetition fees, and would find that postpetition retention agreements were void and unenforceable either by attorney or factoring agency. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016(b).

19. Bankruptcy ⚷2128, 3179

While attorney violated Bankruptcy Rule governing the payment of court filing fee in installments, which required debtors who elected to pay the filing fee in installments to complete their installment payments prior to making any further payment for legal services to their bankruptcy counsel or anyone else, by entering into factoring arrangement that he should have realized would result in collection activity by factor and payments to it before filing fees were fully paid, bankruptcy court would not impose any additional sanctions beyond those imposed for attorney's fee disclosure violations, where all required court filing fees were eventually fully paid, either by debtors or attorney, and each of the debtors received their discharge. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 1006, 2016(b).

J. Ken Gallon, Law Office of J. Ken Gallon, Miami, OK, for Debtor.

Katherine Vance, U.S. Trustee, Tulsa, OK, for U.S. Trustee.

Memorandum Opinion

TERRENCE L. MICHAEL, CHIEF JUDGE

"*. . ., but at the length truth will out.*"[1]

It is an oft-stated maxim that attorneys are "officers of the court." What exactly does it mean to be an "officer of the court?" Is it enough for an attorney to obtain a desired result for his or her client, even if they mislead, fail to fully inform, or violate rules of the Court in the process? Is a United States Bankruptcy Court a place where, when it comes to the areas of attorney conduct and non-disclosure, no harm equals no foul? Does ignorance of the law excuse misconduct? All of these questions are raised in the seventeen cases presently before the Court. For each question, the answer is the same: absolutely, unequivocally, no.

Before the Court is the Motion for Review of Debtor's Transactions with J. Ken Gallon, Attorney (the "Motion"),[2] filed in Case No. 17-11936-M, *Roberta Ellarae Wright*, by Katherine Vance, on behalf of the United States Trustee ("UST"), and 17 contested matters initiated *sua sponte* by the Court in each of the above captioned cases (the "Captioned Cases").[3] Because the matters are based on substantially identical facts and raise identical issues regarding the conduct of J. Ken Gallon

1. William Shakespeare, *The Merchant of Venice* act 2, sc. 2.

2. Case No. 17-11936-M, *at Docket No. 38*.

3. Although not all of the Captioned Cases were originally assigned to the undersigned Judge, they were transferred to him after the facts described herein came to light, so that counsel's conduct could be reviewed by the Court in a comprehensive manner.

("Gallon"), counsel for debtors in each of these cases, they were consolidated for purposes of resolution.[4] The matters discussed herein were first brought to the Court's attention in the *Wright* case, and the Court will continue to treat it as the lead case. A hearing on the Motion and these contested matters was held on May 10, 2018, at which the Court heard argument and took evidence related to the conduct of Gallon in these cases. The following findings of fact and conclusions of law are made pursuant to Federal Rule of Bankruptcy Procedure 7052, made applicable to this contested matter by Federal Rule of Bankruptcy Procedure 9014.[5]

Jurisdiction

The Court has jurisdiction over these bankruptcy cases pursuant to 28 U.S.C.A. § 1334(b).[6] Reference to the Court of these bankruptcy cases is proper pursuant to 28 U.S.C.A. § 157(a). Matters concerning the administration of the estate are core proceedings as defined by 28 U.S.C.A. § 157(b)(2)(A).

Findings of Fact

1. The BK Billing Model

Gallon is a consumer debtors' attorney based in Miami, Oklahoma. BK Billing, LLC ("BK Billing"), a Utah limited liability company, is a finance company that provides factoring services to bankruptcy counsel in Chapter 7 cases. On May 11, 2017, Gallon executed an Accounts Receivable Assignment Agreement (the "AR Agreement"), in which he established a factoring arrangement with BK Billing.[7] The AR Agreement set up a mechanism where Gallon would sell his accounts receivable for "post-petition services" to Chapter 7 consumer debtors based on client contracts that he uploaded to the BK Billing system. Gallon ultimately factored, or sold, 14 client contracts to BK Billing under the AR Agreement ("the BK Billing Cases"). Under the original AR Agreement, Gallon agreed to transfer each account receivable in exchange for 70% of the total contractual value of the account, which amount was to be received by Gallon with 2-3 business days.[8] An amendment executed on July 5, 2017, increased the total amount paid to Gallon upon the submission of an account to 75% of the value of the contract, but lowered the amount immediately available to Gallon to 60%, and set the other 15% aside in an escrow account to be maintained by BK Billing as security for performance of the transferred accounts.[9] The AR Agreement gives BK Billing the "right to approve of [Gallon's] form engagement agreement prior to accepting any [accounts]."[10] In addition,

4. *See* Order Scheduling Hearing and Directing Counsel for the Debtor to Address Issues of Compensation, Case No. 17-11936-M, *at Docket No. 60*. An Order and Notice of Hearing was entered in each of the other Captioned Cases, alerting each debtor to their opportunity to appear and be heard in this matter.

5. The Court will recite the factual differences for each specific case, but notes that those differences are immaterial to the Court's analysis and resolution of these matters.

6. Unless otherwise noted, all statutory references are to sections of the United States Bankruptcy Code, 11 U.S.C.A. § 101 *et seq.* Unless otherwise noted, all references to a "Rule" or "the Rules" are to the Federal Rules of Bankruptcy Procedure.

7. Trial Ex. 22.

8. *Id.* at 1, § 1.

9. Trial Ex. 23 at 1, § 2.1. Except for Case No. 17-11172-M, *Gomes*, all of the BK Billing Cases were submitted pursuant to the amended AR Agreement. All further references to the AR Agreement will refer to the agreement as amended.

10. Trial Ex. 22 at 2, § 4.2.

Gallon is obligated to "cooperate with the collections by BK Billing of the [accounts], including, but not limited to providing evidence reasonably required for any legal action, arbitration, or mediation instituted by BK Billing for collection purposes, and permitting BK Billing to use [Gallon's] name, address, and telephone number for collection purposes." [11]

In addition to the factoring services, BK Billing provided Gallon with various pleadings and templates to effectuate a business model whereby Gallon would enter two separate retention agreements with his clients. The first, executed prior to filing a Chapter 7 bankruptcy case, was for services up to and including filing the petition. The second, executed after the case was filed, was for all remaining services that were rendered to a debtor post-petition.

At a hearing in these matters, Gallon testified that upon meeting with a new client, if he determined that the client was in need of immediate bankruptcy relief but was unable to pay his fee prior to filing the case, Gallon would present them with the "BK Billing Model." [12] Key features of the BK Billing Model include:

A. The debtors entered into a "Contract for Pre-Petition Legal Services in a Chapter 7 Bankruptcy Case" (the "Pre-Petition Agreement") [13] with Gallon.[14]

B. Under the Pre-Petition Agreement, the debtors were to pay Gallon a specified fee [15] for various pre-petition bankruptcy services, including "meeting and consulting with [Gallon] as needed," a "detailed analysis of [ ] client questionnaire," and "preparation and filing of a Chapter 7 Voluntary Petition, Statement About Social Security Numbers[.]" [16] The debtors agreed to pay additional fees for a "Pre-filing Credit Counseling Briefing Certificate" and a credit report.

C. The Pre-Petition Agreement gave the debtors the option to pay the Bankruptcy Court filing fee of $335 in full up front, apply to pay it in installments, or request that Gallon pay the fee and seek reimbursement from the debtors at a later time.

D. The Pre-Petition Agreement stated that Gallon's contractual responsibilities would end "upon completion of the filing of [the] bankruptcy case." It also stated that "the Law Firm will remain professionally obligated to serve as counsel for Client in the case until the Bankruptcy Court allows the Law Firm to formally withdraw." [17]

E. The Pre-Petition Agreement laid out various options regarding the completion of the debtors' bankruptcy case through discharge. The debtors could 1) retain Gallon under a second retainer agreement to be

11. *Id.* at 3, § 4.4.

12. Gallon did not use this terminology, but the Court will use the term "BK Billing Model" to refer to the two contract bifurcated filing system provided by BK Billing, which included the factoring of Gallon's attorney fees.

13. *See, e.g.,* Trial Ex. 14.1 (*Wright*). Substantially similar agreements were entered with each of the debtors in the Captioned Cases.

14. In the contracts with debtors, Gallon represented himself as the "Law Firm." The Court will use the term "Gallon" to refer to both J. Ken Gallon, as attorney, and any law firm he may represent.

15. This amount varied by debtor. Details for each debtor are discussed in the next section.

16. Trial Ex. 14.1 at 1.

17. *Id.*

executed post-petition, where Gallon would complete the case for an additional specified fee;[18] 2) seek other counsel to complete the case; or 3) proceed without legal representation, i.e., *pro se*. If the debtors did not choose to retain Gallon for post-petition services within 10 days after filing the bankruptcy petition, they agreed to consent to Gallon's withdrawal as counsel in the case. The Pre-Petition Agreement also placed the responsibility on the debtors to notify their creditors once the bankruptcy case was filed.

F. After execution of the Pre-Petition Agreement, Gallon filed what is colloquially referred to as a "barebones" Chapter 7 petition on behalf of the debtors. That means the documents filed represent the bare minimum necessary to successfully open a bankruptcy case and invoke the automatic stay. In all cases, this consisted of Official Form 101, Voluntary Petition for Individuals Filing for Bankruptcy, required by Rule 1002(a); a Certificate of Counseling, required by Rule 1007(b)(3)(A); a list of creditors, required by Rule 1007(a)(1); and a Verification as to Official Mailing Matrix, required by Rule 1008.[19] In the seven cases filed prior to August 24, 2017, the initial filing also included Official Form 106Sum, Summary of Your Assets and Liabilities and Certain Statistical Information, required by Bankr. N.D. Okla. Local Rule 1007-1(G); Official Form 106D, Schedule D: Creditors Who Have Claims Secured by Property, required by Rule 1007(b)(1)(A); Official Form 106E/F, Schedule E/F: Creditors Who Have Unsecured Claims, required by Rule 1007(b)(1)(A); and Official Form 106Dec, Declaration About an Individual Debtor's Schedules, required by Rule 1008.[20]

G. In eleven of the seventeen Captioned Cases, Gallon filed Bankruptcy Form 103A, Application for Individuals to Pay the Filing Fee in Installments (the "Installment Application"), on behalf of the debtors, requesting that they be allowed to pay the Court filing fee in installments of $83.75 per month for four months, beginning one month from the date the petition was filed. At the time the Installment Application was filed in each case, the Court had no information regarding the financial condition of the debtors, i.e., no schedules of current income or expenditure had been filed.

H. In each of the BK Billing Cases, Gallon and the debtors executed a "Contract for Post-Petition Legal Services in a Chapter 7 Bankruptcy Case" (the "Post-Petition Agreement").[21] In the Post-Petition Agreement, the debtors agreed to retain Gallon to represent them in the post-petition proceedings of their bankruptcy case in exchange

18. *See supra* note 15. As far as the Court is aware, all of the debtors that executed a Pre-Petition Agreement chose this option.

19. The *Sullivan* case included this list of documents plus the Official Form 106Sum, Summary of Your Assets and Liabilities and Certain Statistical Information, required by Bankr. N.D. Okla. Local Rule 1007-1(G).

20. These cases were *Gomes*, *Dirkswager*, *Brown*, *Inman*, *Lawrence*, *Guthrie*, and *Lawson*.

21. Trial Ex. 14.2.

for a specified fee,[22] described as a non-refundable flat fee. Gallon agreed to perform the following services for debtors:

1) Preparation and filing of the Statement of Financial Affairs and Schedules;

2) Preparation for and attendance at the Section 341 Meeting of Creditors;

3) Review and attendance (if necessary) to motions for stay relief;

4) Review of any redemption agreements;

5) Review of any reaffirmation agreements;

6) Follow through with case administration and monitoring;

7) File motions to reopen (if necessary)[.] [23]

I. The Post-Petition Agreement included the following statements:

I acknowledge and agree that as all of these fees are for post-petition services, they are not dischargeable in my Chapter 7 case. In the event of nonpayment of the agreed-upon fees, the Law Firm may commence legal proceedings for collection.

I understand that the Law Firm may assign my post-petition accounts receivable to BK Billing, LLC. I authorize the Law Firm or BK Billing to communicate with me via e-mail, text, and/or telephone. I explicitly give my consent to the Law Firm to share my client file information with BK Billing, including my contact information and social security number. I acknowledge that my payments to BK Billing will be reported to credit bureaus. I acknowledge that on-time payments can help my credit and late payments can hurt my credit. I have been provided an opportunity to ask the Law Firm questions regarding the Law Firm's accounts receivable assignment agreement with BK Billing. The Law Firm has answered all such questions to my satisfaction.

I agree to submit to the personal jurisdiction of the Oklahoma courts with respect to such action, and Oklahoma law will apply. If such collection procedures shall become necessary, I agree to pay all reasonable costs of such collection, including reasonable attorney fees.

I understand that I am to notify my creditors of my bankruptcy case once my case is filed.[24]

J. Attached to the Post-Petition Agreement was a "Recurring Payment Authorization and Consent Form" in which the debtors authorized Gallon or BK Billing, LLC, referred to as an "independent billing company," to charge their debit card a specified fee per month until a specified amount was paid in full.[25] That form included the following statement:

I give my consent that the Law Firm may sell or factor the accounts receivable associated with my contract to BK Billing. I acknowledge my payments would then be made directly to BK Billing on behalf of the Law Firm. I authorize the Law Firm or BK Billing to communicate with me via mail, e-mail, text, and/or telephone. I give

22. *See supra* note 15.

23. Trial Ex. 14.2 at 1.

24. *Id.* at 2–3 (emphasis added). The last sentence was included in each of the Post-Petition Agreements, but it was set out separately in bold and underlined, with instruction for the debtor to initial the clause, only in the *Wright* case.

25. *See supra* note 15.

my consent for the Law Firm to share my client file information, including my Social Security Number, with BK Billing for the purpose of processing and reporting my payments. I acknowledge that my payments may be reported to the Credit Bureaus. I acknowledge that on-time payments may help my credit and late payments may hurt my credit.[26]

K. In all of the Captioned Cases, Gallon filed the remaining schedules and statements required by § 521 and Rule 1007(b) sometime after the petition date.

L. Among the documents filed post-petition in each case was a Disclosure of Compensation of Attorney for Debtor ("Disclosure of Compensation"), which indicated that Gallon had agreed to accept a specified fee [27] "for services rendered or to be rendered on behalf of the debtor(s) in contemplation of or in connection with the bankruptcy case." [28] Gallon stated that he had received a specified fee [29] prior to filing the statement, leaving a specified balance due.[30] In every case, he checked the box next to the statement "I have not agreed to share the above-disclosed compensation with any other person unless they are members and associates of my law firm." Gallon also indicated that "by agreement with the debtor(s), the above-disclosed fee does not include the following service: 1) Lien Avoidance; 2) Adversary Proceeding; 3) Judgment Lien Removal; 4) Re-Affirmation (sic) Agreement; 5) Re-Affirmation (sic) Agreement Recession; 6) Amendment to Peition (sic), Schedules and Statements; 7) Objection to Discharge." [31]

2. The debtors

The facts in each of the Captioned Cases are as follows:

a. BK Billing Cases

Roberta Ellarae Wright, Case No. 17-11936-M

On September 12, 2017, Roberta Ellarae Wright ("Wright") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $200 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report.[32] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,350. Wright's case, Case No. 17-11936-M, was filed on September 28, 2017. On October 5, 2017, Wright executed a Post-Petition Agreement, where she agreed to pay $1,425 as a flat fee for Gallon to represent her in the completion of the case.[33] No receipt was offered to show the amount received by Gallon. What appears to be an internal information sheet was offered to show that Gallon received $200 from Wright.[34] Under the AR Agreement, Gallon received $855 from BK Billing upon submission of the Wright account, with an additional $213.75 placed in

26. *Motion,* Case No. 17-11936-M*, at Docket No. 38* at 9.

27. *See supra* note 15.

28. Bankruptcy Form 2030.

29. *See supra* note 15.

30. *Id.*

31. Trial Ex. 14.5.

32. Trial Ex. 14.1.

33. Trial Ex. 14.2.

34. Trial Ex. 14.3.

escrow.[35] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $75; leaving a balance due of $1,425.[36] Wright's Statement of Financial Affairs ("SOFA") disclosed that she had paid Gallon $125 (date not indicated), and included the description "Prepare petition schedules & Statements, credit counseling, credit report." [37] Gallon filed an Installment Application on behalf of Wright.[38] The final installment of Wright's filing fee was paid on December 6, 2017. BK Billing collected $118.75 from Wright on October 15, 2017, a date before the filing fee was paid in full.[39]

Ian Gomes and Stephanie Ann Gomes, Case No. 17-11172-M

On June 12, 2017, Ian Gomes and Stephanie Ann Gomes (the "Gomeses") retained Gallon under a Pre-Petition Agreement, where they agreed to pay $100 for pre-petition services in a Chapter 7 bankruptcy case.[40] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in post-petition proceedings for $1,400. Their case, Case No. 17-11172-M, was filed on June 13, 2017. On that same date, the Gomeses executed a Post-Petition Agreement, where they agreed to pay $1,400 as a flat fee for Gallon to represent them in the completion of their case.[41] A receipt shows that Gallon received $500 in cash from Ian Gomes on June 12, 2017, which was described as a "Bankruptcy Retainer." [42] Under the original AR Agreement, Gallon received $980 from BK Billing upon submission of the Gomeses' account.[43] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[44] The Gomeses' SOFA disclosed they had paid Gallon $100 on June 12, 2017, and that "[t]he Debtors paid $100 dollars to prepare and to file the Petition, Credit Counseling, Creditors and Verification of Creditors. Debotrs [sic] paid $400 was for [sic] the Filing Fee, Credit Counseling Course, Debtors Education Course and the Credit Report." [45] The filing fee of $335 was paid on the filing date.

Ryan Michael Brown, Case No. 17-11411-M

On July 14, 2017, Ryan Michael Brown ("Brown") retained Gallon under a Pre-Petition Agreement, where he agreed to pay $158 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report.[46] The Pre-Petition Agreement gave him the option of retaining Gallon to complete his case in post-petition proceedings for $1,400. Brown's case, Case No. 17-11411-M, was filed on July 14, 2017. On July 24, 2017, Brown executed a Post-Petition Agreement, where he agreed to pay $1,350 as a flat fee for Gallon to represent him in the completion of the

35. Trial Ex. 14.4. This is based on an invoice amount of $1,425, which BK Billing was to collect from Wright.

36. Trial Ex. 14.6.

37. Trial Ex. 14.7.

38. Case No. 17-11936-M, *at Docket No. 4*.

39. Trial Ex. 14.4.

40. Trial Ex. 1.1.

41. Trial Ex. 1.2.

42. Trial Ex. 1.3.

43. Trial Ex. 1.4. *See supra* note 13.

44. Trial Ex. 1.6.

45. Trial Ex. 1.7.

46. Trial Ex. 2.1.

case.[47] A receipt shows that Gallon received $200 in cash from Brown on July 7, 2017, which was described as a "Attorney Fee's [sic] to file Petition; For CC CR." [48] Under the AR Agreement, Gallon received $810 from BK Billing upon submission of the Brown account, with an additional $202.50 placed in escrow.[49] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $150; leaving a balance due of $1,350. Brown's SOFA disclosed that he had paid Gallon $200 on July 11, 2017. Gallon filed an Installment Application on behalf of Brown.[50] The final installment of Brown's filing fee was paid on November 14, 2017. BK Billing collected $112.50 from Brown on September 15, 2017, September 29, 2017, and November 2, 2017, all dates before the filing fee was paid in full.[51]

Brittany Marie Dirkswager, Case No. 17-11410-M

Sometime in June 2017, Brittany Marie Dirkswager ("Dirkswager") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $1,400 for prepetition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[52] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Dirkswager's case, Case No. 17-11410-M, was filed on July 14, 2017. On July 19, 2017, Dirkswager executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[53] No receipt was offered to show the actual amount received by Gallon. Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Dirkswager account, with an additional $210 placed in escrow.[54] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[55] Dirkswager's SOFA disclosed that she had paid Gallon $150 on June 22, 2017, and that "[t]he Debtor paid $100 dollars to file the Petition, Credit Counseling Course, Creditors, Verification of Creditors. The Debtor paid $50 for the Credit Counseling Course and Credit Report." [56] Gallon filed an Installment Application on behalf of Dirkswager.[57] The final installment of Dirkswager's filing fee was paid on November 28, 2017. BK Billing collected $58.33 from Dirkswager on September 1, 2017, September 26, 2017, October 7, 2017, October 20, 2017, and November 10, 2017, all dates before the filing fee was paid in full.[58]

Tommy Lenard Guthrie and Debra Denise Guthrie, Case No. 17-11555-M

No Pre-Petition Agreement was offered to show when or the terms under which Tommy Lenard Guthrie and Debra Denise Guthrie (the "Guthries") retained Gallon. Their Chapter 7 bankruptcy case, Case

47. Trial Ex. 2.2.

48. Trial Ex. 2.3.

49. Trial Ex. 2.4.

50. Case No. 17-11411-M, *at Docket No. 2*.

51. Trial Ex. 2.4.

52. Trial Ex. 3.1. The Court hesitates to refer to the $1,400 as a ''typo'' because it was written into a blank by hand, but it does appear to be a mistake.

53. Trial Ex. 3.2.

54. Trial Ex. 3.4.

55. Trial Ex. 3.6.

56. Trial Ex. 3.7.

57. Case No. 17-11410-M, *at Docket No. 2*.

58. Trial Ex. 3.4.

No. 17-11555-M, was filed on August 4, 2017. On August 9, 2017, the Guthries executed a Post-Petition Agreement, where they agreed to pay $1,400 as a flat fee for Gallon to represent them in the completion of their case.[59] A receipt shows that Gallon received $500 by credit card from Debra Guthrie on July 28, 2017, which was described as "for payment of Bankruptc" [sic].[60] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Guthries' account, with an additional $210 placed in escrow.[61] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[62] The Guthries' SOFA disclosed that they had paid Gallon $500 (date not indicated), and included the description "Form 122, prepare petition & creditor matrix. pull credit report and credit counseling." [63] The filing fee of $335 was paid on the filing date.

Karen Dawn Inman, Case No. 17-11559-M

On July 5, 2017, Karen Dawn Inman ("Inman") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $1,400 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[64] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Inman's case, Case No. 17-11559-M, was filed on August 4, 2017. On August 8, 2017, Inman executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[65] A receipt shows that Gallon received $100 from Inman on July 6, 2017, which was described as "CR & CC for BK." [66] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Inman, with an additional $210 placed in escrow.[67] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[68] Inman's SOFA disclosed that she had paid Gallon $150 (date not indicated), and included the description "Credit Report, Credit Couseling [sic] and attorney fees." [69] Gallon filed an Installment Application on behalf of Inman.[70] The final installment of Inman's filing fee was paid on November 22, 2017. BK Billing collected $116 from Inman on September 1, 2017, October 1, 2017, and November 1, 2017, all dates before the filing fee was paid in full.[71]

Kiley Gene Lawrence, Case No. 17-11557-M

On August 1, 2017, Kiley Gene Lawrence ("Lawrence") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $100 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a

59. Trial Ex. 4.2.

60. Trial Ex. 4.3.

61. Trial Ex. 4.4.

62. Trial Ex. 4.6.

63. Trial Ex. 4.7.

64. Trial Ex. 5.1.

65. Trial Ex. 5.2.

66. Trial Ex. 5.3. The method of payment was not indicated.

67. Trial Ex. 5.4.

68. Trial Ex. 5.6.

69. Trial Ex. 5.7.

70. Case No. 17-11559-M, *at Docket No. 2*.

71. Trial Ex. 5.4.

credit report.[72] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Lawrence's case, Case No. 17-11557-M, was filed on August 4, 2017. On August 9, 2017, Lawrence executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[73] A receipt shows that Gallon received $153 in cash from Lawrence on August 1, 2017, which was described as "Attorney Fee's [sic] – BK." [74] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Lawrence account, with an additional $210 placed in escrow.[75] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[76] Lawrence's SOFA disclosed that she had paid Gallon $150 (date not indicated), and included the description "payment for credit report, credit counseling & fees." [77] Gallon filed an Installment Application on behalf of Lawrence.[78] The final installment of Lawrence's filing fee was paid on December 4, 2017. BK Billing collected $120 from Lawrence on September 6, 2017, October 6, 2017, and November 6, 2017, all dates before the filing fee was paid in full.[79]

Michael Joe Lawson and Sara Lynne Lawson, Case No. 17-11558-M

On July 27, 2017, Michael Joe Lawson and Sara Lynne Lawson (the "Lawsons") retained Gallon under a Pre-Petition Agreement, where they agreed to pay $40 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[80] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in post-petition proceedings for $1,400. Their Chapter 7 bankruptcy case, Case No. 17-11558-M, was filed on August 4, 2017. On August 15, 2017, the Lawsons executed a Post-Petition Agreement, where they agreed to pay $1,460 as a flat fee for Gallon to represent them in the completion of their case.[81] A receipt shows that Gallon received $100 in cash from Sara Lawson on July 27, 2017, which was described as "for BK [unreadable]." [82] Under the AR Agreement, Gallon received $876 from BK Billing upon submission of the Lawson account, with an additional $219 placed in escrow.[83] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $40; leaving a balance due of $1,460.[84] The Lawsons' SOFA disclosed that they had paid Gallon $100 (date not indicated), and included the description "prepare petition, e, f, creditor matrix and run credit report and credit counseling." [85]

72. Trial Ex. 6.1. Handwriting obscures the amount of $53 for a credit report on the exhibit submitted to the Court, but its intent in changing the meaning of the printed text is unclear.

73. Trial Ex. 6.2.

74. Trial Ex. 6.3.

75. Trial Ex. 6.4.

76. Trial Ex. 6.6.

77. Trial Ex. 6.7.

78. Case No. 17-11557-M, *at Docket No. 2*.

79. Trial Ex. 6.4.

80. Trial Ex. 7.1.

81. Trial Ex. 7.2.

82. Trial Ex. 7.3.

83. Trial Ex. 7.4.

84. Trial Ex. 7.6.

85. Trial Ex. 7.7.

Gallon filed an Installment Application on behalf of the Lawsons.[86] The final installment of the Lawsons' filing fee was paid on November 30, 2017. BK Billing collected $121.66 from the Lawsons on September 1, 2017, October 1, 2017, and November 1, 2017, all dates before the filing fee was paid in full.[87]

Kimberly LeAnn Sullivan, Case No. 17-11690-M

An undated and unexecuted Pre-Petition Agreement was offered as evidence that Kimberly LeAnn Sullivan ("Sullivan") retained Gallon, where she agreed to pay $110 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report.[88] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Sullivan's case, Case No. 17-11690-M, was filed on August 24, 2017. On August 25, 2017, Sullivan executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[89] A receipt shows that Gallon received $500 in cash from Sullivan on August 17, 2017, without further notation.[90] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Sullivan account, with an additional $210 placed in escrow.[91] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[92] Sullivan's SOFA disclosed that she had paid Gallon $500 (date not indicated), and included the description "prepare petition, verify creditors, pull credit report, credit counseling." [93] The filing fee of $335 was paid on the filing date.

David Charles Williams, Case No. 17-11688-M

On August 22, 2017, David Charles Williams ("Williams") retained Gallon under a Pre-Petition Agreement, where he agreed to pay $200 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report.[94] The Pre-Petition Agreement gave him the option of retaining Gallon to complete his case in post-petition proceedings for $1,300. Williams's case, Case No. 17-11688-M, was filed on August 24, 2017. On August 25, 2017, Williams executed a Post-Petition Agreement, where he agreed to pay $1,300 as a flat fee for Gallon to represent him in the completion of the case.[95] A receipt shows that Gallon received $600 in cash from Williams on June 23, 2017, which was described as "Attorney Fee's [sic] BK" [96] The receipt also shows an amount due of $1680, and a balance (due) of $1080. Under the AR Agreement, Gallon received $780 from BK Billing upon submission of the Williams account, with an additional $195 placed in escrow.[97] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $200;

86. Case No. 17-11558-M, *at Docket No. 2*.

87. Trial Ex. 7.4.

88. Trial Ex. 8.1. The document was executed by Gallon, but not by Sullivan.

89. Trial Ex. 8.2.

90. Trial Ex. 8.3.

91. Trial Ex. 8.4.

92. Trial Ex. 8.6.

93. Trial Ex. 8.7.

94. Trial Ex. 9.1.

95. Trial Ex. 9.2.

96. Trial Ex. 9.3.

97. Trial Ex. 9.4.

leaving a balance due of $1,300. Williams's SOFA disclosed that he had paid Gallon $600 (date not indicated), and included the description "prepare petition, creditor matrix and verification [sic], obtain credit report, filing fee and credit counseling." [98] The filing fee of $335 was paid on the filing date.

Daphne Leannette Robitaille, Case No. 17-11689-M

On August 1, 2017, Daphne Leannette Robitaille ("Robitaille") retained Gallon under a Pre-Petition Agreement, where she agreed to pay $100 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $33 for a credit report.[99] The Pre-Petition Agreement gave her the option of retaining Gallon to complete her case in post-petition proceedings for $1,400. Robitaille's case, Case No. 17-11689-M, was filed on August 24, 2017. On August 25, 2017, Robitaille executed a Post-Petition Agreement, where she agreed to pay $1,400 as a flat fee for Gallon to represent her in the completion of the case.[100] A receipt shows that Gallon received $150 in cash from Robitaille on August 1, 2017, which was described as "50 CC & CR & 100 [unreadable]." [101] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Robitaille account, with an additional $210 placed in escrow.[102] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[103] Robitaille's SOFA disclosed that she had paid Gallon $150 (date not indicated), and included the description "prepare petition, creditor verifcation [sic], credit report & credit counseling." [104] Gallon filed an Installment Application on behalf of Robitaille.[105] The final installment of Robitaille's filing fee was paid on December 18, 2017. BK Billing collected $116.66 from Robitaille on September 11, 2017, October 5, 2017, and November 5, 2017, all dates before the filing fee was paid in full.[106]

Daniel Bruce Bowers and Janie Mae Bowers, Case No. 17-11932-M

On September 22, 2017, Daniel Bruce Bowers and Janie Mae Bowers (the "Bowers") retained Gallon under a Pre-Petition Agreement, where they agreed to pay $500 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[107] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in post-petition proceedings for $1,400. Their Chapter 7 bankruptcy case, Case No. 17-11932-M, was filed on September 28, 2017. On September 29, 2017, the Bowers executed a Post-Petition Agreement, where they agreed to pay $575 as a flat fee for Gallon to represent them in the completion of their case.[108] A receipt

98. Trial Ex. 9.7.

99. Trial Ex. 10.1.

100. Trial Ex. 10.2.

101. Trial Ex. 10.3.

102. Trial Ex. 10.4.

103. Trial Ex. 10.6.

104. Trial Ex. 10.7.

105. Case No. 17-11689-M, *at Docket No. 3*. An amended application was filed at Docket No. 10 to change the due dates for payments. This amended application was later granted by the Court. *See Docket No. 16.*

106. Trial Ex. 10.4.

107. Trial Ex. 11.1.

108. Trial Ex. 11.2.

shows that Gallon received $1,000 in cash from Bruce Bowers on September 19, 2017, which was described as "Retainer for BK." [109] Under the AR Agreement, Gallon received $345 from BK Billing upon submission of the Bower account, with an additional $86.25 placed in escrow.[110] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $1,000; leaving a balance due of $500.[111] The Bowers' SOFA disclosed that they had paid Gallon $1,000 (date not indicated), and included the description "prepare petition schedules & statements, filing fee, credit counseling." [112] The filing fee of $335 was paid on the filing date.

Dale Daniel Burris, Jr. and Sheila Mae Burris, Case No. 17-11933-M

An undated and unexecuted Pre-Petition Agreement was offered as evidence that Dale Daniel Burris, Jr. and Sheila Mae Burris (the "Burrises") retained Gallon, where they agreed to pay $90 for prepetition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[113] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in postpetition proceedings for $1,410. Their Chapter 7 bankruptcy case, Case No. 17-11933-M, was filed on September 28, 2017. On September 29, 2017, the Burrises executed a Post-Petition Agreement, where they agreed to pay $1,400 as a flat fee for Gallon to represent them in the completion of their case.[114] No receipt was offered to show the actual amount received by Gallon. Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Burris account, with an additional $210 placed in escrow.[115] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,250; had received $0; leaving a balance due of $1,250.[116] The Burrises' SOFA disclosed that they had paid Gallon $150 (date not indicated), and included the description "Prepare petition, schedules & statements, credit report, credit counseling." [117] Gallon filed an Installment Application on behalf of the Burrises.[118] The final installment of the Burrises' filing fee was paid on November 27, 2017. BK Billing collected $58.34 from the Burrises on October 13, 2017, October 21, 2017, and November 4, 2017, all dates before the filing fee was paid in full.[119]

Brett Wayne Murphy and April Irene Conder, Case No. 17-11930-M

On September 28, 2017, Brett Wayne Murphy ("Murphy") and April Irene Conder ("Conder"), retained Gallon under a Pre-Petition Agreement, where they

109. Trial Ex. 11.3.

110. Trial Ex. 11.4.

111. Trial Ex. 11.6

112. Trial Ex. 11.7

113. Trial Ex. 12.1. The document was not executed by any party.

114. Trial Ex. 12.2.

115. Trial Ex. 12.4. This is based on an invoice amount of $1,400, which BK Billing was to collect from the Burrises.

116. Trial Ex. 12.6. On October 20, 2017, an amended Disclosure of Compensation was filed, which recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400. *See* Case No. 17-11933-M, *at Docket No. 18*.

117. Trial Ex. 12.7.

118. Case No. 17-11933-M, *at Docket No. 3*.

119. Trial Ex. 12.4.

agreed to pay $100 for pre-petition services in a Chapter 7 bankruptcy case, plus $9 for credit counseling and $53 for a credit report.[120] The Pre-Petition Agreement gave them the option of retaining Gallon to complete their case in post-petition proceedings for $1,400. Their Chapter 7 bankruptcy case, Case No. 17-11930-M, was filed on September 28, 2017. On September 29, 2017, Murphy and Conder executed a Post-Petition Agreement, where they agreed to pay $1,400 as a flat fee for Gallon to represent them in the completion of their case.[121] A receipt shows that Gallon received $500 in cash from Murphy and Conder on September 20, 2017.[122] Under the AR Agreement, Gallon received $840 from BK Billing upon submission of the Murphy/Conder account, with an additional $210 placed in escrow.[123] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[124] Murphy's and Conder's SOFA disclosed that they had paid Gallon $500 (date not indicated), and included the description "Prepare petition ceritors [sic] & verifcation. [sic] Credit report, credit counseling & filing fee." [125] The filing fee of $335 was paid on the filing date.

b. *Non-Factored Cases* [126]

Kenneth Charles Burton, Case No. 17-12028-M

On October, 12, 2017, Kenneth Charles Burton ("Burton") filed a petition for relief under Chapter 7 of the Bankruptcy Code, Case No. 17-12028-M. The bare bones petition was filed by Gallon as counsel. A receipt shows that Gallon received $150 in cash from Burton on October 3, 2017." [127] No Pre-Petition Agreement was offered to show the terms under which Burton retained Gallon. According to Gallon, no Post-Petition Agreement was executed with Burton because Gallon had ceased doing business with BK Billing and had agreed to complete the Burton case pending further Court review.[128] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $100; leaving a balance due of $1,400.[129] Burton's SOFA disclosed that he had paid Gallon $150 (date not indicated), and included the description "prepare petition, schedules, statements, credit counseling, credit report150" [130] Gallon filed an Installment Application on behalf of Burton.[131]

120. Trial Ex. 13.1.

121. Trial Ex. 13.2.

122. Trial Ex. 13.3.

123. Trial Ex. 13.4.

124. Trial Ex. 13.6.

125. Trial Ex. 13.7.

126. The Non-Factored Cases are those initiated by Gallon under the BK Billing Model, but whose accounts were never submitted to BK Billing because of the issues raised at the October 17 Hearing. *See infra* text accompanying note 150.

127. Trial Ex. 15.3.

128. Trial Tr. at 25–26, May 10, 2018, Case No. 11936-M, *at Docket No. 71*.

129. Trial Ex. 15.6.

130. Trial Ex. 15.7.

131. Case No. 17-12028-M, *at Docket No. 3*. An amended application was filed at Docket No. 13 to change the due dates for payments. This amended application was later granted by the Court. *See Docket No. 15*.

Darin Dwane Miller and Kathy Jo Miller, Case No. 17-12027-M

On October, 12, 2017, Darin Dwane Miller and Kathy Jo Miller (the "Millers") filed a petition for relief under Chapter 7 of the Bankruptcy Code, Case No. 17-12027-M. The bare bones petition was filed by Gallon as counsel. No receipt was offered to show the amount received by Gallon. No Pre-Petition Agreement was offered to show the terms under which the Millers retained Gallon. According to Gallon, no Post-Petition Agreement was executed with the Millers because Gallon had ceased doing business with BK Billing and had agreed to complete the Miller case pending further Court review.[132] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $130; leaving a balance due of $1,370.[133] The Millers' SOFA disclosed that they had paid Gallon $200 (date not indicated), and included the description "prepare petition schedules & statements, credit counseling, credit report." [134] Gallon filed an Installment Application on behalf of the Millers.[135] Although Gallon had no contract or agreement with the Millers, they voluntarily paid Gallon $1,325 post-petition.[136]

Kirby Dwayne Smith and Rebecca Leann Smith, Case No. 17-12029-M

On October, 12, 2017, Kirby Dwayne Smith and Rebecca Leann Smith (the "Smiths") filed a petition for relief under Chapter 7 of the Bankruptcy Code, Case No. 17-12029-M. The bare bones petition was filed by Gallon as counsel. A receipt shows that Gallon received $200 by check from Kirby Smith on October 9, 2017.[137] No Pre-Petition Agreement was offered to show the terms under which the Smiths retained Gallon. According to Gallon, no Post-Petition Agreement was executed with the Smiths because Gallon had ceased doing business with BK Billing and had agreed to complete the Smith case pending further Court review.[138] The Disclosure of Compensation recited that, for legal services, Gallon had agreed to accept $1,500; had received $125; leaving a balance due of $1,375.[139] The Smiths' SOFA disclosed that they had paid Gallon $200 (date not indicated), and included the description "prepare petition schedules & Statements, credit report, credit counseling, Debtor Education." [140] Gallon filed an Installment Application on behalf of the Smiths.[141]

132. Trial Tr. at 25–26, May 10, 2018, Case No. 11936-M, *at Docket No. 71*.

133. Trial Ex. 16.6.

134. Trial Ex. 16.7.

135. Case No. 17-12027-M, *at Docket No. 3*. An amended application was filed at Docket No. 14 to change the due dates for payments. This amended application was later granted by the Court. *See Docket No. 15*.

136. According to Gallon, "Mrs. Miller called me up and basically told me that she had received her income tax return and that she wanted me to get paid and I told her I didn't really know what was going on, but she said that she wanted to pay me. And so I accepted the payment." *See* Trial Tr. at 27 *ll*. 12–16, May 10, 2018, Case No. 11936-M, *at Docket No. 71*. *See also* Trial Ex. 19 (note regarding *Miller* case).

137. Trial Ex. 17.3.

138. Trial Tr. at 25–26, May 10, 2018, Case No. 11936-M, *at Docket No. 71*.

139. Trial Ex. 17.6.

140. Trial Ex. 17.7.

141. Case No. 17-12029-M, *at Docket No. 3*. An amended application was filed at Docket No. 11 to change the due dates for payments. This amended application was later granted by the Court. *See Docket No. 13*.

c. Conventional Cases

Between June 13, 2017, the date Gallon filed the first BK Billing Case, and October 17, 2017, the date of the hearing where Gallon first disclosed his relationship with BK Billing to the Court, Gallon filed nineteen cases that did not utilize the services of BK Billing (the "Conventional Cases").[142] Gallon's disclosed attorney fee[143] in the Conventional Cases ranged from $900 to $1,250, and averaged $1,160.53.[144] In each of the Conventional Cases, the debtor paid the filing fee on the filing date and did not seek to pay it in installments. In each of the Conventional Cases, Gallon attached all required schedules and statements to the petition on the filing date, i.e., none were filed as barebones cases.[145]

3. Court proceedings

Completely unaware of the bifurcated contractual relationships Gallon had entered into with his clients, the Court set the Disclosure of Compensation in the *Wright* case for hearing, noting that the Court had previously ruled that some of the excluded services were required to be performed by counsel for debtors in every Chapter 7 case.[146] In addition, the Court noticed an unusual spate of Installment Applications filed by Gallon in the previous few months without sufficient information for Court review, and set the Installment Agreement in the *Wright* case for hearing to inquire about this practice. It was at this hearing (the "October 17 Hearing") that the Court was first informed of Gallon's use of the BK Billing Model and his factoring arrangement with BK Billing. The UST stated that she had only become aware of the arrangement the day before when preparing for the hearing with Gallon. At the hearing, the Court bluntly asked Gallon to explain "Why wouldn't this be disclosed?" His answer:

> MR. GALLON: Well, it might -- the reason I did not disclose it, Your Honor, in my mind, is that once -- I mean, what, what is happening here is there, is a bifurcation process.
>
> So the client hires you to perform, to, to file the petition and the creditors and the verification. Then once that's done,

142. The Conventional Cases are Case Nos. 17-11177-M; 17-11179-M; 17-11180-M; 17-11181-M; 17-11182-M; 17-11183-M; 17-11407-M; 17-11408-M; 17-11409-M; 17-11561-M; 17-11562-M; 17-11683-M; 17-11684-M; 17-11685-M; 17-11686-M; 17-11831-M; 17-11934-M; 17-12025-M; 17-12026-M. In addition, Gallon filed one case during this period that had the hallmarks of a BK Billing Case, e.g., an Installment Application was filed, attorney fees of $1,500 were disclosed, etc., but it was dismissed because the debtor was ineligible for a discharge due to § 727(a)(8) (debtor had received a discharge within 8 years before the filing date). *See* Case No. 17-11556-M, *Tracie Lynn Tennant*.

143. These amounts are taken from the Disclosure of Compensation filed in each of the Conventional Cases. These amounts differ from that disclosed on the SOFA in every case.

144. This number represents the attorney fee collected by Gallon, and does not include any amounts for filing fees or other fees Gallon collected for credit reports, counseling, etc.

145. The only required pleading Gallon failed to consistently attach to the petition in the Conventional Cases was the Payment Advice Certification, which was sporadically submitted as a later pleading.

146. *See In re Minardi*, 399 B.R. 841, 849–850 (Bankr. N.D. Okla. 2009). After the Disclosure of Compensation was set for hearing, but prior to the October 17 Hearing, Gallon amended the Disclosure of Compensation in the *Wright* case to exclude only 1) Adversary Proceeding; 2) Amendment(s) to Schedules to add creditors; and 3) Objection to Discharge from the services he agreed to perform for debtors. *See* Trial Ex. 14.6.

> you have a second meeting, which is the bifurcation, where they rehire you to finish the, the schedules, statements, and all that. Then once that's done, that's whenever it is factored. And so it is just my way of receiving, I mean, I could collect it from the debtor instead of BK Billing. And so I didn't, I mean, I just didn't think it was something that I was required to disclose. It's my receivable. It's monies that's owed me.[147]

Two days after the October 17 Hearing, Gallon filed an amended Disclosure of Compensation in the *Wright* case (the "Amended Disclosure"), which added the following statement:

> Counsel may receive financing from a third-party via a financing or factoring facility. Although in undersigned counsel's view such financing or factoring facility should not be considered an agreement to share compensation, the terms of such agreement will include the granting by undersigned counsel of an interest in the undersigned counsel's accounts and the creditor may have rights to receive payment from the client. Any such financing or factoring facility agreement will clearly provide that client must first give consent to the party relationship and under no circumstances will any of the terms of the financing or factoring facility agreement require counsel to disclose any information that is either confidential or may be considered a privileged communication with the client. The actual agreement will be made available upon request by a party-in-interest.[148]

Gallon has since filed the same Amended Disclosure in all of the BK Billing Cases.

The Court continued the hearing to allow the UST to gather more information regarding Gallon's relationship with BK Billing and decide on a course of action. At the continued hearing, the Court heard from the UST and Gallon, and discussed the UST's Motion filed in the *Wright* case.[149] The Motion proposed an agreement between the UST and Gallon, whereby Gallon would: 1) disgorge his fee in the *Wright* case "in part;" 2) continue to represent debtors in any of the open BK Billing Cases; 3) continue representing debtors in the Non-Factored Cases;[150] and 4) cease doing business with BK Billing going forward. A proposed agreed order along those lines was later submitted to (not filed with) the Court that indicated Gallon would disgorge $855 received post-petition (presumably from BK Billing) and cancel any post-petition contract that allowed BK Billing to further collect from Wright. The Court found the proposed agreement wholly unsatisfactory, and held a telephonic hearing on January 31, 2018, at which it requested more information from Gallon regarding the Captioned Cases. The Court subsequently issued an Order Scheduling Hearing and Directing Counsel for the Debtor to Address Issues of Compensation.[151] The Order outlined the concerns of the Court and advised Gallon of the various types of sanctions or remedies the Court was contemplating in these cases. Among the possible sanctions was disgorgement of all fees paid by debtors in

147. *See* Trial Tr. at 7 *ll.* 4–18, October 17, 2017, Case No. 17-11936-M, *at Docket No. 29*.

148. Trial Ex. 14.6.

149. Case No. 17-11936-M, *at Docket No. 38*.

150. These are the *Burton, Miller,* and *Smith* cases.

151. Case No. 17-11936-M, *at Docket No. 60*. An order giving the debtors an opportunity to appear and be heard at the hearing was also entered in each of the other 16 Captioned Cases.

any of the Captioned Cases and the indemnification by Gallon of his clients against any further collection action brought by BK Billing.[152]

On May 10, 2018, the Court held a hearing (the "May 10 Hearing") on these matters. Gallon's arguments and defenses were presented in a pre-hearing brief.[153] His arguments can be summarized as follows:

1. Use of the BK Billing Model made Gallon financially worse off than if he had used a conventional, pre-petition billing method.[154]
2. Gallon relied on BK Billing, based on the vigor and sophistication used to induce him to adopt the BK Billing Model. BK Billing appeared to be a highly professional organization, presented a polished sales pitch, and was a high-level sponsor of the National Association of Consumer Bankruptcy Attorneys annual meeting. Gallon was given the impression that its model was widely and successfully used.[155]
3. Gallon did not disclose the BK Billing Model because 1) he relied on BK Billing to advise him of the need to change his usual procedures; 2) he was not aware that BK Billing provided a specific form of disclosure to be filed with the Court; and 3) "it just did not occur to him that such disclosure was required." [156]
4. Gallon did not understand that participating in the BK Billing program might involve violation of bankruptcy law.[157]
5. A significant motivation for Gallon to offer the BK Billing Model "was to allow clients to obtain relief from their debt problems more quickly." [158]
6. Gallon's long-time bankruptcy legal assistant was distracted and ultimately quit during the period he was utilizing the BK Billing Model. He states that many of the mistakes in the disclosures and statements were due to that distracted assistant, his own inept efforts at learning the software, and finally the learning curve of training a new assistant.[159]
7. Each of the debtors in the Captioned Cases received a discharge without complaint or complication. Gallon suggests that this is a vindication of any charge that his prepetition investigation and analysis of the debtors' cases, without preparing schedules and statements, was inadequate.[160]

When questioned about the reason for the bifurcation and performance of services post-petition, Gallon admitted that the practice was not for the benefit of debtors, but was done solely to facilitate the BK Billing Model of collection, by making all fees attributed to post-petition work non-dischargeable.[161] Gallon valued

152. *Id.* at. 7.

153. J. Ken Gallon's Brief Regarding Issues of Compensation, Case No. 17-11936-M, *at Docket No. 65*.

154. *Id.* at 3.

155. *Id.* at 5.

156. *Id.* at 6.

157. *Id.*

158. *Id.*

159. *Id.*

160. *Id.* at 6–7.

161. Trial Tr. at 58 *ll.* 9–24, May 10, 2018, Case No. 11936-M, *at Docket No. 71*.

his time at $250 per hour, based on the amount he charges in Chapter 13 cases. He acknowledged that he did not accurately account for services provided pre-petition to debtors, and often spent more time working on their cases pre-petition than the debtors paid for before the case was filed. For example, if a debtor paid only $100 prior to the case being filed, Gallon acknowledged that he spent more than 4/10 of an hour preparing the case for filing.[162] Under the BK Billing Model, Gallon then shifted the remainder of his fee to be collected post-petition, even though some of the services being compensated had already been provided pre-petition.

Gallon testified that he immediately stopped using the services of BK Billing as soon as he became aware of the concerns of the Court and the UST. The UST stipulated that Gallon cooperated fully in amending disclosures and providing documents and information during their investigation of these matters.[163] At the May 10 Hearing, Gallon reiterated his understanding that the factoring of his fee to BK Billing did not involve any sharing of fees since they were simply a collection agency and not providing any services to the debtors.[164]

Conclusions of Law

1. Counsel's duty of disclosure pursuant to § 329

Section 329 of the Bankruptcy Code lies at the heart of these cases. Under that section, if a debtor pays or makes an agreement to pay an attorney for services related to a bankruptcy case,[165] that attorney is required to file a statement with the Court that discloses: 1) any compensation paid to the attorney, if the payment was made after one year before the date of the filing of the petition; 2) any compensation agreed to be paid to the attorney, if such agreement was made after one year before the date of the filing of the petition; and 3) the source of such compensation paid or agreed to be paid.[166] For Chapter 7 debtors' counsel, § 329 is implemented by Bankruptcy Rule 2016(b).[167] In addition to

162. *Id.* at 60.

163. *Id.* at 9–10.

164. *Id.* at 64.

165. The language of the statute requires disclosure of compensation paid or agreed to be paid ''for services rendered or to be rendered in contemplation of or in connection with the case by such attorney.'' § 329(a). There is no issue in this case that the services rendered by Gallon to the various debtors were not related to their bankruptcy cases.

166. (a) Any attorney representing a debtor in a case under this title, or in connection with such a case, whether or not such attorney applies for compensation under this title, shall file with the court a statement of the compensation paid or agreed to be paid, if such payment or agreement was made after one year before the date of the filing of the petition, for services rendered or to be rendered in contemplation of or in connection with the case by such attorney, and the source of such compensation.

§ 329(a).

167. (b) Disclosure of compensation paid or promised to attorney for debtor

Every attorney for a debtor, whether or not the attorney applies for compensation, shall file and transmit to the United States trustee within 14 days after the order for relief, or at another time as the court may direct, the statement required by § 329 of the Code including whether the attorney has shared or agreed to share the compensation with any other entity. The statement shall include the particulars of any such sharing or agreement to share by the attorney, but the details of any agreement for the sharing of the compensation with a member or regular associate of the attorney's law firm shall not be required. A supplemental statement shall be filed and transmitted to the United States trustee within 14 days after any payment or agreement not previously disclosed.

the duties specified in § 329, the Rule adds the requirement that counsel disclose "whether the attorney has shared or agreed to share the compensation with any other entity," including "the particulars of any such sharing or agreement to share by the attorney[.]" [168] These disclosures are required to be filed within 14 days after the case is filed, and supplemented within 14 days after any payment or agreement not previously disclosed.[169]

[1–5] Counsel's duties of disclosure apply whether or not the attorney applies for compensation from the estate.[170] The disclosure requirements of § 329 are "mandatory not permissive." [171] The statute is "designed to prevent bankruptcy attorneys from extracting more than their fair share from prospective debtors willing to do whatever is necessary to obtain their counsel of choice and avoid unfavorable bankruptcy proceedings." [172] "Counsel's fee revelations must be direct and comprehensive. Coy or incomplete disclosures which leave the court to ferret out pertinent information from other sources are not sufficient." [173] "Absent complete disclosure, the court is unable to make an informed judgment regarding the nature and amount of compensation paid or promised by the debtor for legal services in contemplation of bankruptcy." [174]

Rule 2017 directs the court to review any payments or transfers, or agreements for either, made directly or indirectly by debtors to an attorney, either before or after the filing of the bankruptcy case, to determine if those payments or transfers are excessive.[175] According to the advisory committee's note appended to the Rule's original publication,

> This rule ... is premised on the need for and appropriateness of judicial scrutiny of arrangements between a debtor and his attorney to protect the creditors

Rule 2016(b).

168. *Id.*

169. *Id.*

170. § 329. *See In re Brown*, 371 B.R. 486, 497 (Bankr. N.D. Okla. 2007), *amended by* 371 B.R. 505 (Bankr. N.D. Okla. 2007).

171. *See Turner v. Davis, Gillenwater & Lynch (In re Inv. Bankers, Inc.)*, 4 F.3d 1556, 1565 (10th Cir. 1993) (*citing In re Bennett*, 133 B.R. 374, 378 (Bankr. N.D. Tex. 1991)).

172. *Id.* (*citing In re NBI, Inc.*, 129 B.R. 212, 222 (Bankr. D. Colo. 1991)).

173. *In re Woodward*, 229 B.R. 468, 474 (Bankr. N.D. Okla. 1999) (*quoting In re Saturley*, 131 B.R. 509, 517 (Bankr. D. Me. 1991)).

174. *In re Perrine*, 369 B.R. 571, 580 (Bankr. C.D. Cal. 2007).

175. *See In re Brown*, 371 B.R. at 497. Rule 2017 reads:

> (a) Payment or transfer to attorney before order for relief
> On motion by any party in interest or on the court's own initiative, the court after notice and a hearing may determine whether any payment of money or any transfer of property by the debtor, made directly or indirectly and in contemplation of the filing of a petition under the Code by or against the debtor or before entry of the order for relief in an involuntary case, to an attorney for services rendered or to be rendered is excessive.
> (b) Payment or transfer to attorney after order for relief
> On motion by the debtor, the United States trustee, or on the court's own initiative, the court after notice and a hearing may determine whether any payment of money or any transfer of property, or any agreement therefor, by the debtor to an attorney after entry of an order for relief in a case under the Code is excessive, whether the payment or transfer is made or is to be made directly or indirectly, if the payment, transfer, or agreement therefor is for services in any way related to the case.

Rule 2017.

> of the estate and the debtor against overreaching by an officer of the court who is in a peculiarly advantageous position to impose on both the creditors and his client.[176]

If the payment or agreement is found to exceed the reasonable value of the services provided by the attorney, the Court may cancel the agreement or disgorge any such payment to its source.[177]

[6–11] The consequences of an attorney's failure to comply with the disclosure requirements of § 329 can be severe, including forfeiting the right to receive *any* compensation for services rendered to the debtor.[178] "Disgorgement of fees as a result of inadequate disclosure by counsel is a matter left to the sound discretion of the bankruptcy court." [179] "The imposition of a disgorgement order should be commensurate with the egregiousness of the conduct and will depend on the particular facts of each case." [180] "The Court may sanction failure to disclose 'regardless of actual harm to the estate.' " [181] This Court has previously adopted a strict position regarding failure of debtors' counsel to disclose compensation arrangements to the Court:

> This Court takes the requirement of full disclosure under § 329 seriously, for to do less is to judicially repeal the statute. . . . Were the Court to require less than full disclosure, the purpose behind § 329(a) would be defeated. Counsel could avoid disclosure of any or all of the fees paid to them by making a covert decision that the undisclosed fee was so unrelated to the bankruptcy case that its disclosure was not required, and eliminating the possibility of Court review in the process. The Court's ability to make a meaningful review of attorney's fees would be hindered if not destroyed. Such a result can be neither condoned nor allowed.[182]

Nothing presented to the Court in these matters suggests that any lesser standard should prevail. Nor does the Court find that a "pure heart," without a subjective intent to violate the Code or Rules, provides counsel any defense to the failure to file the proper disclosures under § 329.[183] "Negligent or inadvertent omissions 'do

176. Rule 2017 advisory committee's note (*citing* 2 Collier on Bankruptcy ¶ 329.02 (15th ed. 1980); MacLachlan, Bankruptcy 318 (1956)).

177. § 329 (b) reads:

> (b) If such compensation exceeds the reasonable value of any such services, the court may cancel any such agreement, or order the return of any such payment, to the extent excessive, to–
>
> (1) the estate, if the property transferred–
>
> (A) would have been property of the estate; or
>
> (B) was to be paid by or on behalf of the debtor under a plan under chapter 11, 12, or 13 of this title; or
>
> (2) the entity that made such payment.

178. *In re Inv. Bankers*, 4 F.3d at 1565; *In re Smitty's Truck Stop, Inc.*, 210 B.R. 844, 848–49 (10th Cir. BAP 1997).

179. *In re Brown*, 371 B.R. at 499. *See also In re Stewart*, 583 B.R. 775, 783 (Bankr. W.D. Okla. 2018) (*citing In re Brown*).

180. *In re Brown*, 371 B.R. at 499 (*citing In re Hackney*, 347 B.R. 432, 443 (Bankr. M.D. Fla. 2006)) (internal citations and quotations omitted).

181. *In re Smitty's Truck Stop*, 210 B.R. at 849 (*citing In re Maui 14K, Ltd.*, 133 B.R. 657, 660 (Bankr. D. Haw. 1991)).

182. *In re Woodward*, 229 B.R. at 474–75 (disgorgement of all fees). *See also In re Lewis*, 309 B.R. 597 (Bankr. N.D. Okla. 2004) (same); *In re Brown*, 371 B.R. at 486 (same). *Accord In re Inv. Bankers*, 4 F.3d at 1565–66; *In re Smitty's Truck Stop*, 210 B.R. at 848.

183. *In re Stewart*, 583 B.R. at 782.

not vitiate the failure to disclose.' "[184]

[12] The Court finds Gallon's original Disclosure of Compensation in each of these cases to be grossly misleading and indicative of a wanton disregard—*to the point of negligence*—for the level of candor required under § 329. Some of Gallon's errors defy comprehension. For example, in the *Wright* case, Gallon disclosed that he had agreed to accept $1,500 for legal services with a balance due of $1,425, when he actually had agreed to receive $855, plus $213.75 paid to escrow, from BK Billing.[185] The statement is flat-out deceptive, whether or not that is what Gallon intended. The disclosure conflates the total amount a debtor agreed to pay for his services with the amount he agreed to accept for his services, even though those amounts differ by several hundred dollars in each of the BK Billing Cases.

[13] Other errors demonstrate the general level of sloppiness evident in much of Gallon's record keeping. For example, in the *Wright* case, Gallon disclosed that "prior to the filing of this statement I have received $75," even though his Pre-Petition Agreement indicated Ms. Wright had agreed to pay $200 plus an additional $42 in fees. An internal office memo indicated that she had actually paid $200. Although Gallon blamed such mistakes on the loss of his long-time assistant and the difficulty in training a new one, Gallon has duties of competence to his clients that transcend bankruptcy law.[186] He should not accept clients if he does not have the basic skills to file their cases in a complete and competent manner. This Court does not accept laying the blame at the foot of an employee as an excuse.

Of equal concern is that Gallon indicated in each Disclosure of Compensation that he had not shared his fee with any other person. Both in his written brief and testimony, Gallon insisted on his understanding that he was not sharing fees because "it was his receivable" that he could dispose of or sell in any way he wanted, and that BK Billing was simply a collection agency. The Court is not particularly concerned here with the legal or ethical violations involved with any possible sharing arrangement.[187] What concerns the Court is Gallon's rather brazen position, with no citation to authority, that collection of a fee from his client that is split between himself and BK Billing does not constitute sufficient "sharing of compensation" that it should—*at a minimum*—be disclosed to the Court. Courts have found that a failure to comply with disclosure requirements is sanctionable even if proper disclosure would have shown no violation of the Code

184. *In re Smitty's Truck Stop*, 210 B.R. at 848 (*quoting Neben & Starrett, Inc. v. Chartwell Fin. Corp. (In re Park-Helena Corp.)*, 63 F.3d 877, 881 (9th Cir. 1995)) (internal citations omitted).

185. Trial Ex. 14-4, 14-6.

186. Rules of Prof'l Conduct, Rule 1.1, Okla. Stat. tit. 5, ch. 1, app. 3-A ("A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness, and preparation reasonably necessary for the representation.").

187. *See, e.g.*, § 504(a) ("Except as provided in subsection (b) of this section, a person receiving compensation or reimbursement under section 503(b)(2) or 503(b)(4) of this title may not share or agree to share–(1) any such compensation or reimbursement with another person[.]") This statute suggests that while sharing of fees is prohibited in some circumstances, not every receipt of fees related to a bankruptcy case is affected. *But see* Rules of Prof'l Conduct, Rule 5.4(a), Okla. Stat. tit. 5, ch. 1, app. 3-A ("A lawyer or law firm shall not share legal fees with a nonlawyer[.]") (listing several exceptions that do not apply here).

or Rules.[188]

[14] Gallon filed an Amended Disclosure in each of the cases in an effort to remedy the deficiencies in the original. His efforts fell woefully short. His statement that "counsel may receive financing from a third-party" does not adequately disclose that in each of the affected cases he *did in fact* receive such financing, and on what terms. He goes on to state his view that the arrangement does not involve sharing of fees, but gives no particulars of the arrangement. Offering to make the agreement available upon request does not satisfy Rule 2016(b)'s requirement of disclosing "the particulars of any such sharing or agreement to share." [189]

2. Counsel's duty of candor to the tribunal

[15] In addition to the statutory duties provided in the Bankruptcy Code, Gallon has other duties to his clients and the Court based on his role as an officer of the court. An attorney becomes an officer of the court upon taking an oath and meeting other requirements imposed by state law.[190] In Oklahoma, that oath requires counsel to show complete candor toward the tribunal.[191] Oklahoma Rule of Professional Conduct 3.3 reinforces the requirement of candor.[192] Such candor is vital to the integrity of the bankruptcy process itself.

The Court is troubled by Gallon's practice of charging a higher fee to his clients that use the BK Billing Model than to his conventional clients. Gallon charged his average conventional client $1,250 when the fee was fully paid prior to filing a debtor's petition. Under the BK Billing Model, a debtor was charged a total of $1,500 for attorney fees. From the debtor's perspective, that is a $250 premium, or 20% above the fee charged in a conventional case, for the convenience of paying the fee over 12 months. From Gallon's perspective, the math is even worse. For example in the *Wright* case, Gallon invoiced Wright's account to BK Billing for $1,425. He actually received $855 from BK Billing. That means Wright agreed to pay a 66% markup over

188. *In re Stewart*, 583 B.R. at 782. *See also In re Waldo*, 417 B.R. 854, 893 (Bankr. E.D. Tenn. 2009).

189. Rule 2016(b).

190. Rules of Prof'l Conduct, Preamble cmt. 1, Okla. Stat. tit. 5, ch. 1, app. 3-A ("A lawyer, as a member of the legal profession, is a representative of clients, *an officer of the legal system* and a public citizen having special responsibility for the quality of justice.") (emphasis added).

191. The oath required to practice law in Oklahoma reads as follows:

> I do solemnly swear that I will support, protect and defend the Constitution of the United States, and the Constitution of the State of Oklahoma; that I will do no falsehood, or consent that any be done in court, and if I know of any I will give knowledge thereof to the judges of the court, or some one of them, that it may be reformed; I will not wittingly, willingly or knowingly promote, sue, or procure to be sued, any false or unlawful suit, or give aid or consent to the same; I will delay no person for lucre or malice, but will act in the office of attorney in all courts according to my best learning and discretion with all good fidelity as well to the court as to my client, so help me God.

Okla. Stat. tit. 5, ch. 1, § 2. *See also id.*, app. 5, § 1.

192. Rule 3.3. Candor Toward The Tribunal:

> (a) A lawyer shall not knowingly:
> (1) make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by the lawyer[.]

Rules of Prof'l Conduct, Rule 3.3, Okla. Stat. tit. 5, ch. 1, app. 3-A. *See also id.*, Preamble cmt. 12, Okla. Stat. tit. 5, ch. 1, app. 3-A ("Every lawyer is responsible for observance of the Rules of Professional Conduct.").

the amount Gallon actually received for providing her services.[193] Additionally, if Gallon was willing to accept roughly $1,069, or 75% of $1,425, in a typical BK Billing Case, assuming he received the escrowed payments, the Court could rightly conclude that he consistently overcharges his conventional clients for the value of his services. Gallon's only defense of the practice of charging higher fees to BK Billing clients was that it was encouraged by BK Billing as part of their training package.

[16] It is clear to the Court that a prominent feature of the BK Billing Model is the designation of the bulk of services as "post-petition" in order to render them beyond the Chapter 7 discharge and therefore collectable by BK Billing. There are (at least) two problems with this approach. First, by waiting until after the petition is filed to perform most of the actual services, such as filing out schedules and statements, counsel risks overlooking essential information regarding the debtors' financial condition, which may have been missed in the cursory interview conducted pre-petition. Counsel may discover too late that he or she should have chosen a different chapter, or not filed the case at all. Second, the amount of Gallon's fees designated pre- or post-petition was motivated by how much money the debtor was able to pay up front, and not related in any way to when Gallon's services were actually performed. Valuing his time at $250 per hour, Gallon admitted that in several cases he spent much more time pre-petition than he was paid for, but then designated the remaining fee as "post-petition," thus turning an otherwise dischargeable pre-petition claim into a non-discharged claim.[194] Such a scheme works a fraud both on the debtor and the Court.

Of additional concern to the Court is that Gallon indicated that the source of the compensation to be paid to him was the debtor, even though Bankruptcy Form 2030 presented him with another option. Courts have consistently held that payment of funds from a third-party payor to pay a debtor's legal fees does not alter counsel's obligation of proper disclosure.[195] In each of the BK Billing Cases except *Gomes*, Gallon received a direct deposit equal to 60% of the invoiced account value from BK Billing, with an agreement he would be paid an additional 15% if the accounts were sufficiently remitted by the debtors.[196] Clearly, "the "source of such compensation" is directly required to be disclosed under § 329. Gallon tries to deflect responsibility for this failure by stating that he relied on BK Billing to train and advise him on the use of their model. Such reliance on BK Billing in the discharge of his professional duties and judgment is a breach of the Oklahoma Rules of Professional Conduct.[197] Despite not being

193. Even if Gallon had received the additional escrow payment, Wright would have paid a 33% markup over the amount Gallon received.

194. Trial Tr. at 60, May 10, 2018, Case No. 11936-M, *at Docket No. 71*.

195. *In re Stewart*, 583 B.R. at 781.

196. Under the original AR Agreement, Gallon received 70% of the invoiced Gomes account, with no escrowed payment.

197. *See, e.g.*, Rules of Prof'l Conduct, Rule 5.4(c), Okla. Stat. tit. 5, ch. 1, app. 3-A (''A lawyer shall not permit a person who recommends, employs, *or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services*.'') (emphasis added); *Id.* Rule 1.8(f) (''A lawyer shall not accept compensation for representing a client from one other than the client unless: (1) the client gives informed consent; (2) there is *no interference with the lawyer's independence of professional judgment* or with the client-lawyer relationship[.]'') (emphasis added); Rule 1.7(a) (''A concurrent conflict of interest exists if: . . .(2) there is a significant risk that the

"trained" or provided a form by BK Billing, Gallon certainly understood that he was only indirectly being compensated by his clients, but that the actual funds he received came directly from BK Billing. He should have known that the information provided to the Court in the Disclosure of Compensation filed in these cases was grossly misleading, if not out right false. His declaration that it simply "did not occur to him that such disclosure was required" is both disheartening and astonishing. This Court has published no less than three opinions directly related to the failure of debtors' counsel to properly disclose all financial dealings with their clients.[198] As an officer of the Court, Gallon is expected to be aware of such rulings.

Gallon tries to rationalize his failures by citing the blind faith he put in BK Billing as a company. He suggests that he was induced to adopt the BK Billing Model based on the company's slick sales pitch and high-profile sponsorship of a leading bankruptcy conference. While the Court does not doubt that BK Billing rolled out a persuasive marketing campaign, the Court believes that any reasonable attorney would have at least questioned the "too good to be true" aspect of the model. Instead, Gallon blindly adopted the BK Billing Model, without conducting even a minimal inquiry into the legal or ethical issues that such a system might raise. The Court finds that such abdication of his professional judgment is unreasonable.

[17, 18] This Court has previously noted the bankruptcy system is a fragile one, built on the principles of full and candid disclosure.[199] Its operation and survival rely on the integrity and professionalism of its practitioners. Only through serendipity were these matters brought to the Court's attention. "This is not an area where the Court will engage in or tolerate a game of 'catch me if you can,' or allow 'I guess I did not know better' to be a palatable excuse." [200] The Court finds Gallon's disclosures regarding the nature and source of his compensation in these cases to be grossly inadequate to the point of being misleading. The Court is aware that it has discretion when determining the degree of sanctions for non-disclosure.[201] The Court finds Gallon's entire fee in each of these cases to be unreasonable. His failures are sufficiently severe and pervasive to warrant disgorgement. The Court would be justified in disgorging all fees received by Gallon or collected by BK Billing, but finds that such an order would be administratively unworkable, since some of the funds paid by the debtors pre-petition were allocated to court fees and other miscellaneous services. The Court will limit disgorgement to the value of fees actually collected by BK Billing from each of the debtors in the Captioned Cases after their petitions were filed.[202] Such funds shall be remitted by Gallon to the debtor that made the payment. The Post-Petition Agreements in each case are found to be void, and neither

representation of one or more clients will be materially limited by the lawyer's responsibilities to ... *a third person or by a personal interest of the lawyer*.") (emphasis added).

198. *In re Woodward*, 229 B.R. at 468; *In re Lewis*, 309 B.R. at 597; *In re Brown*, 371 B.R. at 486.

199. *In re Lewis*, 309 B.R. at 602.

200. *Id.* at 603.

201. *In re Brown*, 371 B.R. at 499; *In re Stewart*, 583 B.R. at 783.

202. To be abundantly clear, these fees are ordered disgorged *from Gallon*, and not from BK Billing, over which the Court has not exercised jurisdiction. In addition, the Court will not disturb the voluntary payment of $1,325 made directly to Gallon from the Millers in Case No. 17-12027-M.

Gallon nor BK Billing may enforce any claim against the debtors under those contracts.[203] The Court is aware this is a harsh sanction, but anything less would minimize the serious nature of Gallon's conduct.

3. Debtors' violations of Rule 1006

[19] Section 1930 of title 28 of the United States Code sets out the schedule of fees to be collected by the clerk when a bankruptcy case is filed. The statute explicitly allows a debtor in a voluntary case to pay the required fee in installments.[204] Rule 1006 implements this statute, but adds that a debtor that utilizes the installment provision may make no further payments "to an attorney or any other person who renders services to the debtor in connection with the case" until the filing fee is paid in full.[205]

In eleven of the seventeen Captioned Cases, Gallon filed an Installment Application. In each of those cases, the application included a statement executed by both the debtors and Gallon that the debtors understood they must pay their entire filing fee before they make any more payments or transfer any more property to an attorney *or anyone else* for services in connection with their bankruptcy case.[206] In eight of those cases, due to the scheme orchestrated by Gallon, debtors unwittingly made payments to BK Billing toward Gallon's attorney fee before their entire filing fee was paid to the Court, in direct violation of Rule 1006. The remaining three cases were not submitted to BK Billing for factoring, therefore no violation occurred.

Gallon, as an attorney admitted to practice before this Court, is charged with knowing and understanding the Federal Rules of Bankruptcy Procedure, as well as the applicable provisions of the Bankruptcy Code. His signature on the Installment Application was a violation of both his ethical and statutory duties. Rule 9011(b)(3) outlines counsel's ethical duty of candor in signing an application submitted to the Court:

> (b) Representations to the court
>
> By presenting to the court (whether by signing, filing, submitting, or later advocating) a petition, pleading, written motion, or other paper, an attorney or unrepresented party is certifying that to the best of the person's knowledge, information, and belief, formed after an inquiry reasonable under the circumstances,–
>
> * * *
>
> (3) *the allegations and other factual contentions have evidentiary support* or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery[.][207]

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") was enacted "to correct perceived abuses of the bankruptcy system."[208] Among its reforms were §§ 526–528,

203. The Court offers no opinion on how this ruling affects the contractual duties between Gallon and BK Billing.

204. 28 U.S.C. § 1930(a) (hanging paragraph).

205. Rule 1006(b)(3)("All installments of the filing fee must be paid in full before the debtor or chapter 13 trustee may make further payments to an attorney or any other person who renders services to the debtor in connection with the case.").

206. *See, e.g.,* Case No. 17-11936-M, *at Docket No. 4*.

207. Rule 9011(b)(3) (emphasis added).

208. *Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 231–32, 130 S.Ct. 1324, 176 L.Ed.2d 79 (2010).

which target debt relief agencies, "*i.e.*, professionals who provide bankruptcy assistance to consumer debtors." [209] As a debt relief agency, Gallon is bound by duties of candor therein.[210] The relevant subsection of § 526 reads as follows:

> (a) A debt relief agency shall not–
>
> * * *
>
> (2) *make any statement*, *or counsel or advise any assisted person* or prospective assisted person *to make a statement* in a document filed in a case or proceeding under this title, *that is untrue or misleading*, or that upon the exercise of reasonable care, should have been known by such agency to be untrue or misleading[.] [211]

Considering he set these events in motion by factoring his fee to BK Billing, Gallon knew or should have known that BK Billing would begin collection activity prior to the debtors' court fees being paid in full. He is also charged with knowing that such payment to BK Billing was a violation of the debtors' duties under Rule 1006. His signature on the Installment Agreements is a violation of his duty of candor under both Rule 9011(b)(3) and § 526(a)(2). Gallon compounded the violation of § 526(a)(2) by advising his clients to sign the Installment Agreements and causing them to make misleading statements regarding their payment of his fees.

The Court does not take these violations lightly. The bankruptcy system requires complete candor from both debtors and their engaged professionals.[212] Standing alone, the Court would find cause to sanction Gallon under Rule 9011(c) or § 526(c)(5) for filing and endorsing the debtors' misleading statements found in the Installment Agreements. The Court notes that in all eleven cases, all required Court filing fees were eventually fully paid, either by the debtors or Gallon, and each of the debtors received their discharge. Therefore, despite the authority to do so, the Court will not impose additional sanctions.

4. *Counsel's duties under BAPCPA*

As soon as Gallon became aware of his missteps in these cases, he worked diligently to assist the UST to investigate this matter and cut ties with BK Billing. As such, he offered no defense of the BK Billing Model of bifurcating services into pre- and post-petition categories or its factoring practice, which required debtors to incur debt to pay their attorney's fee. Several courts across the country have faced variations on this theme. Some have offered advice and recommendations in order to craft an acceptable scheme whereby attorneys may offer bifurcated services.[213]

209. *Id.* at 232, 130 S.Ct. 1324.

210. *Id.* (holding that consumer debtors' attorneys qualify as "debt relief agencies," as defined in § 101(12A), and are therefore subject to §§ 526–528).

211. § 526 (as amended by Bankruptcy Technical Corrections Act of 2010, Pub. L. 111-327, § 2(a)(2), 124 Stat. 3557) (emphasis added).

212. *See Grogan v. Garner*, 498 U.S. 279, 287, 111 S.Ct. 654, 112 L.Ed.2d 755 (1991) (The Bankruptcy Code "limits the opportunity for a completely unencumbered new beginning to the 'honest but unfortunate debtor.' ") (*quoting Local Loan Co. v. Hunt*, 292 U.S. 234, 244, 54 S.Ct. 695, 78 L.Ed. 1230 (1934)). *See also* Rule 9011.

213. *Bethea v. Robert J. Adams & Assocs.*, 352 F.3d 1125, 1128 (7th Cir. 2003) (proposes bifurcation of services model; pre-BAPCPA case); *Walton v. Clark & Washington, P.C.*, 469 B.R. 383 (Bankr. M.D. Fla. 2012) (endorses specific bifurcation of services model; provides guidance); *In re Slabbinck*, 482 B.R. 576, 584 (Bankr. E.D. Mich. 2012) (same); *In re Waldo*, 417 B.R. 854 (Bankr. E.D. Tenn. 2009) (rejects model utilized by counsel; endorses bifurcation of services model in dicta); *In re Lawson*, 437 B.R. 609 (Bankr. E.D.

Others have noted that various provisions added to the Code by BAPCPA appear to thwart such schemes.[214] This Court has reviewed the cases carefully and believes that BAPCPA presents serious impediments to the legality of this kind of bifurcated services scheme, such as the BK Billing Model.[215] The difficulty here is that

Tenn. 2010) (same); *In re Griffin*, 313 B.R. 757, 769–70 (Bankr. N.D. Ill. 2004) (endorses bifurcation of services model in dicta; provides guidance); *In re Abdel-Hak*, No. 12-46329-MBM, 2012 WL 5874317, at *7 (Bankr. E.D. Mich. Nov. 16, 2012) (same).

214. *See In re Jackson*, No. 14-11415, 2014 WL 3722019 (Bankr. W.D. La. July 24, 2014) (two contract procedure used by counsel did not comply with ''material requirements'' of § 528; both agreements found void under § 526(c)(1)); *In re Green*, No. 14-11458, 2014 WL 3724986 (Bankr. W.D. La. July 24, 2014) (same). *But see In re Slabbinck*, 482 B.R. at 584 n.1 (acknowledged §§ 526–528 added by BAPCPA, but ignored because not raised by any party).

215. Relevant subsections of § 526 read as follows:

(a) A debt relief agency shall not–

(1) fail to perform any service that such agency informed an assisted person or prospective assisted person it would provide in connection with a case or proceeding under this title;

(2) make any statement, or counsel or advise any assisted person or prospective assisted person to make a statement in a document filed in a case or proceeding under this title, that is untrue or misleading, or that upon the exercise of reasonable care, should have been known by such agency to be untrue or misleading;

(3) misrepresent to any assisted person or prospective assisted person, directly or indirectly, affirmatively or by material omission, with respect to–

(A) the services that such agency will provide to such person; or

(B) the benefits and risks that may result if such person becomes a debtor in a case under this title; or

(4) advise an assisted person or prospective assisted person to incur more debt in contemplation of such person filing a case under this title or to pay an attorney or bankruptcy petition preparer a fee or charge for services performed as part of preparing for or representing a debtor in a case under this title.

(b) Any waiver by any assisted person of any protection or right provided under this section shall not be enforceable against the debtor by any Federal or State court or any other person, but may be enforced against a debt relief agency.

(c)(1) Any contract for bankruptcy assistance between a debt relief agency and an assisted person that does not comply with the material requirements of this section, section 527, or section 528 shall be void and may not be enforced by any Federal or State court or by any other person, other than such assisted person.

(2) Any debt relief agency shall be liable to an assisted person in the amount of any fees or charges in connection with providing bankruptcy assistance to such person that such debt relief agency has received, for actual damages, and for reasonable attorneys' fees and costs if such agency is found, after notice and a hearing, to have–

(A) intentionally or negligently failed to comply with any provision of this section, section 527, or section 528 with respect to a case or proceeding under this title for such assisted person;

(B) provided bankruptcy assistance to an assisted person in a case or proceeding under this title that is dismissed or converted to a case under another chapter of this title because of such agency's intentional or negligent failure to file any required document including those specified in section 521; or

(C) intentionally or negligently disregarded the material requirements of this title or the Federal Rules of Bankruptcy Procedure applicable to such agency.

* * *

(5) Notwithstanding any other provision of Federal law and in addition to any other remedy provided under Federal or State law, if the court, on its own motion or on the motion of the United States trustee or the debtor, finds that a person intentionally violated this section, or engaged in a clear and consistent pattern or practice of violating this section, the court may--

(A) enjoin the violation of such section; or

no one appears in these cases to defend the model or offer an alternative argument to the Court. That seems like shaky ground to rule or comment on the validity of the model. Because the Court has disposed of these matters under section 329, it is not necessary to review them further on alternative grounds. Therefore the Court will wait until issues of bifurcation of services and fee factoring are before it in an actual case or controversy before it weighs in on §§ 526 and 528. The Court raises these issues in the hope that counsel considering use of a similar scheme will carefully review the legal and ethical provisions of BAPCPA and state ethics rules *before* they file a petition in this district.

Conclusion

Gallon must disgorge the value of all fees actually collected by BK Billing from the debtors after their petitions were filed in each of the Captioned Cases. Such funds shall be remitted by Gallon to the debtor that made the payment. The Post-Petition Agreements in each case are found to be void, and neither Gallon nor BK Billing may enforce any claim against the debtors under those contracts. A separate order consistent with this Memorandum Opinion is entered concurrently herewith in each of the Captioned Cases.

(B) impose an appropriate civil penalty against such person.

§ 526 (as amended by Bankruptcy Technical Corrections Act of 2010, Pub. L. 111-327, § 2(a)(2), 124 Stat. 3557).

Section 528 provides in part:

(a) A debt relief agency shall–

(1) not later than 5 business days after the first date on which such agency provides any bankruptcy assistance services to an assisted person, but prior to such assisted person's petition under this title being filed, execute a written contract with such assisted person that explains clearly and conspicuously–

(A) the services such agency will provide to such assisted person; and

(B) the fees or charges for such services, and the terms of payment;

(2) provide the assisted person with a copy of the fully executed and completed contract;

§ 528(a)(1–2).

In the MATTER OF: Allyson Renea CLARK, Debtor.

Panawe Batanado, Plaintiff,

v.

Allyson Renea Clark, Defendant,

Allyson Renea Clark, Counter-Claimant,

v.

Panawe Batanado, Counter-Defendant.

BANKRUPTCY CASE NO. 17-53487-JWC ADVERSARY PROCEEDING NO. 17-5147

United States Bankruptcy Court, N.D. Georgia, Atlanta Division.

Signed 09/06/2018

Filed 09/07/2018

Background: Man with whom Chapter 7 debtor was involved in eight-year sexual relationship, and who had paid child support for her children in reliance on debtor's representations as to his paternity, brought adversary proceeding to except debt from discharge on "false pretenses, false representation, or actual fraud" theory, and debtor counterclaimed against him to recover for his alleged fraud and intentional infliction of emotional distress.

Holdings: The Bankruptcy Court, Jeffery W. Cavender, J., held that:

whether the trustee had fulfilled her fiduciary duties to the estate when she made her decision. Therefore, it follows that the number of creditors objecting to a proposed settlement should be equally irrelevant when the trustee requests the court to approve a settlement prior to its consummation.

CONCLUSION

[38] Odysseus was within eyesight of his home when a violent storm returned him to his famous travels about the Mediterranean basin. The outcome of the Section 108(b)/Section 365 motion seemed equally within reach last June. However, just as a wiser and more experienced Odysseus finally was allowed to return to Ithaca and his beloved Penelope, this court can now return to the question whose answer once appeared so deceptively close: should the court interpose its own special knowledge concerning the outcome of the Trustee's motion to extend the time to assume or reject the November 1999 Dalen/Metropolitan Judgment Settlement in evaluating whether to approve the settlement which Trustee had reached with Metropolitan Plant. For the reasons stated in this opinion, this court has concluded that it should not have.

The court is further satisfied that the settlement for which the Trustee sought approval meets the standards established by the Sixth Circuit in *Vukovich* and related cases and the requirements of the business judgment rule. This court is satisfied that there is nothing collusive or illegal about the settlement reached and there is nothing to suggest that Trustee had an interest in the outcome of this matter which would call into question his loyalty to the interests of the estate.

This court is similarly satisfied that Trustee made a rational decision after thoughtful consideration of its merits and drawbacks. This court begins with the presumption that the settlement which the Trustee has proposed is reasonable. No creditor or other party in interest has objected to the settlement. Nor is there anything in the record to suggest that Trustee has not exercised reasonable judgment in making his decision. Trustee himself is an attorney and the attorneys whom he retained to represent him are experienced bankruptcy counsel. Although this court ultimately would have ruled in favor of Trustee on the underlying motion, Trustee had no way of knowing this at the time he reached his settlement with Metropolitan and therefore Trustee had to factor the risk of an unfavorable outcome into his calculations.

Therefore, Metropolitan Plant's motion to alter this court's August 25, 2000 order denying the approval of Trustee's settlement with it is granted.[40] This court will issue a separate order consistent with this opinion.

In re William D. CAMPBELL, Debtor.

No. 94–14704.

United States Bankruptcy Court,
N.D. Ohio,
Eastern Division.

Feb. 22, 2001.

United States Trustee (UST) and Chapter 13 debtor sought to cancel debt-

40. One consequence of this decision is that the approval of Trustee's settlement with Metropolitan renders moot the court's separate decision that Trustee may extend the time within which to assume or reject the November 1999 Dalen/Metropolitan Judgment Settlement. Metropolitan Plant has appealed the August 25, 2000 order which extended the Trustee's time to assume or reject that settlement. A copy of this opinion will be forwarded to the District Court.

or's fee agreements with attorney who represented debtor in connection with refinancing that debtor needed to complete his Chapter 13 plan. The Bankruptcy Court, Pat E. Morgenstern-Clarren, J., held that: (1) although some legal services performed for debtor while bankruptcy case is pending may be so unrelated to case as to fall outside scope of attorney fee disclosure statute, services that attorney provided in connection with refinancing that debtor wanted to complete plan were not such services; (2) attorney did not make proper fee disclosure; and (3) appropriate sanction was entry of order cancelling fee agreements and requiring attorney to refund all fees previously collected.

So ordered.

1. Bankruptcy ⚷3179

Fee disclosure requirements of Bankruptcy Code and Bankruptcy Rules are not limited in their application only to attorney representing debtor at time that petition is filed, but also apply to attorneys retained to represent debtor in bankruptcy case after case is filed. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc. Rule 2016(b), 11 U.S.C.A.

2. Bankruptcy ⚷3179

Disclosure, in accordance with attorney fee disclosure requirements of Bankruptcy Code and of Bankruptcy Rules, is critical in permitting court to review fee agreements and payments for reasonableness. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

3. Bankruptcy ⚷3192

Bankruptcy court has express power to review debtor's payments to attorneys for excessiveness and to restore status quo when assets have improvidently been bartered for legal services. Bankr.Code, 11 U.S.C.A. § 329(b); Fed.Rules Bankr.Proc. Rule 2017, 11 U.S.C.A.

4. Bankruptcy ⚷3179

Required disclosure, under bankruptcy statute indicating that debtor's attorney must file with court a statement of compensation paid or agreed to be paid, relates only to services rendered "in contemplation of or in connection with the case." Bankr.Code, 11 U.S.C.A. § 329(a).

5. Bankruptcy ⚷3179

Phrase "in connection with the case," as used in bankruptcy statute defining scope of bankruptcy counsel's required fee disclosures, is broad, and may include services related to precipitating cause of bankruptcy, or services which are inextricably intertwined with bankruptcy. Bankr.Code, 11 U.S.C.A. § 329(a).

See publication Words and Phrases for other judicial constructions and definitions.

6. Bankruptcy ⚷3179

Phrase "in connection with the case," as used in bankruptcy statute defining scope of bankruptcy counsel's required fee disclosures, is not so broad as to include every service rendered to person who is debtor. Bankr.Code, 11 U.S.C.A. § 329(a).

7. Bankruptcy ⚷3179

While some legal services performed for debtor while bankruptcy case is pending may be so unrelated to case as to fall outside scope of attorney fee disclosure statute, services that attorney provided to debtor in connection with refinancing that debtor wanted to complete plan early and to obtain discharge were not such services; rather, attorney was obligated to make required statutory disclosure of any compensation paid or agreed to be paid in connection with such services. Bankr. Code, 11 U.S.C.A. § 329(a).

8. Bankruptcy ⚷3179

Compliance with attorney fee disclosure requirements of Bankruptcy Code and Bankruptcy Rules is crucial to administration and disposition of cases before bankruptcy courts. Bankr.Code, 11

U.S.C.A. § 329; Fed.Rules Bankr.Proc. Rule 2016(b), 11 U.S.C.A.

9. Bankruptcy ⟹3179

Compliance with attorney fee disclosure requirements of Bankruptcy Code and Bankruptcy Rules is mandatory. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

10. Bankruptcy ⟹3179

Counsel's fee revelations must be direct and comprehensive; coy or incomplete disclosures that leave court to ferret out pertinent information from other sources will not suffice. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

11. Bankruptcy ⟹3179

Attorney fee disclosure requirements of Bankruptcy Code and of Bankruptcy Rules are fundamentally rooted in fiduciary relationship between attorneys and courts. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

12. Bankruptcy ⟹2187

Bankruptcy courts have inherent power to sanction attorney for breach of his/her fiduciary fee disclosure obligations. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

13. Bankruptcy ⟹2187

Failure to comply with disclosure rules is sanctionable violation, even if proper disclosure would have shown that attorney had not actually violated any Bankruptcy Code provision or any Bankruptcy Rule. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

14. Bankruptcy ⟹2187

Sanctions may be imposed for attorney's negligent or inadvertent failures to disclose fees. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

15. Bankruptcy ⟹3179

Fee "disclosure" that was buried in another document, did not refer to pertinent Bankruptcy Rule, was not served on United States Trustee, did not address whether debtor's attorney had agreed to share compensation, and was not separately signed by attorney did not comply with Bankruptcy Code or Bankruptcy Rules, either in letter or spirit, and did not constitute proper fee disclosure by debtor's attorney. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

16. Bankruptcy ⟹3179

Bankruptcy counsel's fee disclosure must be straightforward, whether disclosure is made when case is filed or at later time. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

17. Bankruptcy ⟹3179

Counsel's fee disclosure should include clear reference to disclosure rule, and should address each element of that rule. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

18. Bankruptcy ⟹3172.1, 3181, 3192

Debtors' counsel in Chapter 13 cases may be awarded reasonable compensation for representing debtor, but may not be paid without court approval. Bankr.Code, 11 U.S.C.A. § 330.

19. Bankruptcy ⟹3194

Reasonable compensation for debtor's counsel is determined using lodestar analysis. Bankr.Code, 11 U.S.C.A. § 330.

20. Bankruptcy ⟹3179

Failure by debtor's counsel to obey mandate of Bankruptcy Code and of Bankruptcy Rules concerning fee disclosure, and by implication review by court, is basis for entry of order denying compensation, and requiring return of sums already paid. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

21. Bankruptcy ⚷2187

Sanction imposed for attorney's violation of fee disclosure obligations must be commensurate with egregiousness of conduct, and will depend on particular facts of case. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

22. Bankruptcy ⚷3179

If attorney's failure to disclose compensation paid or agreed to be paid is willful, bankruptcy court must deny all compensation. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc.Rule 2016(b), 11 U.S.C.A.

23. Bankruptcy ⚷2187

Appropriate sanction for attorney's failure to disclose her bankruptcy-related fee agreements with, and fees paid by, debtor, failure to maintain adequate records of work she performed for debtor, and failure to produce any support for $1,600.00 in fees that she demanded for services provided in connection with refinancing that debtor needed to complete Chapter 13 plan and to obtain discharge was entry of order cancelling fee agreements and requiring attorney to refund all fees previously collected. Bankr.Code, 11 U.S.C.A. § 329; Fed.Rules Bankr.Proc. Rule 2016(b), 11 U.S.C.A.

Sheldon Stein, Cleveland, for William D. Campbell.

Dean Wyman, Office of the U.S. Trustee, Cleveland, for the United States Trustee.

Joanne Brown, Virgil Brown, Jr., Cleveland, for Joanne Brown.

MEMORANDUM OF OPINION

PAT E. MORGENSTERN–CLARREN, Bankruptcy Judge.

This attorney fee dispute arises out of Chapter 13 Debtor William Campbell's attempts to refinance his home mortgage loan after confirmation of his plan of reorganization and while his case was still pending. The United States Trustee filed a motion to review fees paid post-confirmation by the Debtor to Attorney Joanne Brown, to cancel the fee agreement between them, and to order a refund of fees. The Debtor joins in the motion. The movants contend that Ms. Brown received $700 in fees in connection with the attempted refinancing without a court order or adequate disclosure and that she is improperly attempting to collect an additional $800 through a state court lawsuit. (Docket 65, 68, 82).

Ms. Brown responds with several points. With respect to some of the fees, she claims that she did not need court authority because they were not for legal services at all or, if they were for legal services, they were not for services connected to the bankruptcy case. With respect to others, Ms. Brown alleges that she did make adequate disclosure. Finally, in the event that her position is not accepted, she disputes the amount of fees paid and argues that disgorgement is too severe a sanction. (Docket 81).

The Court held an evidentiary hearing on January 16 and 17, 2001. For the reasons stated below, the Court finds that all fees were for legal services related to the bankruptcy, that Ms. Brown did not adequately disclose the fees, and that disgorgement is the appropriate remedy.

JURISDICTION

The Court has jurisdiction under 28 U.S.C. § 1334 and General Order No. 84 entered on July 16, 1984 by the United States District Court for the Northern District of Ohio. This dispute is a core proceeding under 28 U.S.C. § 157(b)(2) because it arises in a bankruptcy case and involves the application of Title 11 and the Bankruptcy Rules. *See Michigan Employment Sec. Comm'n v. Wolverine Radio Co. (In re Wolverine Radio Co.),* 930 F.2d 1132, 1144 (6th Cir.1991) (citations omitted) (determining that core proceedings

include proceedings arising under title 11 and proceedings arising in title 11 cases and noting that "[t]he phrase 'arising under title 11' describes those proceedings that involve a cause of action created or determined by a statutory provision of title 11 ... and 'arising in' proceedings are those that, by their very nature, could arise only in bankruptcy cases."). *See also In re Bressman,* 214 B.R. 131, 132 (Bankr. D.N.J.1997) ("Issues relating to the debtor's retention and compensation of bankruptcy counsel pursuant to §§ 328, 329, 330 and 331 of the Bankruptcy Code are 'core' proceedings as defined by Congress in 28 U.S.C. § 157."); *In re Telemaintenance, Inc.,* 157 B.R. 352, 354 (Bankr. N.D.Ohio 1993) (review of attorney compensation under § 329 is a core proceeding under 28 U.S.C. § 157(b)(2)(A)).

FACTS

The parties agree about very little in this case, from the underlying facts to the applicable law. This recitation of the facts reflects the Court's findings of fact after considering all of the evidence. In weighing the evidence and determining the credibility of the witnesses, the Court considered the witness' demeanor, the substance of the testimony, and the context in which the statements were made. Fed. R. Bankr. P. 7052, incorporating Fed. R. Civ. P. 52; Fed. R. Bankr. P. 9014.

A. *Background*

At the time the Debtor filed his Chapter 13 case, he owed money on a note to First Nationwide Mortgage Corporation, which note was secured by a mortgage on the Debtor's house. The Debtor's Chapter 13 plan required him to make regular monthly payments to First Nationwide and additionally to make monthly payments to the Chapter 13 Trustee to satisfy pre-petition obligations. The order confirming the plan also included these provisions:

1. Alan Silver, then counsel to the Debtor, was authorized to receive $600 in fees for his services;
2. The Debtor was prohibited from incurring additional debt exceeding $500 in the aggregate without Court approval; and
3. The Debtor was prohibited from transferring any interest in real property without Court approval.

(Docket 22).[1]

Like many others in similar situations, the Debtor later sought to refinance his existing home mortgage loan with a new lender to consolidate his debts. He intended to use the new loan proceeds to pay in full the balances due on the First Nationwide loan and the Chapter 13 plan (and receive his Chapter 13 discharge earlier than he otherwise would) with the hope that his one new monthly payment would be less than the existing payments. To accomplish this, the Debtor, through Mr. Silver, filed a motion to approve a new loan with AMRESCO Residential Mortgage Corporation, as he was required to do under the confirmation order before incurring significant new debt or transferring real estate.

After a hearing, the Court granted the motion as amended. The order giving the Debtor authority to enter into this transaction was entered on August 20, 1997, but the loan never closed. (Docket 34, 36, 37, 40).

This is the point where the dispute between the Debtor and Ms. Brown begins.

B. *The Relationship between the Debtor and Ms. Brown created in September 1997*

The next month, the Debtor approached attorney Virgil Brown, Jr. for legal assistance in connection with the hoped-for refinancing. The Debtor testified that he

1. The order is a standard form that has been required for use in this division for several years.

sought new counsel because Mr. Silver had not completed the paperwork to close the AMRESCO loan. Because the Debtor still wanted to refinance his house, he had applied for a different loan with American Business Credit. He wanted an attorney to handle the legal work with respect to this alternative refinancing so that he could obtain his Chapter 13 discharge.

Mr. Brown was not available and referred the Debtor to Ms. Brown, his law associate. The Debtor gave Ms. Brown paperwork from American Business Credit and a statement relating to the Chapter 13 case. At that first meeting, the Debtor signed a document titled "Attorney Client Agreement" (the "Agreement"). The parties disagree as to the relationship they entered into at that time, with the Debtor believing that he had hired an attorney in his Chapter 13 case and Ms. Brown denying an attorney-client relationship.

The Agreement states in part:

> I, William Campbel [sic]... request of, Joanne Brown ... hereinafter called Attorney, that she advise and represent and prepared [sic] any necessary and incidental documents regarding ***acquiring buy-out amount for mortgage loan on residential home and amount of buy-out on Chapter 13 plan to assist in ending the plan.*** And any and all thing [sic] necessary or incidental to the above activity. In return I agree to pay Attorney an hourly fee of 00.00 or a flat estimated fee of *$750.00.* This fee is to be paid as follows: $*300.00 down* ....

(UST Exh. 4; emphasis in original).[2] Ms. Brown did not file a fee application or Bankruptcy Rule 2016 fee disclosure in connection with this Agreement.

Ms. Brown denied that the Debtor hired her under the Agreement to perform legal services. Instead, she testified that the Debtor only wanted her to find out how much money he owed to certain creditors whose names appeared on a list that he gave her, some of whom were included in the Chapter 13 plan and some of whom were not. Although she told him that he did not need an attorney to get that information, he persisted and so she agreed to help him with what she characterized as ministerial acts outside of the bankruptcy case, rather than legal acts in connection with the Chapter 13.

In a letter to the Cleveland Bar Association Grievance Committee, however, Ms. Brown stated in part that "Mr. Campbell has obtained *my services as an attorney* on three separate occasions. [The first was] September 16, 1997 at a fee of $750...." (Brown Exh. 3) (emphasis added).[3] Beyond that, on November 10, 1997, Ms. Brown filed a Notice of Appearance in the Chapter 13 case in which she stated that "Attorney Joanne Brown ... has been retained as Attorney for William D. Campbell in the above captioned proceedings. Copies of all further communications, pleadings, court notices, and other papers should be served upon the undersigned as Attorney of Record." (Docket 42). Ms. Brown testified that she only entered this appearance because the Debtor asked her to get and forward to him copies of documents filed in his case, and not because she was going to represent him in the Chapter 13. The Court did not find this explanation convincing.

After considering all of the evidence, the Court finds the Debtor's testimony on this point to be credible and concludes that Ms. Brown did agree in September 1997 to act as the Debtor's lawyer in connection with the Chapter 13 case.

C. *How many other agreements did Ms. Brown and the Debtor enter into?*

Ms. Brown testified that she entered into a total of four written agreements

2. The Debtor has adopted all of the United States Trustee's exhibits.

3. The Court notes that the flat fee of $750 is an amount that many Chapter 13 counsel charge a debtor for handling a routine Chapter 13 case.

with the Debtor from September 1997 forward, while the Debtor testified that he only entered into the Agreement and one additional oral agreement. The issue is relevant because Ms. Brown contends that some of the fees she received from the Debtor related to non-bankruptcy work under separate written agreements.

Normally, the question of how many agreements a lawyer entered into with a client would be easy to answer by reference to the lawyer's file and the written agreements. The easy answer is not available in this case because Ms. Brown acknowledges that she lost the Debtor's file in connection with office remodeling upheaval and she does not have copies of the agreements.

Resolving this point again requires weighing the evidence and considering conflicting testimony. Ms. Brown testified she entered into a second written agreement with the Debtor for legal services relating to a traffic ticket on November 5, 1997 for a flat fee of $100 (the "Second Agreement"). The Debtor denied this, and testified that he did consult Ms. Brown about a traffic ticket, but in the context of needing car insurance which Virgil Brown Insurance then sold to him. The Court finds that there is insufficient evidence to establish that the parties entered into the Second Agreement or what the terms of the agreement might have been.

The parties agree that they met again in about June 1998. The American Business Credit transaction had not yet closed (for reasons not established by the evidence) and the Debtor still wanted to go forward. Ms. Brown testified that she and the Debtor entered into a third and fourth written agreement on June 22, 1998. According to her testimony, the third agreement related to the Chapter 13 case and provided that the Debtor would pay her an additional $800 fee for the refinancing work (the "Third Agreement"). The Debtor acknowledged that he agreed to pay this amount, but only from the proceeds of the new loan as part of the closing. He also denied having signed a Third Agreement to that effect. Having considered the competing versions of what went on, the Court concludes that while the Debtor and Ms. Brown did enter into another agreement at that time with respect to the Debtor's Chapter 13 case, there is insufficient evidence to prove what the terms of that Third Agreement were, including whether the Debtor unconditionally promised to pay an additional $800 or whether the payment was only to be made out of the loan proceeds.

The remaining question is whether the Debtor and Ms. Brown entered into a fourth agreement, also dated June 22, 1998, relating to a matter other than the bankruptcy case (the "Fourth Agreement"). Ms. Brown testified that this Fourth Agreement, calling for yet another $800 payment, was for another type of loan, but she did not provide details about it. She did offer into evidence a cognovit promissory note (the "Note") signed by the Debtor, with a typed date of June 22, 1998, in which he promised to repay $800 within 30 days with interest at 8% per year from the date on which the Note was executed. (Brown Exh. 1; ¶ 2). The Note further stated that if any installment was not paid when due there would be an additional $25 late charge for each month the payment was due and unpaid. Ms. Brown acknowledged that the Debtor did not borrow any money from her. She testified that she actually had him sign the Note to emphasize the importance of the attorney-client agreement.

As noted, Ms. Brown did not explain what this non-bankruptcy matter was and there is no file to support it. The Court also returns to the correspondence from Ms. Brown to the Cleveland Bar Association in which she stated that:

> Mr. Campbell has obtained my services as an attorney on three separate occasions. September 16, 1997, at a fee of $750, November 5, 1997 at a fee of $100 and *June 22, 1998 at a fee of $800.* On

> each of those occasions he signed the attorney client agreements, include [sic] with this document ....

(Brown Exh. 3) (emphasis added).[4] Ms. Brown testified that she did not refer to the Fourth Agreement in this letter because it was not the subject of the Association's inquiry. Regardless, the Court finds that if there had, in fact, been a Fourth Agreement entered into on that same date, it is more likely than not that Ms. Brown would have referred to it in this letter. Finally, the Debtor denied having entered into a Fourth Agreement or having agreed to pay an additional $800 in fees for a non-bankruptcy matter. On review of all of the evidence, the Court finds that there is insufficient evidence to prove that the Debtor and Ms. Brown entered into a Fourth Agreement or what the terms of that agreement might have been.

In sum, the evidence established that the Debtor and Ms. Brown entered into the Agreement in September 1997 under which the Debtor agreed to pay her $750 to serve as his lawyer in the Chapter 13. The evidence also established that they entered into the Third Agreement in June 1998 relating to the Chapter 13, although there was insufficient evidence to prove the terms of that agreement.

D. *How much did the Debtor pay to Ms. Brown under the Agreement?*

The question of how much the Debtor actually paid to Ms. Brown under the Agreement would, again, ordinarily be easy to answer by reference to the attorney's accounting records, including ledger books and bills. Those documents were, however, also lost.

The testimony again conflicted. Ms. Brown testified that the Debtor paid between $400 and $450 of the $750 due under the Agreement, with any other payments being attributable to one of the other three alleged agreements. The Debtor testified that he paid $700 of the $750.

The UST introduced into evidence several receipts which shed some light on this issue (UST Exh. 5):

Date	What the Receipt Says
9/16/97	Credit 125; balance 625

The date and these amounts are consistent with $125 having been paid against the $750, leaving a balance of $625.

9/18/97	Paid 175; retainer payment

Again, the date and amount are consistent with $175 having been paid against the $625 balance, leaving a new balance of $450.

10/28/97	300 balance

This receipt, more likely than not, shows that the Debtor paid an additional $150, leaving a new balance of $300.

11/5/97	Credit 100; balance 50

There are no receipts for payments made between October 28, 1997 and November 5, 1997, but it is more likely than not that the Debtor did make a $150 payment in that time period, leaving a $150 new balance, especially because there is a note on Exhibit 5 that says "Amount due $150." Starting with that $150 balance and crediting a $100 payment on November 5, 1997 leaves a new balance of $50 on the original $750, as reflected on this receipt.

In sum, the Court concludes based on all of the evidence that the Debtor paid $700 of the $750 called for by the Agreement.[5]

E. *The Return to the Bankruptcy Court in June 1998*

Starting on June 22,1998, Ms. Brown filed a Motion, an Amended Motion, and a Second Amended Motion seeking authority for the Debtor to borrow money from

4. The copy of this document introduced by Ms. Brown into evidence did not have attachments.

5. The Debtor suggested that Ms. Brown also received legal fees paid through the Chapter 13 Trustee's office. Ms. Brown denied receiving any such funds and there was insufficient evidence to prove receipt of additional funds.

American Business Credit (again to consolidate his debts and pay off the Chapter 13 plan) and setting a hearing date of July 14, 1998. (Docket 44, 45, 46). The filings did not comply with Administrative Order 98–1,[6] which specifies the information that must be included in a motion to incur new debt. The hearing was adjourned by the Court to give the Debtor the opportunity to comply and a new hearing was set for August 11, 1998. (Docket entry 7/14/98).

Within the time allotted, the Debtor filed two supplemental documents. (Docket 49, 50). The hearing went forward, the Court granted the motion in part, and an order to that effect was entered on August 28, 1998 (the "Order"). (Docket 52).

F. *Ms. Brown Demands Payment of $1,600 in Legal Fees*

On September 2, 1998, Ms. Brown sent the Debtor a letter telling him that she had received a copy of the Order and that he would be getting a copy as well (presumably from the Court, although it is not clear why Ms. Brown did not send a copy to him). She then stated:

> This fulfills my obligation as outlined in the Attorney Client Agreement dated June 22, 1998. Please forward, by September 8, 1998, to my office a check for $1,600.00, (One Thousand Six Hundred Dollars and No Cents) representing payment of legal fees for drafting and filing motions, attending hearings on motions, negotiations with American Business Credit, and Tower City Title, obtaining amount needed to pay-off loan to First Nationwide Mortgage and the Chapter 13 Trustee.

(UST Exh. 7). She followed this up with a letter dated September 4, 1998 stating:

> . . . This process has taken over almost a year [7] and it [sic] my understanding that your loan which was to close on August 28, 1998, base [sic] on the information I provided to you, Jeff and Tower City Title, was canceled, because of your lack of cooperation . . . As I indicated in my letter of September 2, 1998, I am requesting payment of legal fees by September 8, 1998. If payment is not receive [sic] by that date I will have no choice but to seek other recourse to enforce my rights . . . .

(UST Exh. 8). At the hearing, Ms. Brown did not offer a credible explanation for how she arrived at the conclusion that the Debtor owed $1,600 in legal fees. Although she suggested that the $1,600 was for more than the work described in the letter, she did not provide evidence of the work she performed using the lodestar standard.[8]

In the absence of time records, the Court has considered the description in the above correspondence of the work performed, consisting of obtaining pay-off numbers, drafting motions, appearing in court, and negotiating with the lender and title company. The pay-off amount from the Chapter 13 Trustee is typically obtained through a letter to that office. Obtaining a pay-off number from a mortgage loan holder may take slightly longer, but it is generally not a time-consuming task. Preparing an application for authority to refinance is straightforward in that Administrative Order 98–1 advises counsel what needs to be included. If that information is contained in the original filing, then only

6. Northern District of Ohio General and Administrative Orders, together with the undersigned's standing orders and memoranda, are on the court's web site at www.ohnb.uscourts.gov. and are available in the Clerk's office.

7. One year before this letter would have been September 1997, which further supports the conclusion that Ms. Brown agreed in September 1997 to serve as the Debtor's attorney in connection with the refinancing.

8. The lodestar calculation generally requires multiplying the reasonable number of professional hours expended by the reasonable hourly rate for those services. *Boddy v. United States Bankruptcy Court, Western District of Kentucky (In re Boddy),* 950 F.2d 334 (6th Cir.1991).

one filing and hearing are generally needed. Ms. Brown did not testify about the referenced negotiations with the lender and title company, but debtors usually have little leverage in refinancings and there are few issues to negotiate. Based on the Court's assessment of the work done here, and having reviewed countless applications for similar work under the lodestar standard, the Court finds that typically it would involve about 2 to 3 hours of work at a rate in the range of $150 an hour and that a reasonable fee would be no more than that.

G. *Ms. Brown Sues the Debtor in State Court*

When the Debtor did not pay, Ms. Brown sued him in state court. The record is not clear as to what happened to the original complaint, but in September 2000 Ms. Brown filed an Amended Complaint. In that Amended Complaint, Ms. Brown sued on the Note, alleging that:

> The note was given for the following business purpose: Legal fees associated with obtaining information and securing court permission to seek a business loan . . . .

(UST Exh. 9). She demanded judgment for $800 plus interest at 8% from July 22, 1998 and costs. That lawsuit is pending.

Ms. Brown testified that the Amended Complaint is inaccurate, but she did not clarify what cause of action she hoped to pursue. The argument may have been that the lawsuit should be permitted to proceed because it is unrelated to bankruptcy work. To the extent that this is the argument, the Court finds that the Amended Complaint is not unrelated to the Chapter 13, but is instead an effort to collect additional fees for bankruptcy legal work as discussed above. The additional or alternative argument that Ms. Brown may have been making is that the fees do relate to the Chapter 13 under the Third Agreement, that she appropriately disclosed them, and that the Order authorized her to collect them. That argument is discussed further below.

H. *Ms. Brown's Knowledge of the Code, Rules, and Orders relating to compensation of professionals in Chapter 13 cases*

Ms. Brown, who has been a member of the Ohio Bar since about 1978, testified that she has been in active practice for approximately 8 of the years from that date to the present, having taken time off at various points for family reasons. She has handled several bankruptcy matters, including representing debtors in cases under Chapter 7 and 13 and serving as counsel to Mr. Brown in his capacity as a Chapter 7 Trustee. Ms. Brown was not, however, able to estimate the number of bankruptcy matters that she has handled and did not provide details of her bankruptcy work.

Until this motion was filed about six months ago, Ms. Brown was not familiar with Bankruptcy Rule 2016 "Compensation for Services Rendered and Reimbursement of Expenses" or Bankruptcy Code § 329 "Debtor's Transactions with Attorneys." She had filed statements that complied with Rule 2016 in other cases, but only when she was the lawyer filing the case. She contended that counsel is not required to file the same Rule 2016 statement when counsel enters a case after it has been filed, but that the requirement is, in effect, somewhat relaxed.

With respect to Bankruptcy Code § 330 "Compensation of Officers," Ms. Brown testified that she was more familiar with it at the time of the hearing than she had been before, but she did not know how long she had been familiar with it. Ms. Brown was not aware of Administrative Order 93–1 "Amended and Restated Order Governing Procedure for Allowance of Attorneys Fees in Chapter 13 cases" until this motion was filed. She was not generally aware that attorneys are prohibited from receiving fees in respect of a bankruptcy case in this district after the case is

filed and while it is pending, absent court order. Similarly, Ms. Brown did not recall whether she had read Administrative Order 98–1, governing motions to incur new debt, including refinancing, before she filed the motion to approve the loan.[9]

THE RELIEF SOUGHT AND THE RESPONSE

The Debtor and the UST ask that the Agreement be cancelled, that Ms. Brown be ordered to return the monies paid by the Debtor, and that she be enjoined from collecting any further amounts. Ms. Brown asks that she be found entitled to the money already paid and permitted to proceed with the state court lawsuit.

DISCUSSION

A. *Disclosure of Compensation Required*

[1] Bankruptcy Code § 329 requires a debtor's attorney to make certain disclosures regarding compensation:

> (a) Any attorney representing a debtor in a case under this title, or in connection with such a case, whether or not such attorney applies for compensation under this title, shall file with the court a statement of the compensation paid or agreed to be paid, if such payment or agreement was made after one year before the date of the filing of the petition, for services rendered or to be rendered in contemplation of or in connection with the case by such attorney, and the source of such compensation.

11 U.S.C. § 329(a). This section was enacted because "[p]ayments to a debtor's attorney provide serious potential for evasion of creditor protection provisions of the bankruptcy laws, and serious potential for overreaching by the debtor's attorney, and should be subject to careful scrutiny." H.R.Rep. No. 95–595, at 329 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5787, 6285. *See also Jensen v. United States Trustee (In re Smitty's Truck Stop, Inc.),* 210 B.R. 844, 848 (10th Cir. BAP 1997) ("The purpose of this process is to prevent overreaching by an attorney and provide protection for creditors."). An attorney who is retained to represent a debtor in a case after it has been filed is required to make a § 329 disclosure. *Mapother & Mapother, P.S.C. v. Cooper (In re Downs),* 103 F.3d 472, 477 (6th Cir.1996).

Bankruptcy Rule 2016(b) implements § 329 and provides:

> (b) *Disclosure of Compensation Paid or Promised to Attorney for Debtor.* Every attorney for a debtor, whether or not the attorney applies for compensation, shall file and transmit to the United States trustee within 15 days after the order for relief, or at any other time as the court may direct, the statement required by § 329 of the Code including whether the attorney has shared or agreed to share the compensation with any other entity ... A supplemental statement shall be filed and transmitted to the United States trustee within 15 days after any payment or agreement not previously disclosed.

FED. R. BANKR. P. 2016(b). As with § 329, an attorney retained as debtor's counsel after a case is filed is required to meet the 15 day supplemental disclosure provisions of this rule. *In re Downs,* 103 F.3d at 477.

[2, 3] Disclosure is critical because it permits a court to review fee agreements and payments for reasonableness. If review shows that the compensation is not reasonable, the court may cancel the agreement or order a refund of payments made. 11 U.S.C. § 329(b). Bankruptcy

9. The Court admitted evidence at the hearing concerning another case in which Ms. Brown served as debtor's counsel, for the limited purpose of showing when Ms. Brown knew about the disclosure rules. *(In re Broadnax,* Case No. 98–50742, N.D. Ohio, Eastern Division at Akron). On further reflection, the Court concludes that the *Broadnax* evidence is not relevant even for the limited purpose for which it was admitted, and the Court has not given any weight to it in this Opinion.

Rule 2017 implements this provision. FED. R. BANKR. P. 2017. Taken together, § 329 and Rule 2017 "furnish the court with express power to review payments to attorneys for excessiveness and to restore the status quo when assets have improvidently been bartered for legal services[.]" *In re Martin,* 817 F.2d 175, 180 (1st Cir.1987).

[4–6] The required disclosure relates only to services rendered "in contemplation of or in connection with the case[.]" The scope of the phrase "in connection with the case" is broad. *In re Keller Fin. Servs. of Fla., Inc.,* 248 B.R. 859, 878–79 (Bankr.M.D.Fla.2000); *Cohn v. U.S. Trustee (In re Ostas),* 158 B.R. 312, 321 (N.D.N.Y.1993). "The phrase may include services related to the precipitating cause of the bankruptcy, or services which are inextricably intertwined with the bankruptcy." *In re Keller Fin. Servs. of Fla.,* 248 B.R. at 879. *See also In re Hargis,* 148 B.R. 19, 21 (Bankr.N.D.Tex.1991) (holding in the Chapter 11 context that services by an attorney which enhance, preserve, litigate, or discharge liabilities, or which affect assets of the debtor are services in connection with the case). The phrase is not so broad, however, that it includes every service rendered to a person who is a debtor. *See for example, In re Swartout,* 20 B.R. 102 (Bankr.S.D.Ohio 1982) (determining that services related to a debtor's divorce proceeding were not connected to the bankruptcy case within the meaning of § 329).

[7] Ms. Brown argues that she was not required to disclose the Agreement or the fees paid because she did not agree to represent the Debtor in his Chapter 13 case in September 1997 and the services were not related to that case.[10] As found above, Ms. Brown did agree to represent the Debtor at that time in connection with the refinancing in an effort to get his Chapter 13 discharge. The debtor's right to obtain a discharge in exchange for meeting his or her obligations under the plan is the heart of a Chapter 13 case and services relating to that issue are clearly rendered in connection with the case, whether they are performed at the beginning of a case or mid-stream. Therefore, while some legal services performed for a debtor while a bankruptcy is pending may be so unrelated to the bankruptcy case that they fall outside the scope of § 329, services connected to obtaining a discharge are not such services. Consequently, the Bankruptcy Code and Rules required Ms. Brown to disclose the Agreement and payments received under it.

B. *Failure to Disclose*

[8–10] Compliance with § 329 and Rule 2016 is "crucial to the administration and disposition of cases before the bankruptcy courts." [11] *In re Downs,* 103 F.3d at 480. Compliance is mandatory. "Coun-

10. In support of this argument, Ms. Brown cites cases which discuss bankruptcy jurisdiction as to related matters. See *Loomis Elec. Inc. v. Lucerne Prods., Inc.,* 225 B.R. 381 (N.D.Ohio 1998) (holding that a contractor's removed state court action against a debtor for amounts due was a related proceeding); *176–60 Union Turnpike, Inc. v. Howard Beach Fitness Center, Inc.,* 209 B.R. 307 (S.D.N.Y. 1997) (holding that a debtor's removed state court negligence claims were not related proceedings). These cases are factually different and are not relevant to the determination of whether Ms. Brown's services were rendered in connection with Mr. Campbell's case for purposes of § 329. Moreover, these cases are not relevant on the issue of jurisdiction, because (as previously discussed) this matter is a core proceeding involving the administration of this bankruptcy case and is within this court's jurisdiction. See 28 U.S.C. §§ 1334 and 157(b)(2)(A).

11. The failure to comply with these disclosure requirements is especially significant in Chapter 13 and 7 cases. *See In re Bell,* 212 B.R. 654, 657 (Bankr.E.D.Cal.1997) (noting that the disclosure requirements are especially significant in a Chapter 13 case, because the court does not approve the employment of Chapter 13 counsel); *In re Saturley,* 131 B.R. 509, 517 (Bankr.D.Me.1991) (stating that transactions between Chapter 7 debtors and their counsel should be subject to particular scrutiny).

sel's fee revelations must be direct and comprehensive. Coy or incomplete disclosures which leave the court to ferret out pertinent information from other sources are not sufficient." *In re Saturley,* 131 B.R. 509, 517 (Bankr.D.Me.1991).

[11–14] "Section 329 and Rule 2016 are fundamentally rooted in the fiduciary relationship between attorneys and the courts." *In re Downs,* 103 F.3d at 480. Bankruptcy courts have the inherent power to sanction an attorney for a breach of this fiduciary obligation. *In re Downs,* 103 F.3d at 478. The "failure to comply with the disclosure rules is a sanctionable violation, even if proper disclosure would have shown that the attorney had not actually violated any Bankruptcy Code provision or any Bankruptcy Rule." *Neben & Starrett, Inc. v. Chartwell Fin. Corp. (In re Park–Helena Corp.),* 63 F.3d 877, 880 (9th Cir. 1995). Sanctions may also be imposed for negligent or inadvertent failures to disclose. *In re Park–Helena Corp.,* 63 F.3d at 881.

[15] The $700 paid under the Agreement admittedly was not disclosed and the Court concluded above that it should have been. Ms. Brown argues that she did disclose an additional $850 fee that the Debtor allegedly agreed to pay in connection with the Third Agreement relating to the refinancing effort. For support, she relies on the supplement to the motion for authority to refinance, which was ultimately attached as an exhibit to the Order. Ms. Brown contends that this attachment established her right to receive additional fees and satisfied her disclosure obligations.

First, while the Court has found that there was a bankruptcy-related Third Agreement, the Court also found that there was insufficient evidence to show that the Debtor unconditionally agreed to pay an additional fee in connection with the refinancing and so the Debtor is not responsible to pay those funds regardless of disclosure. Even if he had so agreed, however, the documents filed by Ms. Brown did not provide appropriate disclosure of the Third Agreement. The supplement consists of several pages. Exhibit A to it, titled "Estimated Costs" has two lines for attorneys fees, both of which are marked "$.00." Exhibit C, "Settlement Charges," includes this line item: "Attorney Fee to Joanne Brown, Attorney." The amount of $850 then appears across from that line item under the column heading: "Paid From Borrower's Funds at Settlement."

[16, 17] This information does not comply with the Code or the Rules, either in letter or spirit. The law requires that a disclosure be straightforward, whether the disclosure is made when the case is filed or at a later time. To meet that standard, a disclosure should include a clear reference to Rule 2016 and should address each of the elements of that Rule. Here, the "disclosure" is buried in another document, does not refer to Rule 2016, was not served on the United States Trustee, does not address whether Ms. Brown had agreed to share compensation, and is not separately signed by Ms. Brown.

The Court also notes that there are two inconsistencies between Ms. Brown's testimony and this exhibit: (1) the $850 amount in Exhibit C is inconsistent with her testimony that she had agreed to accept $800 for the additional refinancing work; and (2) the exhibit states that the fees are to be paid from the loan proceeds, while Ms. Brown's testimony was that the Debtor owed the fees even when the loan did not close.

The Court finds, based on all of the evidence, that Ms. Brown did not adequately disclose this additional fee, even if it were otherwise recoverable, which it is not.

C. *Allowance and Payment of Attorney Fees in Chapter 13 cases*

[18, 19] Debtors' counsel in Chapter 13 cases may be awarded reasonable compen-

sation for representing a Chapter 13 debtor, but may not be paid without court approval. Under § 330, "... the court may allow reasonable compensation to the debtor's attorney for representing the interests of the debtor in connection with the bankruptcy case based on a consideration of the benefit and necessity of such services to the debtor and the other factors set forth in this section." 11 U.S.C. § 330(a)(4)(B). Reasonable compensation is determined using a lodestar fee analysis. *In re Boddy.* In this division, Administrative Order No. 93–1 provides that:

> In accordance with the Bankruptcy Code and Rules no attorney may, directly or indirectly receive any fees in respect of a case after the case is filed and while it is pending except pursuant to order of the Court.

Administrative Order 93–1, ¶ 3.[12]

If Ms. Brown had followed the applicable law, she would have been eligible to receive fees for the legal work she performed on behalf of the Debtor. The situation, however, is that Ms. Brown first failed to disclose the Agreement under § 329 and Rule 2016(b) and then compounded the problem by receiving $700 in fees in violation of Administrative Order No. 93–1 and § 330 and suing the Debtor in an attempt to recover more fees.

D. *The Appropriate Sanction*

[20–22] The " 'failure of counsel to obey the mandate of § 329 and Rule 2016 concerning disclosure, and by implication review by the Court, is a basis for entry of an order denying compensation and requiring the return of sums already paid.' " *In re Downs,* 103 F.3d at 477 (quoting *In re Chapel Gate Apartments, Ltd.,* 64 B.R. 569, 575 (Bankr.N.D.Tex.1986)). The sanction imposed must "be commensurate with the egregiousness of the conduct" and will depend on the particular facts of the case. *In re Downs,* 103 F.3d at 478–480. If, however, the failure to disclose is willful, a bankruptcy court must deny all compensation. *In re Downs,* 103 F.3d at 479–80.

[23] Ms. Brown argues that if she is found to have violated the rules, she did not do so intentionally and that disgorgement is too harsh a remedy. The United States Trustee requests disgorgement and the Debtor suggests that disgorgement should only be the starting point for the sanction.

In deciding what sanction is appropriate, the Court has considered the totality of the circumstances, including these points:

1. An attorney should disclose all bankruptcy-related fee agreements and fees paid, but Ms. Brown did not;

2. An attorney appearing in the bankruptcy court should be familiar with the Bankruptcy Code and Rules governing professional compensation, as well as with local orders, but Ms. Brown was not;

3. An attorney entering an appearance for a debtor after a case has been filed should review the case file either before or immediately after entering the appearance, but Ms. Brown did not. If Ms. Brown had timely reviewed this file, she would have had the benefit of seeing that Mr. Silver had applied for additional attorney fees and the standards used by the Court to consider that application.[13] She also would have seen that the confirmation order prohibited the Debtor from incurring additional debt greater than $500 without Court approval;

12. Administrative Order No. 93–1 was entered on January 11, 1993 and applies to all cases filed between that date and June 6, 1996. Subsequent Administrative Orders which apply to cases filed after June 6, 1996 include the same provision. See Administrative Orders 96–6, ¶ 5 and 98–4, ¶ 5.

13. In 1996, Mr. Silver applied for, and was granted, an additional $100 in fees, to be paid over 12 months through the plan. (Docket 28, 31). The order granting the application refers to the Bankruptcy Code and Rules, *In re Boddy,* 950 F.2d 334 (6th Cir.1991), General Order No. 93, and Administrative Order No. 93–1.

4. An attorney should maintain adequate records of the work she performs for a debtor, but Ms. Brown did not;

5. An attorney should maintain adequate records reflecting legal fees and filing fees paid by a debtor, but Ms. Brown did not; and

6. An attorney should have support for any fee demand made on a debtor, but Ms. Brown did not.

The Court believes that Ms. Brown acted negligently rather than intentionally in her failure to follow the appropriate procedures. The Court also believes it is entirely possible that the Debtor was not easy to deal with. Nevertheless, the Court concludes that the appropriate sanction is that the Agreement should be cancelled, all fees should be refunded to the Debtor, and no further fees should be collected.

CONCLUSION

For the reasons stated, the fee agreements between the Debtor and Ms. Brown are cancelled, Ms. Brown is ordered to refund $700 to the Debtor, and she is enjoined from collecting further fees from him.

In re Renata Witt DRYJA, Debtor.

Aristocrat Lakewood Nursing Home, Plaintiff,

v.

Renata Witt Dryja, Defendant.

Bankruptcy No. 00–11911.
Adversary No. 00–1372.

United States Bankruptcy Court,
N.D. Ohio,
Eastern Division.

Feb. 26, 2001.

Judgment creditor, which previously had obtained a judgment against Chapter 7 debtor's aunt for arrearages in aunt's nursing home account, brought adversary proceeding against debtor, seeking determination that judgment debt arising from debtor's purportedly fraudulent transfers of money from aunt's checking account was excepted from discharge. The Bankruptcy Court, Randolph Baxter, J., held that: (1) judgment creditor failed to establish the requisite elements of embezzlement, for nondischargeability purposes; (2) judgment creditor failed to show that judgment debt fell within the discharge exception for willful and malicious injury; and (3) under Ohio law, debtor was not collaterally estopped from disputing the fraudulent nature of the transfers.

Judgment for defendant, and debt found dischargeable.

1. Bankruptcy ⚿3420(1), 3422(10.1)

Judgment creditor's burden as complainant in nondischargeability proceeding was to show by a preponderance of the evidence that a dischargeability exception was warranted. Bankr.Code, 11 U.S.C.A. § 523(a)(4).

2. Bankruptcy ⚿3356

For nondischargeability purposes, "embezzlement" means the fraudulent appropriation of property by a person to whom such property has been entrusted or into whose hands it has lawfully come. Bankr.Code, 11 U.S.C.A. § 523(a)(4).

See publication Words and Phrases for other judicial constructions and definitions.

3. Bankruptcy ⚿3356

Creditor proves embezzlement, for nondischargeability purposes, by showing that (1) creditor entrusted creditor's property to debtor, (2) debtor appropriated the property for a use other than that for which it was entrusted, and (3) the circumstances indicate fraud. Bankr.Code, 11 U.S.C.A. § 523(a)(4).

IN RE: J. Timothy SHELNUT, Debtor

Number 17–40113

United States Bankruptcy Court,
S.D. Georgia, Savannah Division.

Signed 10/04/2017

Background: Debtor's counsel filed application seeking attorney fees and expenses in the amount of $44,502.89. United States Trustee (UST) and creditor objected.

Holdings: The Bankruptcy Court, Susan D. Barrett, Chief Judge, held that:

(1) disgorgement of $6,500 payments from non-party, which counsel failed to timely disclose, was warranted;

(2) denial of compensation was not warranted based on conflict of interest;

(3) denial of fee application was not warranted based on debtor's purported bad faith in filing bankruptcy case; and

(4) time spent and rates charged by debtor's counsel were reasonable and not unnecessarily duplicated.

Objections sustained in part and denied in part.

1. Bankruptcy ⚷3155

Bankruptcy Code and Rules require the utmost disclosure and candor from professionals seeking employment and compensation from the bankruptcy estate. 11 U.S.C.A. § 327; Fed. R. Bankr. P. 2014.

2. Bankruptcy ⚷3155

Level of disclosure required by bankruptcy rule governing employment of professional persons is mandatory, regardless of whether the disclosure would expose a conflict of interest. Fed. R. Bankr. P. 2014(a).

3. Bankruptcy ⚷3179

Disclosure duty of bankruptcy rule governing employment of professional persons is a continuing duty, and continues even after counsel's appointment. Fed. R. Bankr. P. 2014(a).

4. Bankruptcy ⚷3179

If a debtor's attorney subsequently receives funds from a non-party, the attorney is required to promptly supplement its disclosure. Fed. R. Bankr. P. 2016(b).

5. Bankruptcy ⚷2187, 3155

Sanctions may be imposed even when the failure to disclose fees was through inadvertence or negligent, and regardless of whether the estate was actually harmed. Fed. R. Bankr. P. 2016(b).

6. Bankruptcy ⚷2187, 3179

Failure by debtor's counsel to timely amend its fee application and disclosure regarding receipt of two post-petition payments from non-party totaling $6,500 warranted disgorgement of the $6,500. Fed. R. Bankr. P. 2016(b).

7. Bankruptcy ⚷2187, 3179

Counsel's failure to properly disclose the required information may result in its disqualification, as well as the disgorgement of fees and imposition of sanctions. Fed. R. Bankr. P. 2016(b).

8. Bankruptcy ⚷3177

Bankruptcy Code provision providing for denial of compensation to professionals who are not disinterested or who have an adverse interest to the bankruptcy estate is permissive and, in the absence of actual injury or prejudice to the debtor's estate, this sanction should not be rigidly applied. 11 U.S.C.A. § 328(c).

9. Bankruptcy ⚷3177

Where attorney fee payments by non-party to debtor's counsel were treated as loan repayments to debtor, denial of compensation was not warranted under Bankruptcy Code provision providing for denial

of compensation to professionals who are not disinterested or who have an adverse interest to the bankruptcy estate. 11 U.S.C.A. § 328(c).

10. Bankruptcy ⚷3178

Denial of fee application was not warranted based on debtor's purported bad faith in filing bankruptcy case as a means to avoid the enforcement of a domestic court order, given that bankruptcy court had granted relief from the stay for former wife to pursue enforcement of the state court order, and in its abstention order, bankruptcy court did not find the bankruptcy case was filed in bad faith as to all creditors or conduct a bad faith dismissal analysis, and parties had settled that dispute and debtor dismissed his appeal and consented to the appointment of a Chapter 11 trustee.

11. Bankruptcy ⚷3769

Motion for relief from stay order was an appealable order. 28 U.S.C.A. § 1334(d).

12. Bankruptcy ⚷3194

Attorney compensation is determined using the "lodestar method," which is the reasonable time expended by counsel in performing the reasonably required services rendered multiplied by a reasonable hourly rate. 11 U.S.C.A. § 330.

13. Bankruptcy ⚷3188

Time spent and rates charged by debtor's counsel were reasonable and not unnecessarily duplicated, as would warrant reduction of fees, where counsel conferred on matters and assigned separate tasks so their combined knowledge and skill could be utilized to best represent debtor. 11 U.S.C.A. § 330.

Tiffany Elizabeth Caron, C. James McCallar, Jr., McCallar Law Firm, Savannah, GA, for Debtor.

James C. Overstreet, Jr., Klosinski Overstreet, LLP, Augusta, GA, for Trustee.

OPINION AND ORDER

SUSAN D. BARRETT, CHIEF UNITED STATES BANKRUPTCY JUDGE

This order addresses the First Application for Attorney's Fees ("Application") filed by the McCallar Law Firm ("MLF") in connection with its representation of J. Timothy Shelnut ("Debtor") as Debtor's counsel. Virginia "Sam" Pannill, f/k/a Virginia P. Shelnut ("Pannill"), and the United States Trustee ("UST") object to the Application. This is a core proceeding under 28 U.S.C. § 157(b)(2)(A) and the Court has jurisdiction to address the matter pursuant to 28 U.S.C. § 1334. For the reasons set forth herein, the objections are sustained in part and denied in part.

FINDINGS OF FACT

MLF's Application seeks attorney fees and expenses in the amount of $44,502.89. The Application includes work performed by two attorneys, C. James McCallar, Jr. ("McCallar") at an hourly rate of $400.00, and Tiffany E. Caron ("Caron") at an hourly rate of $300.00.

In its Disclosure of Compensation of Attorney for Debtor provided pursuant to 11 U.S.C. § 329(a) and Federal Rule of Bankruptcy Procedure 2016(b), MLF certified that the "compensation paid to it within one year before the filing of the petition in bankruptcy, or agreed to be paid to [it], for services rendered or to be rendered on behalf of the debtor[ ] in contemplation of or in connection with the bankruptcy case . . ." by the Debtor has been $8,283.00.

Dckt. No. 1 at 12. MLF certified Debtor was the source of this compensation, and the source of the compensation to be paid to it. Id. MLF also disclosed Debtor has paid an additional $1,717.00 for the filing fee. Id. In the accompanying affidavits provided with the Application to Retain Counsel, both McCallar and Caron certified to the receipt of this $10,000.00 retainer. Dckt. No. 7, ¶ 19–20.

After the petition date, MLF received two payments in connection with its representation of the Debtor: (i) $4,000.00 in February and (ii) $2,500.00 in March. These two payments actually were not made from Debtor's account, but rather from the account of Four Seasons Financial Partners, Inc. ("Four Seasons"), a corporation owned by Debtor. According to Debtor's schedules, Four Seasons owed Debtor $4,484,673.00 as of April 15, 2016.[1] Sch. A/B, Dckt. No. 41. Debtor's schedules also value Four Seasons at $0. Id.

MLF's Application notes it has $11,453.00 on hand to apply to the fee request.[2] Dckt. No. 85 at 3. Pannill deposed Four Seasons' bookkeeper and discovered the two post-petition checks to MLF were drawn on the account of Four Seasons, rather than Debtor's account. MLF has not amended its pleadings to disclose these two post-petition payments were from Four Seasons, rather than Debtor.

For years, Debtor has been in the insurance business selling insurance policies to teachers. Several years ago, Debtor ceased actively selling insurance, but many of the policies continue to generate income based upon renewal premiums and commissions from renewals. Four Seasons is the entity that receives this renewal income. No new policies are actively being sold through Four Seasons. According to Ms. Kathy Kitchens, Four Seasons' bookkeeper, Debtor's personal expenses are being paid from Four Seasons and these payments are designated by a special general ledger number and credited as income to Debtor, and as a loan repayment. Dckt. No. 77, Dep. Tr. 26:3–12; 28:7–15; 30:23–25.

Pannill filed a Motion to Appoint a chapter 11 trustee when she discovered Debtor's actions regarding these renewals and other matters. Dckt. No. 46. Pannill urged the Court to appoint a trustee to take control of these renewals to avoid Debtor's improper depletion of these funds. Ultimately, the parties agreed to the appointment of a chapter 11 trustee and an order was entered giving the trustee control over Four Seasons' income and bank accounts. Dckt. No. 83.

CONCLUSIONS OF LAW

Pannill and the UST object to MLF's Application. Pannill raises five objections to the Application. First, Pannill argues MLF failed to properly disclose that Four Seasons was the source of some of the $11,453.00 on hand to pay its bill. In its post hearing brief, Pannill argues MLF's receipt of the fees from Four Seasons was sufficient to place MLF on notice that Four Seasons was Debtor's alter-ego and negates MLF's required disinterestedness. Second, Pannill argues attorney fees should not be allowed because Debtor filed his bankruptcy in bad faith as a means to avoid the enforcement of a domestic court order finding Debtor in willful contempt

1. The schedules indicate subsequent loan payments have been made since April 15, 2016 and the outstanding balance needs to be updated by the accountant. Sch. A/B, Dckt. No. 41.

2. While the Application does not specify, it appears the $11,453.00 includes the $6,500.00 paid post-petition and the remaining pre-petition retainer.

and ordering his arrest. Third, Pannill contends all fees associated with the appeal of this Court's previous motion for relief order should be disallowed because the order was non-appealable under 28 U.S.C. § 1334(d). Fourth, Pannill contends the time spent by two senior attorneys was an unnecessary duplication of work. Finally, Pannill argues the time and expenses expended by the lawyers are unnecessarily high and unreasonable.

The UST raises three objections to the Application. First, it contends MLF's Application should be reduced for its failure to comply with the disclosure requirements of 11 U.S.C. § 329 and Bankruptcy Rules 2014(c) and 2016. Second, it contends Four Seasons is a non-debtor affiliate and insider of the Debtor. Thus, the UST contends MLF's receipt of the undisclosed payments from Four Seasons negates its disinterestedness and creates a disqualifying conflict because the post-petition transfers are unauthorized and therefore the bankruptcy estate may have a claim against MLF to recover the post-petition transfers. Lastly, the UST argues there was an unnecessary duplication of services by two senior attorneys, meriting a deduction in the Application.

Contrarily, MLF argues it still fulfills the disinterested requirement because:

> The checks were written on an account of Four Seasons; however, all funds paid out of Four Seasons on account of [Debtor's] personal expenses are treated as loan repayments to [Debtor]. Therefore, not only have no fees been paid from the checks received from Four Seasons, but Four Seasons is also not the payor of any fees to be approved since said funds are being credited against the amount owed to Debtor by Four Seasons and are actually being paid by [Debtor] notwithstanding the check not having been run through [Debtor's] personal account. [MLF] never agreed to accept payment and did not receive payment from Four Seasons.

Dckt. No. 109, at 2.

Second, MLF argues the Court's previous order did not make a finding of bad faith. Third, MLF contends the Court's order granting relief from the automatic stay is appealable notwithstanding the abstention. Fourth, MLF disagrees there was a duplication of efforts, stating the lawyers made every attempt to avoid duplication of work by conferring on matters and assigning separate tasks. This work division made it necessary for both attorneys to attend these pivotal hearings so their combined knowledge could efficiently be used to best represent their client. Id. at 5–6. Lastly, regarding the reasonableness of the fees, MLF says "[t]he time spent on this case has been significant, but certainly not out of line with a typical contested Chapter 11 cases." Id. at 6.

Disclosure.

[1–3] The Bankruptcy Code and Rules require the utmost disclosure and candor from professionals seeking employment and compensation from the bankruptcy estate. In re Kisseberth, 273 F.3d 714, 720 (6th Cir. 2001). An application to employ must be filed pursuant to 11 U.S.C. § 327[3] and Federal Rule of Bankruptcy Procedure 2014. Bankruptcy Rule 2014(a) provides:

3. 11 U.S.C. § 327(a) states in pertinent part: Except as otherwise provided in this section, the trustee, with the court's approval, may employ one or more attorneys, accountants, appraisers, auctioneers, or other professional persons, 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.

> An order approving the employment of attorneys ... pursuant to § 327, § 1103, or § 1114 of the Code shall be made only on application of the trustee or committee .... The application shall state 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 the applicant's knowledge, all of the person's connections with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee. 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, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee.

Fed. R. Bankr. P. 2014(a). The level of disclosure required by Rule 2014(a) is mandatory, regardless of whether the disclosure would expose a conflict of interest. In re Matco Elecs. Grp., Inc., 383 B.R. 848, 852 (Bankr. N.D.N.Y. 2008). This disclosure duty is a continuing duty, and continues even after counsel's appointment. In re Keller Fin. Servs. of Fla., Inc., 248 B.R. 859, 898 (Bankr. M.D. Fla. 2000); In Re HLJ Enters., Inc., 2011 WL 3438472, at *3 (Bankr. S.D. Ga. June 28, 2011) (citing In re Jennings, 199 Fed.Appx. 845, 848 (11th Cir. Oct. 4, 2006).

Section 329(a) of the Bankruptcy Code and Bankruptcy Rule 2016 require disclosures specific to compensation. Section 329(a) provides:

> (a) Any attorney representing a debtor in a case under this title, or in connection with such a case, whether or not such attorney applies for compensation under this title, shall file with the court a statement of the compensation paid or agreed to be paid, if such payment or agreement was made after one year before the date of the filing of the petition, for services rendered or to be rendered in contemplation of or in connection with the case by such attorney, and the source of such compensation.

11 U.S.C. § 329(a). Bankruptcy Rule 2016 imposes a duty to fully and completely disclose all fee agreements and payments. Bankruptcy Rule 2016(a) and (b) provides:

> (a) An entity seeking interim or final compensation for services, or reimbursement of necessary expenses, from the estate shall file an application setting forth a detailed statement of (1) the services rendered, time expended and expenses incurred, and (2) the amounts requested. An application for compensation shall include a statement as to what payments have theretofore been made or promised to the applicant for services rendered or to be rendered in any capacity whatsoever in connection with the case, the source of the compensation so paid or promised, ... The requirements of this subdivision shall apply to an application for compensation for services rendered by an attorney or accountant even though the application is filed by a creditor or other entity. Unless the case is a chapter 9 municipality case, the applicant shall transmit to the United States trustee a copy of the application.
>
> (b) Every attorney for a debtor, whether or not the attorney applies for compensation, shall file and transmit to the United States trustee within 14 days after the order for relief, or at another time as the court may direct, the statement required by § 329 of the Code

. . . . A supplemental statement shall be filed and transmitted to the United States trustee within 14 days after any payment or agreement not previously disclosed.

Fed. R. Bankr. P. 2016(a)-(b).

[4, 5] The purpose of Rule 2016(a) is to provide the Court and the UST and other parties in interest with the necessary information to determine whether the Debtor's counsel meets the Bankruptcy Code's threshold requirements to serve as Debtor's counsel. Rule 2016(b) imposes a continuing duty upon Debtor's counsel to supplement its original statement "within 14 days after any payment or agreement not previously disclosed." Id. If a debtor's attorney subsequently receives funds from a non-party, the attorney is required to promptly supplement its disclosure. In re Kisseberth, 273 F.3d 714 (6th Cir. 2001). Sanctions may be imposed even when the failure to disclose was through inadvertence or negligent, and regardless of whether the estate was actually harmed. In re McTyeire, 357 B.R. 898 (Bankr. M.D. Ga. 2006)(even where the failure to disclose is nominal, disgorgement of all fees is appropriate); In re Gay, 390 B.R. 562 (Bankr. D. Md. 2008)(disgorgement appropriate for Rule 2016(b) violation even when there is no identifiable injury to creditors).

[6, 7] In this case, notwithstanding MLF's certifications that all payments were to be made by Debtor, MLF received two post-petition payments from Four Seasons totaling $6,500.00 and failed to timely amend its application and disclosure. MLF's argument that these were actually Debtor's funds because they were loan repayments does not alter the fact that MLF failed to disclose the payments were from Four Seasons' account, rather than Debtor's. The details of the transaction are missing. The source of these funds was initially discovered upon Pannill's deposition of Four Seasons' bookkeeper. Counsel's failure to properly disclose the required information may result in its disqualification, as well as the disgorgement of fees and imposition of sanctions. In re Prince, 40 F.3d 356 (11th Cir. 1994); see generally, Collier on Bankruptcy § 2014.03 (16th ed. 2015); In re Adam Furniture, Indus., Inc., 158 B.R. 291, 299 (Bankr. S.D. Ga. 1993). For MLF's failure to fully disclose the source of these payments as well as the source of payment, the Court finds disgorgement of the $6,500.00 is appropriate.

Conflict of Interest.

Pannill and the UST argue MLF must be denied compensation because it has a conflict of interest due to the undisclosed and unauthorized post-petition receipt of checks from Four Seasons. Pannill argues Four Seasons is the alter ego of Debtor negating MLF's defense that the payments were loan repayments from Four Seasons and therefore the payments are property of the bankruptcy estate. MLF argues Debtor is the true source of the payments, not Four Seasons, as the payments are treated as loan repayments. The UST argues MLF's characterization of the payment as a loan repayment makes the unauthorized post-petition transfers avoidable under 11 U.S.C. § 549. Pannill and the UST argue MLF's conflict arose on the date it received its first undisclosed payment from Four Seasons, February 21, 2017 and continued through the remaining time covered by the Application, May 12, 2017, covering $22,800.00 of professional fees that should be disallowed.

[8] Pursuant to 11 U.S.C. § 328(c) a court may deny compensation to professionals who are not disinterested or who have an adverse interest to the bankruptcy estate. Section 328(c) provides:

> (c) Except as provided in section 327(c), 327(e), or 1107(b) of this title, the court may deny allowance of compensation for services and reimbursement of expenses of a professional person employed under section 327 or 1103 of this title if, at any time during such professional person's employment under section 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.

11 U.S.C. § 328(c). The Bankruptcy Code defines a "disinterested person" as "a person that is not a creditor, an equity security holder, or an insider [of the Debtor] . . . and does not have an interest materially adverse to the interest of the estate or of any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor, or for any other reason." 11 U.S.C § 101(14). The phrase "interest materially adverse to the estate" has been held to mean:

> holding or representing an interest adverse to the estate as possessing, or serving as an attorney for a person possessing, either 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 . . . a predisposition under the circumstances that render such a bias against the estate.'

In re Prince, 40 F.3d 356, 361 (11th Cir. 1994)(quoting Roger J. Au & Son, Inc. v. Aetna Ins. Co., 64 B.R. 600, 604 (N.D. Ohio 1986)(citation omitted). A debtor's counsel's receipt of post-petition payments from a non-debtor wholly owned affiliate of the debtor has been held to create a disqualifying conflict which negates the required disinterestedness necessary to serve as the debtor's counsel. See In re W.T. Mayfield Sons Trucking Co., Inc., 225 B.R. 818 (Bankr. N.D. Ga. 1998)(holding that undisclosed payments by a debtor's subsidiary to bankruptcy counsel constituted unauthorized transfers of property of the estate and even if not property of the bankruptcy estate the court still could disgorge excessive and unreasonable fees). The language of § 328(c) is permissive "[a]nd, in the absence of actual injury or prejudice to the debtor's estate, this sanction [(denial of fees)] should not be rigidly applied. When injury to the debtor's estate occurs however, denial of fees is proper." In re Prince, 40 F.3d at 360 (internal citations omitted).

[9] There has not been a hearing nor enough evidence submitted for the Court to determine whether Four Seasons is the alter-ego of Debtor, and it is not necessary to resolve this matter. Ms. Kitchens testified in her deposition that Debtor's personal expenses paid by Four Seasons are treated as loan repayments to Debtor. As the UST argues, it is not necessary to find Four Seasons is the alter ego because by MLF's admission the transferred money would belong to the bankruptcy estate. MLF states:

> The checks were written on an account of Four Seasons; however, all funds paid out of Four Seasons on account of [Debtor's] personal expenses are treated as loan repayments to [Debtor]. Therefore, not only have no fees been paid from the checks received from Four Seasons, but Four Seasons is also not the payor of any fees to be approved since said funds are being credited against the amount owed to Debtor by Four Seasons and are actually being paid by [Debtor] notwithstanding the check not having been run through [Debtor's] personal account. [MLF] nev-

er agreed to accept payment and did not receive payment from Four Seasons.

Dckt. No. 109, at 2. Furthermore, even if the money belonged to Four Seasons, the Court would still be able to review the fees. See In re W.T. Mayfield Sons Trucking Co., Inc., 225 B.R. at 826; In re Miller Auto. Grp., Inc., 521 B.R. 323, 333 (Bankr. W.D. Mo. 2014)("The general rule is that, notwithstanding an ultimate third party owner of the funds, a retainer is held in trust for the debtor's estate to the extent it is utilized to compensate the estate's attorney" and is subject to bankruptcy court review).

The potential dispute of whether these undisclosed post-petition payments are unauthorized avoidable transfers creates an adverse interest because the bankruptcy estate has a potential cause of action against MLF. In such circumstances, MLF would not be able to independently evaluate the merits of pursuing the cause of action against itself or Four Seasons. See In re Prince, 40 F.3d at 360 (the prejudice is whether the law firm could make unbiased decisions in the best interest of its client).

Notwithstanding the foregoing, in this case, the prejudice is avoided because a chapter 11 trustee has been appointed and can objectively evaluate the merits of any avoidable transfers. See In re Music, 2016 WL 2583734, at *4 (Bankr. S.D. Ga. May 2, 2016) (conditioning debtor's counsel's continued employment upon the debtor obtaining independent counsel to investigate potential preference actions against entities who wrote checks to debtor's counsel on the debtor's behalf). In this case, like in In re Music, the Court will allow Debtor to maintain the counsel of his choosing since a chapter 11 trustee already has been appointed. Furthermore, the Court finds disgorgement is not merited on these grounds.

Bad Faith.

[10] Pannill argues attorney fees should not be allowed because Debtor filed his bankruptcy in bad faith as a means to avoid the enforcement of a domestic court order that found Debtor in willful contempt and ordered his arrest. This Court did find abstention was appropriate under the Eleventh Circuit's Carver v. Carver, 954 F.2d 1573 (11th Cir. 1992) precedent and granted relief from the stay for Pannill to pursue enforcement of the state court order. However, the Court did not find the bankruptcy was filed in bad faith as to all creditors or conduct a bad faith dismissal analysis. See In re Phoenix Piccadilly, Ltd., 849 F.2d 1393, 1394–95 (11th Cir. 1988)(listing factor to consider whether a bankruptcy petition was filed in bad faith). Furthermore, in this case the parties settled that dispute and Debtor dismissed his appeal and consented to the appointment of a chapter 11 trustee. Therefore, the Court does not find counsel's fees should be disallowed for Debtor's purported bad faith.

Appealability Pursuant To 28 U.S.C. § 1334(d).

[11] Pannill contends all fees associated with the appeal of this Court's previous abstention and motion for relief order should be disallowed because Pannill contends that order was non-appealable under 28 U.S.C. § 1334(d). Pannill's request for abstention or in the alternative relief from the automatic stay was addressed by one order. The Court, agrees with MLF, concluding the motion for relief from stay order is an appealable order. See Old W. Annuity & Life Ins. Co. v. Apollo Group, 605 F.3d 856, 862–63 (11th Cir. 2010)(citing BorgWarner Acceptance Corp. v. Hall, 685 F.2d 1306, 1309 (11th Cir. 1982)) ("A stay-relief order is a final order that is immediately appealable."). Further, the parties

agreed to the dismissal of the appeal and appointment of the chapter 11 trustee. The Court finds no fees should be disallowed based upon Pannill's argument that the Court's order abstaining and granting relief from the stay to Pannill was non-appealable.

Duplication and Reasonableness.

[12] Both Pannill and the UST argue MLF's Application includes unnecessary duplications of services and unreasonable fees. They specifically question MLF's entries regarding preparing for and attending the motion for relief/abstention hearing and the subsequent hearing on the appointment of a chapter 11 trustee. A bankruptcy "court shall not allow compensation for unnecessary duplication of services ...." 11 U.S.C. § 330(a)(4)(A)(i). In the Eleventh Circuit, attorney compensation under 11 U.S.C. § 330 is determined using the "lodestar method." See Norman v. Housing Authority of Montgomery, 836 F.2d 1292, 1299 (11th Cir. 1988). The "lodestar" is "the reasonable time expended by counsel in performing the reasonably required services rendered multiplied by a reasonable hourly rate." In re Golf Augusta Pro Shops, Inc., 2004 WL 768576, *2 (Bankr. S.D. Ga. Feb. 6, 2004).

Two MLF attorneys represent Debtor. McCallar has been practicing law for more than 40 years and specializes in complex bankruptcy matters, including in chapter 11 debtor work. His stated hourly rate in this case is $400.00. Caron has been praticing law for over eight years, focusing on complex bankruptcy matters, including chapter 11 debtor work. Her stated hourly rate in this case is $300.00.

To date, this has been a very contested chapter 11 case with a lengthy pre-bankruptcy history. With respect to the hearing on Pannill's motion for relief/abstention, McCallar charged the estate for 22.5 hours at $400/hour, over a four day period including the hearing date, resulting in fees of $9,000.00; and Caron charged 7.75 hours at $300/hour, for $2,325.00 over a two day period, including the hearing. The hearing was highly contested and lengthy, lasting almost 8 hours with both MLF attorneys attending all, or a substantial part, of the hearing.

With respect to the hearing on the appointment of the trustee, for work performed over a two day period including the hearing date, McCallar charged 12 hours at $400/hour, totaling $4,800.00; Caron logged 6.75 hours at $300/hour for $2,025.00. The hearing was concluded after approximately 5 hours, and both MLF attorneys attended all, or a substantial part, of the hearing.

[13] In considering the record in this bankruptcy case, the Court does not find an unnecessary duplication of work. The Court finds MLF avoided duplication when appropriate by conferring on matters and assigning separate tasks. This case has had expedited and lengthy contested hearings and the work done by both attorneys was not unnecessary or duplicative. Based upon the nature of the work and the labor division, the Court finds it was appropriate for both attorneys to attend these pivotal hearings so their combined knowledge and skill could be utilized to best represent Debtor.

Lastly, regarding the reasonableness of the fees, MLF agrees "[t]he time spent on this case has been significant, but certainly not out of line with a typical contested Chapter 11 cases." Dckt. No. 109 at 6. To determine a reasonable rate, courts look to the rates charged in "the relevant legal community for similar services by lawyers of reasonably comparable skills, experience and reputation." In re Augusta Pro Shops, Inc., 2004 WL 768576, at *1 (quoting Blum v. Stenson, 465 U.S. 886, 889 n.

11, 104 S.Ct. 1541, 79 L.Ed.2d 891 (1984). McCallar and Caron are highly skilled and experienced attorneys and the respective hourly rates of $400.00 and $300.00 are reasonable and common for comparable expertise and experience in handling such matters. For these reasons, the Court finds the time spent and the rates charged reasonable and not unnecessarily duplicated.

For the foregoing reasons, the objections of the UST and Pannill are SUSTAINED in part and DENIED in part. MLF's application for compensation is ORDERED reduced by $6,500.00 for total fee award of $37,007.50 in fees and $995.39 in expenses.

not file his claim with such official, the IRS's Chief, Local Insolvency Unit, for the Eastern District of California. 26 C.F.R. §§ 301.7430–1(e)(2), 301.7433–2(e). Sending his claim to two different IRS employees (not the Chief of the Local Insolvency Unit) and an attorney at the U.S. Department of Justice does not suffice under any reading of the applicable regulation. *See Hoogerheide v. I.R.S.,* 637 F.3d 634, 639 (6th Cir. 2011) (finding improperly addressed letters insufficient and rejecting as doubtful any doctrine of substantial compliance). These deficiencies preclude Barcelos from having exhausted his administrative remedies, and the court need not decide whether the content of Barcelos's administrative claim satisfied 26 U.S.C. § 7430(b)(1) and its implementing regulations.

Because Barcelos did not exhaust his administrative remedies as to his attorney's fees and other litigation costs, his action falls outside the scope of the United States' waiver of sovereign immunity. Accordingly, this court lacks jurisdiction over this proceeding.

CONCLUSION

The court lacks jurisdiction over Barcelos's claim for attorney's fees and other litigation costs because Barcelos has failed to exhaust administrative remedies. The adversary proceeding will be dismissed. Each motion for summary judgment is denied. The court will issue a separate order.

IN RE: Erik SUNDQUIST and Renée Sundquist, Debtors.

Erik Sundquistand Renée Sundquist, Plaintiffs,

v.

Bank of America, N.A.; Recontrust Company, N.A.; BAC Home Loans Servicing, LP, Defendants.

Case 14–02278
Case No. 10–35624
Adv. Pro. No. 14–02278
Docket Control No. ELG–1

United States Bankruptcy Court, E.D. California.

Signed November 15, 2017

Background: After bankruptcy court cancelled contingency-fee agreement executed by Chapter 13 debtors and their then-counsel and ordered debtors to pay counsel $70,000 as "reasonable" lodestar compensation for representing them in adversary proceeding in which they recovered more than $6 million in actual and punitive damages for deed of trust creditor's willful automatic stay violations, plus an additional $40 million in punitive damages, the after-tax residue of which was channeled to designated public purpose entities, 566 B.R. 563, counsel asserted a lien for attorney fees. Debtors filed motion to expunge lien.

Holdings: The Bankruptcy Court, Christopher M. Klein, J., held that:

(1) the bankruptcy court had jurisdiction over former counsel's fees, as well as over attendant liens for fees, for representing debtors in their action to enforce the automatic stay, notwithstanding dismissal of the case prior to the filing of the stay-enforcement action or closing of the case;

(2) permissive abstention was not warranted;

(3) given the poor quality of former counsel's work, the agreed compensation in the parties' contingency-fee agreement exceeded the "reasonable value" of her services, warranting cancellation of the agreement and award to counsel of $70,000 lodestar compensation;

(4) former counsel's failure to comply with the Bankruptcy Code's compensation disclosure requirements gave the court discretion to deny all fees, though it would exercise its discretion to refrain from doing so;

(5) former counsel waived and renounced her right to claim additional compensation on quantum meruit or any other theory; and

(6) California state-law quantum-meruit principles were not available to rescue former counsel from cancellation of her contingency-fee agreement and the consequences of not disclosing her secret intent to enforce the contingency fee for a sum greater than a lodestar award.

Motion granted.

1. Bankruptcy ⚷2057

Bankruptcy court had jurisdiction over fees of Chapter 13 debtors' former counsel, as well as over attendant liens for fees, for counsel's representation of debtors in their action against deed of trust creditor to enforce the automatic stay, notwithstanding dismissal of case prior to filing of stay-enforcement action or closing of case; federal subject-matter jurisdiction attached with filing of case, court's powers were ample enough for the exercise of federal jurisdiction over fees of debtors' California lawyer, and attendant liens for fees, in a bankruptcy matter, even though such matters were ordinarily resolved in state court, and existence of retained or residual jurisdiction meant that court's power over ancillary matters, such as attorney fees, did not terminate when case was dismissed or closed. 11 U.S.C.A. §§ 105(a), 329, 349, 350(b), 362; 28 U.S.C.A. §§ 1334(a), 1334(b).

2. Bankruptcy ⚷2063

Federal subject-matter jurisdiction attached with filing of Chapter 13 petition. 28 U.S.C.A. § 1334(a).

3. Bankruptcy ⚷2052

Claims of entitlement to an attorneys fee lien for representation in actions prosecuted under federal bankruptcy jurisdiction are within federal bankruptcy jurisdiction. 28 U.S.C.A. § 1334(b).

4. Bankruptcy ⚷2041.1

Bankruptcy jurisdiction is very broad, including nearly every matter directly or indirectly related to the bankruptcy, and derives directly from the Bankruptcy Clause of the United States Constitution, which grants Congress the power to establish uniform laws on the subject of bankruptcies throughout the United States. U.S. Const. art. 1, § 8; 28 U.S.C.A. § 1334(b).

5. Bankruptcy ⚷2056

Bankruptcy jurisdiction includes supplemental jurisdiction over all other claims that are so related to claims within the court's original jurisdiction that they form part of the same case or controversy under Article III of the United States Constitution. U.S. Const. art. 3; 28 U.S.C.A. §§ 1334(b), 1367.

6. Bankruptcy ⚷3570, 3715(9.1)

Discharge of a debtor does not automatically deprive federal courts of jurisdiction over a claim "related to bankruptcy"; this includes post-confirmation bankruptcy jurisdiction over state-law claims such as

breach of contract, breach of covenant of good faith and fair dealing, and fraud where such claims have a "close nexus" to the bankruptcy case. 28 U.S.C.A. § 1334(b).

7. Bankruptcy ⚿3570, 3715(9.1)

Bankruptcy courts have post-discharge jurisdiction to enjoin collection actions in another country. 28 U.S.C.A. § 1334(b).

8. Bankruptcy ⚿2126

Bankruptcy courts retain broad equitable powers to carry out the provisions of the Bankruptcy Code. 11 U.S.C.A. § 105(a).

9. Bankruptcy ⚿2057

After a bankruptcy case is dismissed, there remains a residuum of federal bankruptcy jurisdiction; such residual jurisdiction includes matters "arising under" the Bankruptcy Code and ancillary matters, such as dealing with attorney fees. 11 U.S.C.A. § 349; 28 U.S.C.A. § 1334(b).

10. Bankruptcy ⚿2057

Enforcement of the automatic stay is a civil proceeding "arising under title 11" over which the bankruptcy court retains jurisdiction after dismissal of the case. 11 U.S.C.A. § 362; 28 U.S.C.A. § 1334(b).

11. Bankruptcy ⚿3192

Attorney fees incurred by a debtor in vindicating violations of the automatic stay remain subject to the section of the Bankruptcy Code authorizing the court to cancel fee agreements or order the return of excessive payments if the fees incurred exceed the "reasonable" value of services rendered. 11 U.S.C.A. § 329(b).

12. Bankruptcy ⚿3444.30(2)

In a Chapter 7 case, because the closing of the case occurs concurrent with termination of the services of the trustee, if unscheduled assets later emerge as property of the estate, it is administratively necessary to reopen the case in order to have a trustee appointed who may deal with the assets. 11 U.S.C.A. §§ 350(a), 350(b).

13. Bankruptcy ⚿3444.50(1)

When reopening a bankruptcy case, court must determine whether a trustee is necessary to protect the interests of creditors and the debtor or to ensure efficient administration of the case. 11 U.S.C.A. § 350(b); Fed. R. Bankr. P. 5010.

14. Bankruptcy ⚿3444.10

Although closing and reopening of bankruptcy cases may have practical and administrative significance, reopening is not an act of jurisdictional significance. 11 U.S.C.A. § 350(b).

15. Bankruptcy ⚿3444.30(1)

Much bankruptcy-related activity may occur without reopening a case, including automatic-stay enforcement, dischargeability actions, awards of compensation, imposition of sanctions, determinations of equitable subordination, contempt, dealing with unclaimed funds, motions for post-judgment relief, and execution of judgments. 11 U.S.C.A. § 350(b).

16. Bankruptcy ⚿2062

Federal jurisdiction over civil proceedings "arising under" title 11 is original but not exclusive jurisdiction, that is, concurrent state-federal jurisdiction. 28 U.S.C.A. § 1334(b).

17. Bankruptcy ⚿2045, 2048.5

Debtors' stay-enforcement action was created by the Bankruptcy Code and, hence, "arose under" title 11, for jurisdictional purposes. 11 U.S.C.A. § 362; 28 U.S.C.A. § 1334(b).

18. Bankruptcy ⚷2045

Bankruptcy court's statutory power to cancel attorneys fee contracts and to limit fees to "reasonable" compensation is created by the Bankruptcy Code and, hence, "arises under" title 11, for jurisdictional purposes. 11 U.S.C.A. § 329(b); 28 U.S.C.A. § 1334(b).

19. Bankruptcy ⚷2052

Attorneys lien for fees fixed through the exercise of a bankruptcy court's statutory authority to cancel attorneys fee contracts and to limit fees to "reasonable" compensation does not "arise under" title 11 but, rather, "arises in" the title 11 case, for jurisdictional purposes. 11 U.S.C.A. § 329(b); 28 U.S.C.A. § 1334(b).

20. Bankruptcy ⚷2043(1)

For jurisdictional purposes, "arising in" proceedings are not based on a right expressly created by the Bankruptcy Code, that is, not "arising under," but would not exist if a title 11 case had not been filed. 28 U.S.C.A. § 1334(b).

See publication Words and Phrases for other judicial constructions and definitions.

21. Bankruptcy ⚷2056

Bankruptcy counsel's claim for a lien for fees for representing Chapter 13 debtors in their stay-enforcement action qualified as "related to" the title 11 case on the supplemental jurisdiction theory that it was so related to the stay-violation and "reasonable compensation" claims within the bankruptcy court's original jurisdictional that they formed part of the same case or controversy under Article III of the United States Constitution. U.S. Const. art. 3; 11 U.S.C.A. §§ 329(b), 362; 28 U.S.C.A. § 1334(b).

22. Federal Courts ⚷2650

Former bankruptcy counsel's assertion that her lien-based claim to fees had to be determined by a California state court would be construed by the bankruptcy court as a request for abstention. 28 U.S.C.A. § 1334(c).

23. Federal Courts ⚷2650

Mandatory abstention was not required with respect to former bankruptcy counsel's request that her lien-based claim to fees for her representation of Chapter 13 debtors in their stay-enforcement action be determined by a California state court where there was no action commenced that could be timely adjudicated in a state forum of appropriate jurisdiction. 11 U.S.C.A. § 362; 28 U.S.C.A. § 1334(c)(2).

24. Federal Courts ⚷2574

Whether to abstain in the interest of justice, or the interest of comity with state courts, or out of respect for state law, is committed to the discretion of the court. 28 U.S.C.A. § 1334(c)(1).

25. Federal Courts ⚷2650

Permissive abstention was not warranted with respect to former bankruptcy counsel's request that her lien-based claim to fees for her representation of Chapter 13 debtors in their stay-enforcement action be determined by a California state court; attorney's assertion of a lien for attorney fees amounted to an end-run around the bankruptcy court's order canceling the parties' contingency-fee agreement and directing debtors to pay attorney $70,000 as "reasonable" lodestar compensation for representing them in the adversary proceeding, interests of justice favored keeping trial-related matters in the one court, subject to one appellate system, comity was not offended, as state appellate court had disclaimed jurisdiction over underlying cause of action, and respect for state law was not a factor because court's order was a federal question not based on state law and it was conceded that the contingency-fee contract had recently been voided as

not having complied with state law. 11 U.S.C.A. §§ 329(b), 362; 28 U.S.C.A. § 1334(c)(1).

26. Bankruptcy ⚷3179

Debtor's payments to, and agreements with, attorneys "made after one year before the filing of the petition," and extending after the filing of the petition indefinitely, must be disclosed in a filed statement. 11 U.S.C.A. § 329(a).

27. Bankruptcy ⚷2557

Unscheduled property, typically an undisclosed cause of action or undisclosed interest in real estate, is not deemed abandoned and administered at the closing of the case and retains its status as property of the estate indefinitely. 11 U.S.C.A. § 554(d).

28. Bankruptcy ⚷2404

Automatic stay of acts against property of the estate does not terminate when a case is closed, but continues until such property is no longer property of the estate. 11 U.S.C.A. § 362(c)(1).

29. Bankruptcy ⚷2364

Discharge injunction is permanent and may lead to enforcement proceedings years later. 11 U.S.C.A. § 524(a).

30. Bankruptcy ⚷3179

Obligation of an attorney for the debtor to disclose fees and fee agreements is co-extensive with a debtor's involvement in a bankruptcy case and remains in effect for so long as jurisdiction connected with that case survives. 11 U.S.C.A. § 329; 28 U.S.C.A. § 1334.

31. Bankruptcy ⚷3179

Statutory requirement that an attorney for the debtor disclose fees and fee agreements "in connection with" the case is a broad concept that extends to services in any way related to the case and necessarily includes everything that is premised on the bankruptcy court's original jurisdiction, including supplemental jurisdiction over all other claims that are so related to claims in the action within the court's original jurisdiction that they form part of the same case or controversy under Article III of the United States Constitution. U.S. Const. art. 3; 11 U.S.C.A. § 329; 28 U.S.C.A. §§ 1334, 1367; Fed. R. Bankr. P. 2017(b).

See publication Words and Phrases for other judicial constructions and definitions.

32. Bankruptcy ⚷3179

For compensation-disclosure purposes, an attorney's representation of a debtor "in connection with" a case is not limited to actions in federal court, but extends to other actions in state courts in other states. 11 U.S.C.A. § 329; 28 U.S.C.A. § 1334(b); Fed. R. Bankr. P. 2017(b).

33. Bankruptcy ⚷3192

Bankruptcy court's statutory powers to cancel bankruptcy counsel's fee agreements and order return of payments to the extent that they exceed the "reasonable value" of services are committed to the discretion of the bankruptcy court. 11 U.S.C.A. § 329(b).

34. Bankruptcy ⚷3193

In determining the "reasonable value" of services provided by bankruptcy counsel, the touchstone is the Bankruptcy Code's list of considerations for determining reasonable compensation for officers and professional persons, which focuses on the nature, extent, and value of services, taking into account all relevant factors, including time spent, rates charged, and customary compensation in comparable cases. 11 U.S.C.A. §§ 329(b), 330(a)(3).

35. Bankruptcy ⚷3194

In the Ninth Circuit, a reasonable hourly rate multiplied by the number of hours actually and reasonably expended, the so-called "lodestar rate," is presumptively a reasonable fee in a bankruptcy case. 11 U.S.C.A. §§ 329(b), 330(a)(3).

See publication Words and Phrases for other judicial constructions and definitions.

36. Bankruptcy ⚷3193, 3200

Given the poor quality of former bankruptcy counsel's work in representing Chapter 13 debtors in their action against deed of trust creditor to enforce the automatic stay, the agreed compensation in the parties' contingency-fee agreement exceeded the "reasonable value" of her services, warranting cancellation of the agreement and award to counsel of $70,000 as "reasonable" lodestar compensation, notwithstanding that debtors, in the stay-enforcement proceeding, recovered more than $6 million in actual and punitive damages for deed of trust creditor's willful automatic stay violations, plus an additional $40 million in punitive damages, the after-tax residue of which was channeled to designated public purpose entities. 11 U.S.C.A. §§ 329(b), 330(a)(3), 362(k)(1).

37. Bankruptcy ⚷3193

Quality of services may be taken into account in determining the "reasonable value" of services provided by bankruptcy counsel. 11 U.S.C.A. §§ 329(b), 330(a)(3).

38. Bankruptcy ⚷3200

Contingency-fee agreements of bankruptcy counsel are as vulnerable to cancellation as "excessive" as are hourly-fee agreements. 11 U.S.C.A. § 329(b).

39. Bankruptcy ⚷3179

Nondisclosure and defective disclosure of compensation by bankruptcy counsel warrant denial of all fees in the discretion of the court. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016, 2017.

40. Bankruptcy ⚷3179

Counsel compensation statements required by the Bankruptcy Code and rules must include "full, candid, and complete" disclosure. 11 U.S.C.A. § 329(a); Fed. R. Bankr. P. 2016(b).

41. Bankruptcy ⚷3179

Where then-bankruptcy counsel for Chapter 13 debtors filed statement asserting that she did not intend to collect more than reasonable compensation and that she would only seek lesser of contingency-fee sum or lodestar fee, which she then fixed at $68,874.55, counsel's failure to comply with Bankruptcy Code's compensation disclosure requirements, in later claiming that she had always secretly intended to collect from debtors the full amount of her contingency to the extent that it exceeded the lodestar fee, gave the bankruptcy court discretion to deny all fees, though, given the bare adequacy of counsel's representation in the matter, the court declined to exercise its discretion to reduce the $70,000 it had awarded her to zero or some intermediate sum. 11 U.S.C.A. § 329(a); Fed. R. Bankr. P. 2016(b), 2017.

42. Bankruptcy ⚷3179

Even a negligent or inadvertent failure by bankruptcy counsel to disclose full relevant information may result in denial of all requested fees in the discretion of the court. 11 U.S.C.A. § 329(a); Fed. R. Bankr. P. 2016(b).

43. Bankruptcy ⚷3176

Former counsel for Chapter 13 debtors waived and renounced her right to claim additional compensation on quantum meruit or any other theory in her responses to the bankruptcy court's request that she justify her contingency-fee agreement with debtors where counsel filed statement

saying that it was never her intent to exceed "reasonable compensation" under the Bankruptcy Code and that she would file a time billing in which she would seek only the lesser of the contingency-fee agreement or the lodestar amount, which she fixed at $68,874.55, and counsel filed a declaration in which she sought costs and fees totaling that amount. 11 U.S.C.A. §§ 329(b), 362(k)(1).

44. Attorney and Client ⚷147
Bankruptcy ⚷3179, 3192

California state-law quantum-meruit principles were not available to rescue Chapter 13 debtors' former bankruptcy counsel from the bankruptcy court's cancellation of her contingency-fee contract as exceeding the "reasonable" value of her services and the consequences of not disclosing her secret intent to enforce the contingency fee for a sum greater than a lodestar award. 11 U.S.C.A. §§ 329(a), 329(b); Cal. Bus. & Prof. Code § 6147(b); Fed. R. Bankr. P. 2016(b).

45. Attorney and Client ⚷148(3)

Under California law, the voiding of a contingency-fee contract disentitles the attorney to any fee greater than a "reasonable" fee. Cal. Bus. & Prof. Code § 6147(b).

46. Bankruptcy ⚷3179

Under federal law, the equitable remedy of quantum meruit is not available following the denial of fees as a remedy for bankruptcy counsel's failure to comply with the Bankruptcy Code's compensation disclosure requirements; one who has not complied with the Code and rules lacks the requisite clean hands. 11 U.S.C.A. § 329(a); Fed. R. Bankr. P. 2016(b).

47. Bankruptcy ⚷3179

Quantum meruit is not available to counsel in state court following denial of fees by a bankruptcy court for counsel's failure to comply with the Bankruptcy Code's compensation disclosure requirements. 11 U.S.C.A. § 329(a); Fed. R. Bankr. P. 2016(b).

48. Judgment ⚷829(3)

Attorney who has been denied fees in bankruptcy court may not pursue an alternative remedy in state court.

49. Bankruptcy ⚷2056

Bankruptcy court has jurisdiction to interpret and enforce its orders.

50. Bankruptcy ⚷3202.1

Proper course for Chapter 13 debtors' former bankruptcy counsel to challenge the bankruptcy court's judgment cancelling the parties' contingency-fee agreement and determining "reasonable" compensation to be $70,000.00 was to appeal that order pursuant to regular federal appellate procedure, not to threaten various collateral attacks in state court. 11 U.S.C.A. § 329(b); 28 U.S.C.A. § 158.

Mark E. Ellis, Ellis Law Group, LLP, Sacramento, California, for Plaintiffs.

Orly Degani, Degani Law Offices, Los Angeles, California; Sandor T. "Ted" Boxer, Law Offices of Sandor T. Boxer, Los Angeles, California, for Dennise Henderson, Attorneys' Lien Claimant.

Before: Christopher M. Klein, Bankruptcy Judge

OPINION ON MOTION TO EXPUNGE ATTORNEYS' FEE LIEN

CHRISTOPHER M. KLEIN, Bankruptcy Judge:

This Motion to Expunge an attorneys' fee lien asserted by the debtors' former attorney involves an important tool in the

judicial toolbox for addressing the dilemma of counsel who incompetently represent debtors who have a meritorious case.

Former counsel asserts an attorneys' fee lien as a challenge to the bankruptcy court's power to cancel an attorneys' contract under Bankruptcy Code § 329(b), 11 U.S.C. § 329(b), and to limit fees for debtors' counsel to "reasonable" compensation.

The lien is being used as a device to create "hold-up" value by impeding settlement efforts by plaintiffs and defendant in order to extract a fee "far higher" than what this court authorized as "reasonable" compensation under § 329(b).

The Motion to Expunge is GRANTED; the § 329(b) order requiring that the plaintiffs pay the former attorney $70,000.00 as § 329(b) "reasonable" compensation remains in effect.

Facts

The underlying facts are set forth in this court's reported decision, Sundquist v. Bank of America, N.A., 566 B.R. 563, 571–85 (Bankr. E.D. Cal. 2017), and will be merely summarized here.

Attorney Dennise Henderson represented Erik and Renée Sundquist in their chapter 13 case filed June 14, 2010. A series of automatic stay violations by Bank of America, including foreclosure, prosecution of an unlawful detainer action, and other uncivilized conduct ensued that prompted the Sundquists to give up their effort to use a chapter 13 plan to cure a bank-induced default while they attempted to negotiate a mortgage modification. They voluntarily dismissed the chapter 13 case on September 20, 2010, and Ms. Henderson ceased to represent them.

Presaging what was to come when she re-emerged in 2014 for the eventual stay violation litigation, during the period between filing the case on June 14 and dismissing on September 20, 2010, Ms. Henderson made no complaint to the court and did not figure out an effective strategy to bring Bank of America to book for its stay violations.

After the chapter 13 case was dismissed, Bank of America kept exacerbating the consequences of its prior stay violations.

The Sundquists, represented by another not-very-competent counsel, sued under state law in 2011, which complaint was dismissed by the state trial court. On appeal, the California Third District Court of Appeal, while critical of the poor quality of the drafting of the complaint, reversed the dismissal in 2014, ruling that the complaint stated causes of action on six state-law counts including deceit and various fiduciary breaches.

As to the count alleging wrongful foreclosure, however, the California appellate court invoked conflict preemption to rule that Bankruptcy Code § 362(k)(1) preempts state-law wrongful foreclosure claims that are based solely on violation of the automatic stay and concluded that such claims are within exclusive federal jurisdiction. It ruled that if the Sundquists desired relief on account of the bankruptcy automatic stay violations, they would have to return to federal court.

The Sundquists re-employed Ms. Henderson to prosecute their § 362(k) (1) cause of action in federal court. Upon filing, the district court referred the civil action to this bankruptcy court as a core proceeding.[1] Accordingly, this court presided over the discovery phase, in which

1. This court does not question the litigation judgment to focus only on the § 362(k)(1) cause of action.

there were discovery disputes, and presided over the bench trial.

At trial, the evidentiary presentation orchestrated by Ms. Henderson consisted of little more than the testimony of the Sundquists, accompanied by a long and vague declaration that summarized the contents of Renée Sundquist's diary, which declaration was admitted by agreement of the parties. Ms. Henderson did not attempt to introduce the actual diary, extracts of which came into evidence as exhibits that had been marked by Bank of America and that were admitted under the circumstances described in footnote 58 of the opinion, without sponsorship by Ms. Henderson. Sundquist, 566 B.R. at 590 n.58.

Although various items of physical damages and economic damages were the subject of testimony, there was virtually no corroborative documentary evidence. This left the court in the uncomfortable position of having to note in its decision that "some components of actual damages will be less than what might have been proved with more precise evidence." Sundquist, 566 B.R. at 590. Time and time again, this court was forced to estimate damages in various categories on the low side and include a footnote to the effect that if the case were to need to be retried, the Sundquist evidence likely would be considerably more robust. E.g., Sundquist, 566 B.R. at 604 n.88.

Since § 362(k)(1) is unusual in that it specifies that attorney fees are a component of actual damages, with the consequence that fees could operate to increase punitive damages, and not merely be an additional charge, it was important to ascertain Ms. Henderson's legitimate fees.

Ms. Henderson did not comply with the requirement of Federal Rule of Bankruptcy Procedure 2016(b) that she file, within 15 days after executing the fee agreement with the Sundquists for representing them in the adversary proceeding, the statement required by § 329 disclosing the compensation agreed to be paid. Accordingly, this court issued an order reminding Ms. Henderson of the applicability of § 329 and of Rule 2016(b) and directing her to file the delinquent statement.

The ensuing supplemental statement stated that fees were on an unspecified contingency. Case 10–35624, Dkt. 69 (9/12/16).

This court thereupon, consistent with Federal Rule of Bankruptcy Procedure 2017(b), ordered that Ms. Henderson file a copy of the contingency fee agreement. The order explained that contingency fee agreements are subject to § 329(b) review for reasonable value of services and noted that it is not clear that a contingency fee is consistent with the attorneys' fee structure in § 362(k)(1). The order required that she justify the agreed contingency fees as representing the reasonable value of services within the meaning of § 329(b) and that she explain how the contingency fees comported with the attorneys' fee structure set forth in § 362(k)(1). Case 10–35624, Dkt. 70 (9/14/16).

Ms. Henderson filed a copy of a contingency fee agreement dated October 22, 2014. Case 10–35624, Dkt. 74 (9/23/16). In fact, the "Attorney–Client Fee Agreement" was two different documents pasted together with non-consecutive paragraphs. The first two pages end in the middle of paragraph no. 3; the third page, in a distinctly different typeface, began with paragraph no. 11.[2] It is now conceded that this

2. It has now been revealed that the purported agreement that Ms. Henderson filed was a 2016 back-dated reconstruction and revision of a supposed 2014 agreement that has never

was a 2016 document back-dated to 2014. Although Ms. Henderson now explains that she filed an inaccurate copy of her fee agreement and "apologizes," [3] she has not filed a corrected copy.

Ms. Henderson also filed a Supplemental Briefing Regarding Attorneys' Fees in which she urged that § 329(b) reasonable compensation be determined consistent with 11 U.S.C. § 330(a)(3) which looks to the nature, extent, and value of services, taking into account all relevant factors, including, time spent, rates charged, and customary compensation of comparably skilled attorneys in other cases. She added, "I will file a time billing with the actual time expended and will only seek the lesser of the contingency agreement or the reasonable hourly rate times the number of hours expended consistent with the Lodestar method." Other than a naked assertion that customary compensation can be a contingency fee, she offered no justification for the contingency fee agreement. Case 10–35624, Dkt. 73 (9/23/16).

Ms. Henderson filed a declaration documenting 207.56 hours spent on the § 362(k)(1) adversary proceeding at a rate of $300.00 per hour (= $62,268), together with costs for depositions, transcripts, and trial binders of $6,606.55 for a total of $68,874.55. Case 10–35624, Dkt. 75 (9/26/16).[4]

Mindful that lodestar compensation measured by counsel's billing rate multiplied by the number of hours devoted to the case, plus reimbursement of actual costs, is "strongly" presumed to be reasonable, Burgess v. Klenske (In re Manoa Finance Co.), 853 F.2d 687, 691–92 (9th Cir. 1988), this court fixed the attorneys' fee component of § 362(k)(1) actual damages at $70,000.00. This was actually more than the lodestar amount that Ms. Henderson stated that she was requesting.

Ms. Henderson did not seek an enhancement above her lodestar compensation. Nor did she proffer specific evidence to rebut the presumption against a bonus. Pennsylvania v. Delaware Valley Citizens' Council for Clean Air, 478 U.S. 546, 564–69, 106 S.Ct. 3088, 92 L.Ed.2d 439 (1986).

Treating Ms. Henderson's doctored, back-dated contingency fee agreement at face value, this court concluded that the

been provided. Exhibits filed by Ms. Henderson responding to this motion to expunge attorneys' lien included an email exchange in September 2016, containing three different versions of an Attorney–Client Fee Agreement, which was being "re-created" and signed at that time. Adv. Pro. 14–02278, Dkt. 452 (9/12/17), Ex. 1, pp. 30–47.

All three of these versions differ from what was actually filed on September 23, 2016. Version 1, transmitted by Ms. Henderson to the Sundquists September 19, 2016, has only the signature of Ms. Henderson, back-dated to 11/2/14. Dkt. 452 (9/12/17), Ex. 1, pp. 33–35. Version 2, transmitted by Mr. Sundquist to Ms. Henderson, adds to version 1 the signature of Mr. Sundquist, back-dated to 11/2/14. Dkt. 452 (9/12/17), Ex. 1, pp. 37–39. Version 3 is not identical to versions 1 and 2 and has the signatures of both Sundquists and Ms. Henderson, back-dated to 10/22/14. Dkt. 452 (9/12/17), Ex. 1, pp. 43–45. Ms. Henderson's message accompanying the transmission of version 3 is: "Sorry round three with this fee agreement. I have to have language in there that lays out exactly how you are made whole. Just a few changes in language if you don't mind taking a look at one more and if you have questions give me a call otherwise send it back with signatures." Ex. 1, pp. 46–47.

3. Declaration of Dennise Henderson in Support of Her Opposition to the Sundquists' Motion to Expunge Her Attorneys'. Fees Lien, Adv. No. 14–02278, Dkt 451, ¶ 22 (9/12/17).

4. Although Ms. Henderson now says that she omitted time and expenses, she has not sought to document additional time and expenses. Declaration of Dennise Henderson in Support of Her Opposition to the Sundquist' Motion to Expunge Her Attorneys' Fees Lien, Adv. No. 14–02278, Dkt 451, ¶ 21 (9/12/17).

contingency fee exceeded the reasonable value of services within the meaning of § 329(b) and canceled the agreement. Two adequate, independent reasons support that conclusion.

First, as stated in this court's published decision on the merits, the structure of § 362(k)(1) that incorporates fees as an element of actual damages leads to a nonsensical loop.

The second adequate, independent reason was Ms. Henderson's lack of competence. This court, out of distaste for being overtly critical of individual counsel, initially preferred to address the problem of her lack of competence between the lines by way of comments scattered throughout the opinion.

Now, however, that Ms. Henderson has announced her intention to appropriate to herself more of the Sundquists' recovery than $70,000.00 and has promised to appeal, the appellate courts deserve candor from the trial court.

With considerable regret at the necessity of being blunt in print, Ms. Henderson's performance in this adversary proceeding was, in this court's experience of having tried bench trials in adversary proceedings and contested matters arising (as of November 14, 2017) in 151,817 bankruptcy cases since February 1988,[5] and considering the importance and magnitude of the issues involved in the litigation, among the ten weakest performances by counsel for debtors that it has had the misfortune to observe. It was as if she was in deep water, flailing with beginner strokes. Ms. Henderson did not prepare a trial brief.[6] Her trial presentation was disorganized. Her notebook of plaintiffs' exhibits was slovenly assembled. She demonstrated no proficient knowledge of the Federal Rules of Evidence or of the Federal Rules of Bankruptcy Procedure and the Federal Rules of Civil Procedure incorporated therein. The pretrial declarations of the Sundquists mandated by Local Bankruptcy Rule 9017–1 were crude and conclusory in content. She made no attempt to introduce the Renée Sundquist diary into evidence, which, ironically, was introduced by way of Bank of America's marked exhibits and wound up putting important flesh on the bones. Her questions were amateurish. She showed no ability to lay a foundation for introducing evidence; fortunately, most of her proffered exhibits were admitted without objection to foundation. Her demonstration of the facts was disjointed and difficult to decipher. She had no coherent theory of damages. Her closing argument did not connect any helpful dots. What saved the case for the plaintiffs was that, while poorly prepared to testify, they were so credible that the court could not in good conscience let the poor performance by counsel stand in the way of justice.

One reason this court's decision took some months to prepare was that Ms. Henderson had been of no help regarding the complex facts and legal theories. The process of wading through all the exhibits in the context of the testimony consumed time, required reflection, and entailed considerable research into intricacies of the law of actual and punitive damages.

This court's § 362(k) (1) judgment awarded the Sundquists $1,074,581.50 in actual damages and $5,000,000.00 in punitive damages, a total of $6,074,581.50. Additional punitive damages of $40,000,000.00 awarded to the Sundquists was allocated

5. Source: Clerk, U.S. Bankruptcy Court, E.D. Cal.

6. AS this court explains whenever it does not specifically mandate a trial brief: ''trial briefs are permitted but not required; good lawyers provide them, not-so-good lawyers do not.''

by mandatory injunction to deliver the after-tax residue of that sum to the National Consumer Law Center, National Consumer Bankruptcy Center, and five public law schools. The Sundquists were also enjoined, by mandatory injunction, to deliver $70,000.00 to Ms. Henderson as § 329(b) "reasonable" compensation.

Far from being the result of Ms. Henderson's performance, the judgment was entered despite her work. Heretofore, the court has expressed its frustration obliquely and intended to keep it that way, but her subsequent activity has forced the court to be explicit so that no appellate tribunal will be confused.

Once the Sundquists replaced her, Ms. Henderson filed a Notice of Lien "by virtue of a written fee agreement with said parties dated October 22, 2014," on any judgment or settlement paid to secure the payment for legal services rendered and costs and expenses "in accordance with the terms of the aforementioned fee agreement." Adv. No. 14–02278, Dkt. 315 (4/26/17).

The notice of lien, by its terms, asserts a contractual lien without referring to an equitable lien or quantum meruit, yet from the manner in which Ms. Henderson conflates apples with oranges by talking about equitable liens (and from her concession that her contract has been voided under state law for violation of California ethics rules) it seems that she must now be asserting only an equitable lien.

If the issue is quantum meruit, then, as a finding of fact, this court determines that the quantum Ms. Henderson's services were worth did not exceed the $70,000.00 previously authorized, which is more than the number of hours she devoted to the case, multiplied by her normal billing rate, plus claimed expenses.

The present procedural posture of the case is that there are pending cross-motions to reopen the evidence—Bank of America wishing to expunge the Renée Sundquist diary and the Sundquists to prove more damages. There is also a motion to vacate the judgment and dismiss the adversary proceeding on account of a settlement that would pay the Sundquists "more than" the $6,074,581.50 provided in the judgment and muzzle them.

Ms. Henderson has been acting through counsel to interfere with that proposed settlement by threatening to sue Bank of America by way of collateral attack unless Ms. Henderson receives fees that "far exceed the $70,000 allocated in Judge Klein's March 23, 2017 decision." [7] She also has

7. By letter dated October 9, 2017, and provided to the court by agreement in open court, Ms. Henderson's attorney Orly Degani wrote to counsel for Bank of America:

> . . . No matter what Judge Klein decides to do regarding Ms. Henderson's lien on the Sundquists' judgment, Bank of America will be acting at its own risk if it makes any payment to the Sundquists in disregard of Ms. Henderson's claim for her fees. While we have been kept in the dark thus far as to the amount of the proposed settlement between Bank of America and the Sundquists, it is our position that Ms. Henderson is entitled to a portion of the settlement sum in an amount yet to be determined, either by a court exercising proper jurisdiction over the matter (not Judge Klein) or by settlement with the Sundquists. Either way,-the fees due to Ms. Henderson far exceed the $70,000 allocated in Judge Klein's March 23, 2017 decision. We will take whatever legal steps are necessary to protect her right to recover the fees we believe she is due, including appealing or petitioning for writ relief, as appropriate, from any potential adverse ruling by Judge Klein. Please be on notice that ignoring Ms. Henderson's fee claim in reliance on any ruling by Judge—Klein which we will take up with a higher court may subject Bank of America to liability . . . .

threatened to sue the Sundquists under the Uniform Voidable Transactions Act.[8]

Jurisdiction

Federal subject-matter jurisdiction is founded on 28 U.S.C. § 1334. This is a core proceeding that a bankruptcy judge may hear and determine. 28 U.S.C. §§ 157(b)(K) & (O).

The challenge to jurisdiction is addressed infra.

Pertinent Statutes and Rules

§ 329 Debtor's transactions with attorneys.

> (a) Any attorney representing a debtor in a case, or i connection with such a case, whether or not such attorney applies for compensation under this title, shall file with the court a statement of the compensation paid or agreed to be paid, if such payment or agreement was made after one year before the date of the filing of the petition, for services rendered or to be rendered in contemplation of or in connection with the case by such attorney, and the source of such compensation.
>
> (b) If such compensation exceeds the reasonable value of any such services, the court may cancel any such agreement, or order the return of any such payment, to the extent excessive, to—
>
> (1) the estate, if the property transferred—
>
> (A) would have been property of the estate;
>
> or
>
> (B) was to be paid by or on behalf of the debtor under a plan under chapter 11, 12, or 13 of this title; or
>
> (2) the entity that made such payment.

11 U.S.C. § 329.

Rule 2016(b). Disclosure of Compensation Paid or Promised to Attorney for Debtor. Every attorney for a debtor, whether or not the attorney applies for compensation, shall file and transmit to the United States trustee within 14 days after the order for relief, or at another time as the court may direct, the statement required by § 329 of the Code including whether the attorney has shared or agreed to share the compensation with any other entity. The statement shall include the particulars of any such sharing or agreement to share by the attorney, but the details of any agreement for the sharing of the com-

8. On October 13, 2017, in an email provided to the court by agreement in open court, Ms. Henderson's attorney Sandor "Ted" Boxer wrote to Sundquist counsel Mark Ellis:

> . . . it does not follow that the Sundquists will be free even if their motion to expunge is granted to at any time in the foreseeable future deal with the amounts sought by my client regardless of Judge Klein's ultimate ruling for at least two reasons.
>
> First, Orly has already made clear what I believe has been well known (if for no other reason than the nature of her practice as an appellate attorney) that whatever ruling Judge Klein makes is unlikely to be final for some time. My purpose by this email is to bring to your attention a second factor impinging upon the ability of the Sundquists to deal anytime soon with a significant portion of their recovery, the potential for a suit under the Uniform Voidable Transaction Act ("UFTA" [sic]) found in Civil Code section 3429 [sic—§ 3439] if the Sundquists were to attempt to deal inappropriately with the recovery.
>
> In general the UFTA provides remedies (set aside the transfer, punitive damages) for any attempt by the Sundquists to transfer their property with the intent to "hinder, delay or defraud" Ms. Henderson. In measuring intent, there are a variety of factors set forth in the statute. One of those factors is "Whether before the transfer was made . . . the debtor had been sued or threatened with suit." Clearly, the Sundquists must understand that Ms. Henderson has and will pursue her legal remedies to recover what she believes is due her . . . .

pensation with a member or regular associate of the attorney's law firm shall not be required. A supplemental statement shall be filed and transmitted to the United States trustee within 14 days after any payment or agreement not previously disclosed.

Fed. R. Bankr. P. 2016(b).

Rule 2017(b). Payment or Transfer to Attorney After Order for Relief. On motion by the debtor, the United States trustee, or on the court's own initiative, the court after notice and a hearing may determine whether any payment of money or any transfer of property, or any agreement therefor, by the debtor to an attorney after entry of an order for relief in a case under the Code is excessive, whether the payment, transfer, or agreement therefor is for services in any way related to the case.

Fed. R. Bankr. P. 2017(b).

Analysis

In order to circumvent this court's § 329(b) order canceling the contingent fee contract and limiting reasonable compensation to $70,000.00, the former counsel challenges this court's jurisdiction. As she concedes that the actual fee contract is, regardless of § 329(b), now unenforceable under state law, her theory is that state-law quantum meruit principles (which equate with "reasonable" in California law) take precedence over § 329(b) and permit a fee that "far exceeds" $70,000.00. Not so.

I

[1] Jurisdiction is the linchpin. Henderson insists there is no federal jurisdiction over her fees for representing the Sundquists in their action enforcing Bankruptcy Code § 362 and that only a California state court may adjudicate her fees.

Her premise that the bankruptcy court's power over the attorneys' fees pursuant to § 329 terminated when the case was closed is flawed by the existence of retained jurisdiction.

Her reasoning that the absence of a bankruptcy estate and of creditors to protect deprives this court of jurisdiction to apply § 329(b) to an award payable directly to the Sundquists is incomplete because § 329(b) also protects the Sundquists.

A

[2] Federal subject-matter jurisdiction attached with the filing of the chapter 13 case on June 14, 2010. 28 U.S.C. § 1334(a).

B

[3] Claims of entitlement to an attorneys' fee lien for representation in actions prosecuted under federal bankruptcy jurisdiction are also within federal bankruptcy jurisdiction.

Bankruptcy jurisdiction extends to cases under title 11, and to civil proceedings arising under title 11 or arising in or related to cases under title 11. 28 U.S.C. § 1334(b).

[4] This jurisdiction is "very broad, including nearly every matter directly or indirectly related to the bankruptcy" and "derives directly from the [Constitution's] Bankruptcy Clause, which grants Congress the power '[t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States.' U.S. Const. art. 1, § 8." Sasson v. Sokoloff (In re Sasson), 424 F.3d 864, 868–69 (9th Cir. 2005).

[5] Bankruptcy jurisdiction includes supplemental jurisdiction pursuant to 28 U.S.C. § 1367 over all other claims that are so related to claims within the court's original jurisdiction that they form part of the same case or controversy under Article III of the United States Constitution. Sasson, 424 F.3d at 869.

[6] Discharge of a debtor does not automatically deprive federal courts of jurisdiction over a claim "related to bankruptcy." Sasson, 424 F.3d at 869; Kieslich v. United States (In re Kieslich), 258 F.3d 968, 971 (9th Cir. 2001).

This includes post-confirmation bankruptcy jurisdiction over state law claims such as breach of contract, breach of covenant of good faith and fair dealing, and fraud where such claims have a "close nexus" to the bankruptcy case. Sasson, 424 F.3d at 869; Montana v. Goldin (In re Pegasus Gold Corp.), 394 F.3d 1189, 1194 (9th Cir. 2005).

[7] Bankruptcy courts even have post-discharge jurisdiction to enjoin collection actions in another country. Sasson, 424 F.3d at 869; Hong Kong & Shanghai Banking Corp. v. Simon (In re Simon), 153 F.3d 991, 996 (9th Cir. 1998).

[8] Bankruptcy courts retain broad equitable powers to carry out the provisions of the Bankruptcy Code. Johnson v. Home State Bank, 501 U.S. 78, 88, 111 S.Ct. 2150, 115 L.Ed.2d 66 (1991); Sasson, 424 F.3d at 869; Saxman v. Educ. Credit Mgmt. Corp. (In re Saxman), 325 F.3d 1168, 1174 (9th Cir. 2003).

These powers are ample for the exercise of federal jurisdiction over the fees of a California lawyer, and attendant liens for fees, in a bankruptcy matter notwithstanding that such matters are ordinarily resolved in state courts.

C

The dismissal of the Sundquist chapter 13 case before this stay enforcement action was filed does not affect the exercise of bankruptcy jurisdiction over the fees of debtors' counsel.

[9] After a bankruptcy case is dismissed under § 349, there remains a residuum of federal bankruptcy jurisdiction. Carraher v. Morgan Electronics, Inc. (In re Carraher), 971 F.2d 327, 328 (9th Cir. 1992) (discretion to retain "related to" case); Fid. & Dep. Co. of Md. v. Morris (In re Morris), 950 F.2d 1531, 1533–35 (11th Cir. 1992) (same).

Such residual jurisdiction includes matters "arising under" the Bankruptcy Code and ancillary matters, such as dealing with attorneys' fees. Elias v. U.S. Trustee (In re Elias), 188 F.3d 1160, 1162 (9th Cir. 1999); Tsafaroff v. Taylor (In re Taylor), 884 F.2d 478, 481 (9th Cir. 1989); U.S.A. Motel Corp. v. Danning (In re U.S.A. Motel Corp.), 521 F.2d 117, 118 (9th Cir. 1975).

[10] Likewise, enforcement of the automatic stay is a civil proceeding "arising under title 11" over which the bankruptcy court retains jurisdiction after dismissal of the case. Johnson v. Smith (In re Johnson), 575 F.3d 1079, 1082–84 (10 Cir. 2009); Price v. Rochford, 947 F.2d 829, 830–32 (7th Cir. 1991); Davis v. Courington (In re Davis), 177 B.R. 907, 911 (9th Cir. BAP 1995); cf. 40235 Washington St. Corp. v. Lusardi, 329 F.3d 1076, 1080 n.2 (9th Cir. 2003) (retained jurisdiction to annul § 362 stay).

[11] Similarly, the attorneys' fees incurred by a debtor in vindicating violations of the automatic stay remain subject to § 329(b). Cases such as Elias and Tsafaroff render the contention that this court lost jurisdiction over attorney fees upon dismissal of the chapter 13 case lacking in merit.

D

Nor did closing the Sundquist chapter 13 case terminate § 1334 jurisdiction. That much is evident from the Bankruptcy Code reopening provision: "A case may be reopened in the court in which such case was

closed to administer assets, to accord relief to the debtor, or for other cause." 11 U.S.C. § 350(b).

[12, 13] In a chapter 7 case, the closing of the case occurs concurrent with termination of the services of the trustee. 11 U.S.C. § 350(a). If unscheduled assets later emerge as property of the estate, it is administratively necessary to reopen the case in order to have a trustee appointed who may deal with the assets. Thus, when reopening a case under § 350(b), a court must determine whether a trustee is necessary to protect the interests of creditors and the debtor or to ensure efficient administration of the case. 11 U.S.C. § 350(b); Fed. R. Bankr. P. 5010.

[14] Although closing and reopening of bankruptcy cases may have practical and administrative significance, reopening is not an act of jurisdictional significance. Staffer v. Predovich (In re Staffer), 306 F.3d 967, 972–73 (9th Cir. 2002); Menk v. LaPaglia (In re Menk), 241 B.R. 896, 905–06 (9th Cir. BAP 1999).

[15] Much bankruptcy-related activity may occur without reopening a case: automatic stay enforcement; dischargeability actions; awards of compensation; imposition of sanctions; determinations of equitable subordination; contempt; dealing with unclaimed funds; motions for post-judgment relief; execution of judgments. Menk, 241 B.R. at 905–06.

It follows that the bankruptcy jurisdiction under § 1334 that attached upon filing in June 2010 survives today to enable the action against Bank of America for willful stay violations and to exercise authority over fees of debtors' counsel.

E

There are more layers to the jurisdictional onion.

[16] Federal jurisdiction over civil proceedings "arising under" title 11 is "original but not exclusive jurisdiction;" i.e. concurrent state-federal jurisdiction. 28 U.S.C. § 1334(b).

[17] The Sundquists' § 362 stay enforcement action is created by the Bankruptcy Code and, hence, "arises under" title 11.

[18] The § 329(b) power to cancel attorneys' fee contracts and to limit fees to "reasonable" compensation is likewise created by the Bankruptcy Code and, hence, "arises under" title 11.

[19] In contrast, an attorneys' lien for fees fixed through the exercise of § 329(b) authority does not "arise under" title 11. Rather, it is either "arising in" or "related to" the title 11 case. 28 U.S.C. § 1334(b).

[20] The lien for fees fixed pursuant to § 329(b) fits best in § 1334(b) as "arising in" the case. "Arising in" proceedings are not based on a right expressly created by the Bankruptcy Code, i.e. not "arising under," but would not exist if a title 11 case had not been filed. Eastport Assocs. v. City of Los Angeles (In re Eastport Assocs.), 935 F.2d 1071, 1076 (9th Cir. 1991); Wood v. Wood (In re Wood), 825 F.2d 90, 97 (5th Cir. 1987); Menk, 241 B.R. at 909; 1 COLLIER ON BANKRUPTCY ¶ 3.01[4][c][iv] (Alan Resnick & Henry Sommer eds. 16th ed. 2016) ("COLLIER").

Henderson's claim to a lien for fees that were subjected to § 329(b) would not exist if the Sundquist title 11 case had not been filed. It is inseparable from its bankruptcy context.

[21] Recognizing the overlap between "arising in" and "related to," the claim for a lien for fees qualifies as "related to" the title 11 case on the supplemental jurisdiction theory that it is so related to the § 362 and § 329(b) claims within this

court's original jurisdictional that they form part of the same case or controversy under Article III of the United States Constitution. 28 U.S.C. §§ 1334(b) & 1367; Sasson, 424 F.3d at 869.

F

The next layer of the onion is abstention.

[22] Henderson's assertion that her lien-based claim to fees must be determined by a California state court is construed as a § 1334(c) request for abstention. 28 U.S.C. § 1334(c).

Abstention subdivides into mandatory abstention and discretionary abstention.

1

[23] This cannot be an instance of mandatory abstention under § 1334(c)(2), which can only occur with respect to a "related to" claim under state law, because there is no action commenced that can be timely adjudicated in a state forum of appropriate jurisdiction. 28 U.S.C. § 1334(c)(2).

Indeed, this adversary proceeding arrived in federal court because the California Third District Court of Appeal ruled that the Sundquists' California cause of action for wrongful foreclosure based solely on a bankruptcy automatic stay violation is a matter of exclusive federal jurisdiction. Regardless of whether its conclusion about exclusivity of federal jurisdiction was correct, this constitutes a ruling by a state appellate court that the Sundquists' wrongful-foreclosure-in-violation-of-automatic-stay theory belongs in federal court.

The corollary is that the California courts view attorney fees associated with such a wrongful foreclosure action premised solely on a bankruptcy automatic stay as a matter also within the jurisdiction of the federal bankruptcy court.

2

[24] Permissive abstention is potentially available under § 1334(c)(1). The statute provides that "nothing prevents" a court "from abstaining" in the interest of justice, or the interest of comity with state courts, or out of respect for state law. 28 U.S.C. § 1334(c)(1). That syntax commits the abstention question to the discretion of the court.

[25] None of the § 1334(c)(1) factors would be served by abstaining from hearing what amounts to an end-run around a bankruptcy court's § 329(b) order. Interests of justice favor keeping trial-related matters in the one court, subject to one appellate system. Comity is not offended where the state court of appeals has disclaimed jurisdiction over the underlying cause of action. Respect for state law is not a factor because, first, § 329(b) is a federal question not based on state law and, second, it is conceded that the contingency fee contract has recently been voided as not having complied with state law.

This court elects not to exercise its discretion to abstain.

G

In sum, automatic stay enforcement is a matter of retained jurisdiction under 28 U.S.C. § 1334. Neither the dismissal of the case, nor the closing of the case vitiates the bankruptcy court's authority to redress the automatic stay violations presented in this case.

Necessarily accompanying that retained jurisdiction is the § 329 bankruptcy court authority over the attorneys' fees that are "connected with" the bankruptcy case under the overlapping "arising in" and "related to" prongs of § 1334 jurisdiction.

While this court has discretion to abstain from exercising such jurisdiction, it elects not to abstain.

II

Having concluded that the exercise of federal bankruptcy jurisdiction over the fees of debtors' counsel is appropriate notwithstanding the dismissal and the closing of the Sundquist chapter 13 case, the focus shifts to the terms of § 329(b).

A

The relevant terms of § 329 require a statement of compensation and a remedy for excessive compensation.

Any attorney representing a debtor in connection with a case under title 11 must file a statement of compensation agreed to be paid, for any payment or agreement "made after one year before the date of the filing of the petition" for services to be rendered in connection with the case. 11 U.S.C. § 329(a).

If the agreed compensation "exceeds the reasonable value of such services, the court may cancel any such agreement" and limit compensation to reasonable value. 11 U.S.C. § 329(b).

1

[26] We start with the temporal. Payments and agreements "made after one year before the filing of the petition" must be disclosed in a filed statement. 11 U.S.C. § 329(a).

At face value, the payments and agreements subjected to disclosure reach back one year before the filing of the petition and extend after the filing of the petition indefinitely—theoretically, to the end of time.

[27–29] That no time limit is suggested in the sweep of § 329 is not surprising. Congress provided for a number of indefinite term situations in the Bankruptcy Code. Unscheduled property (typically an undisclosed cause of action or undisclosed interest in real estate) is not deemed abandoned and administered at the closing of the case and retains its status as property of the estate indefinitely. 11 U.S.C. § 554(d); e.g., In re Dunning Bros., 410 B.R. 877, 879 (Bankr. E.D. Cal. 2009) (case filed in 1936 reopened in 2009 to administer undisclosed interest in real estate). The automatic stay of acts against property of the estate does not terminate when a case is closed and "continues until such property is no longer property of the estate." 11 U.S.C. § 362(c)(1). The discharge injunction is permanent and may lead to enforcement proceedings years later. 11 U.S.C. § 524(a); e.g., Lone Star Sec. & Video, Inc., v. Gurrola (In re Gurrola), 328 B.R. 158, 164–76 (9th Cir. BAP 2005).

[30] The § 329 obligation of an attorney for the debtor to disclose fees and fee agreements is co-extensive with a debtor's involvement in a bankruptcy case and remains in effect for so long as § 1334 jurisdiction connected with that case survives.

2

The limiting principle for § 329 lies in the phrase "in connection with such a case." 11 U.S.C. § 329(a).

[31] Rule 2017(b) supplies a rule of construction emphasizing that "in connection with" in § 329 is a broad concept that extends to "services in any way related to the case." Fed. R. Bankr. P. 2017(b).

Representation "in connection with such a case" necessarily includes everything that is premised on § 1334 jurisdiction.

It also includes supplemental jurisdiction under § 1367 over all other claims that are so related to claims in the action within the court's § 1334 original jurisdic-

tion that they form part of the same case or controversy under Article III of the United States Constitution. Sasson, 424 F.3d at 869; Pegasus Gold, 394 F.3d at 1195.

[32] Representation "in connection with such a case" is not limited to actions in federal court. As § 1334(b) jurisdiction over civil proceedings arising under title 11, or arising in or related to cases under title 11 is "original but not exclusive"—i.e. concurrent federal and state jurisdiction—such actions might be prosecuted in state court. 28 U.S.C. § 1334(b).

Representation "in connection with such a case" extends to other actions in state courts in other states. The Fourth Circuit, speaking through a panel that included retired Supreme Court Justice Lewis Powell, held that two Ohio state-court actions pursued under state-law business tort theories against a bank to create leverage against that bank's nondischargeability action in a West Virginia bankruptcy case were "in connection with" the bankruptcy case. Burd v. Walters (In re Walters), 868 F.2d 665, 667 (4th Cir. 1989). In so ruling, it endorsed the broad "in any way related to" construction set forth in Rule 2017(b) and concluded that the bankruptcy court did not abuse discretion by exercising § 329(a) control over the Ohio lawyer's fees for state-court work. Walters, 868 F.2d at 666 n.1 & 667.

Here, the subject fees are for representing the Sundquists in prosecuting a § 362(k)(1) cause of action that "arises under" the Bankruptcy Code on account of automatic stay violations in their chapter 13 bankruptcy case. Such fees, beyond cavil, are "in connection with" their bankruptcy case for purposes of § 329.

3

[33] The § 329(b) powers to cancel fee agreements and order return of payments to the extent that they exceed the "reasonable value" of services are committed to the discretion of the bankruptcy court. Am. Law Ctr., PC v. Stanley (In re Jastrem), 253 F.3d 438, 442 (9th Cir. 2001).

a

[34] In determining "reasonable value," the touchstone is the § 330(a)(3) list of considerations for determining reasonable compensation for officers and professional persons. 11 U.S.C. § 330(a)(3); Jastrem, 253 F.3d at 443 (invoking § 330(a)(3) in review of § 329(b) order).

The considerations focus on the nature, extent, and value of services, taking into account all relevant factors, including time spent, rates charged, and customary compensation in comparable cases. Jastrem, 253 F.3d at 443; 3 COLLIER ¶ 329.04 [1] [c].

[35] In this circuit, a reasonable hourly rate multiplied by the number of hours actually and reasonably expended, the so-called lodestar rate, is presumptively a reasonable fee in a bankruptcy case. Manoa Finance, 853 F.2d at 691–92.

[36] Here, Henderson documented 207.56 hours devoted to the Sundquist litigation at her usual hourly rate of $300.00, together with $6,606.55 in costs, for a total of $68,874.55.

[37] Quality of services may be taken into account. Hale v. U.S. Trustee, 509 F.3d 1139, 1147 (9th Cir. 2007); In re Sponhouse, 477 B.R. 147, 155 (Bankr. D. Nev. 2012); In re Dean, 401 B.R. 917, 922 (Bankr. D. Id. 2008).

Here, the court took into account the factors identified in Manoa Finance and also considered the risk of nonpayment. The quality of performance was, in this court's judgment, not worthy of $300.00 per hour. Nevertheless, it accepted that

claimed rate, reasoning that it included an implicit enhancement (perhaps 50 percent) above normal lodestar for an attorney of her caliber of performance that could be justified as accommodating the risk of non-payment. Accordingly, the court determined that compensation in excess of $70,000.00 would be excessive within the meaning of § 329(b).

Although this court viewed the "reasonable value" question through the prism of § 329(b), there is an alternative and independent analysis that leads to the same result. The Ninth Circuit recognizes as part of making an actual damages award under § 362(k)(1) the authority of a bankruptcy court to limit fees to "fees reasonably incurred" and holds that courts awarding fees under § 362(k)(1) "retain the discretion to eliminate unnecessary or plainly excessive fees." America's Servicing Co. v. Schwartz–Tallard (In re Schwartz–Tallard), 803 F.3d 1095, 1101 (9th Cir. 2015) (en banc).

Applying Schwartz–Tallard, this court in the exercise of its discretion is persuaded that a fee greater than $70,000.00 would be plainly excessive.

Either way, Manoa Finance teaches that this court's award of $70,000.00 is presumptively reasonable compensation.

b

Congress also provided in § 329(b) that the court may cancel a fee agreement. While the terms of that section do not expressly specify a standard for determining whether to cancel such an agreement, the ultimate question is whether the agreement would call for excessive compensation.

[38] Contingency fee agreements are as vulnerable to cancellation under § 329(b) as hourly fee agreements. Pope v. Knostman (In re Lee), 884 F.2d 897, 899 (5th Cir. 1989) ("Regardless of whether [attorney's] fee was a flat fee or a contingency fee, [attorney] was entitled to receive compensation only for the reasonable value of the services rendered to the Debtors.").

The context of § 362(k)(1) affects the analysis of the reasonableness of a contingency fee. The statutory phrase "shall recover actual damages, including costs and attorneys' fees," makes attorneys' fees a component of damages. Schwartz–Tallard, 803 F.3d at 1099–1101.

Where attorneys' fees are an element of actual damages in a automatic stay proceeding, such as this case, in which there are undeniable and non-trivial stay violations by a deep-pocketed creditor, some degree of § 362(k)(1) liability is virtually inevitable. Any liability will bring with it the certainty that reasonable attorneys' fees will be awarded and be collectable.

The structure of the unusual approach to fees in § 362(k)(1) indicates a policy by Congress to assure that attorneys will be assured of being paid fairly for their time and effort in vindicating the rights of individual victims of stay violations. This attorney-fee-friendly policy is furthered by assuring lodestar compensation for counsel who must enforce the automatic stay for injured individuals who, in the vast majority of cases, are impecunious debtors.

The corollary to the attorney-fee-friendly damages provision in § 362(k)(1) that materially reduces the risk of non-payment is to undermine the standard justification of the need for contingent fees—i.e. risk of nonpayment.

It was not irrational for Congress to create a structure that links attorneys' fees to the time and effort reasonably devoted to the task of enforcing the automatic stay, rather than to the amount of the ultimate award. The prospect of full reasonable compensation as an element of

actual damages reduces the incentives for counsel to complicate stay enforcement litigation by seeking extravagant punitive damages for personal profit or to pursue doubtful cases on speculation. Likewise, this structure gives the stay violator an economic incentive to make amends promptly, so as to minimize fee damages, rather than to wage litigation warfare.

When this court ordered Ms. Henderson to explain how her contingency fee agreement represents the reasonable value of services per § 329(b) and comports with the attorneys' fee structure set forth in § 362(k)(1), she did not try to square her contingency fee with the statute and, instead, quoted from Schwartz–Tallard and saying she "will only seek the lesser of the contingency fee agreement or the reasonable hourly rate times the number of hours expended consistent with the Lodestar method." Supplemental Briefing Regarding Attorneys' Fees, p. 2, Case 10–35624, Dkt. 73 (9/23/16).

It is now claimed that the "quantum meruit value of Ms. Henderson's services far exceeds the $70,000 the court awarded her." Supplemental Opposition to Motion to Expunge Lien, p. 11, Adv. Pro. 14–02278, Dkt. 511 (10/24/17).[9] There is still no attempt by Ms. Henderson to square a contingent fee, or a quantum meruit equivalent, with the structure of § 362(k)(1). The problem remains that the lodestar fee for Ms. Henderson's services is conceded to be $68,874.55. If the real fees "far exceed $70,000," then, in view of their status as actual damages, does the actual damages award need to be increased? How would that be justified in light of the command of Schwartz–Tallard to limit fees to fees reasonably incurred? No answers favorable to Ms. Henderson suggest themselves.

This court had the discretion under § 329(b) to cancel the contingency fee agreement. That discretion was exercised in favor of cancellation, mindful that counsel was being fully compensated according to her own version of lodestar principles.

B

Rules 2016 and 2017 implement § 329. Fed. R. Bankr. P.2016 & 2017.

1

[39] Nondisclosure and defective disclosure warrant denial of all fees in the discretion of the court.

2

Rule 2016(b) required Ms. Henderson to file a disclosure of compensation paid or promised to be paid within 14 days of the order for relief when the Sundquist case was filed in June 2016. She complied with that requirement.

Rule 2016(b) also required Ms. Henderson to file a supplemental statement within 14 days after entering into the agreement to represent the Sundquists in their § 362(k)(1) action. Taking her at her word that there was an agreement executed when or soon after she entered her appearance as counsel on September 19, 2014, she was in default of that obligation from 2014 until September 12, 2016, when she filed a supplemental statement that cryptically revealed "contingency" in response to this court's order. Case 10–35624, Dkt. 69 (9/12/16).

Rule 2017(b) permits the court on its own initiative, after notice and a hearing, to determine whether any fee agreement

9. The noise in Ms. Henderson's brief about the existence of a contingency fee with the Sundquists' successor counsel is a red herring. This court has not endorsed that fee arrangement and has not yet had the occasion to address it.

with an attorney entered after the order for relief in the case is excessive if the agreement "is for services in any way related to the case." Fed. R. Bankr. P. 2017(b).

The phrase "notice and a hearing" means notice as is appropriate in the particular circumstances and opportunity for a hearing as is appropriate in the particular circumstances. 11 U.S.C. § 102(1)(A).

An act is authorized without an actual hearing if notice is given properly and if an actual hearing is not requested timely by a party in interest. 11 U.S.C. § 101(1)(B)(i).

This court complied with the notice and opportunity for hearing requirement by way of two orders that drew written responses from Ms. Henderson. First, the order filed August 24, 2016,—Order that Dennise Henderson File Statement Required by 11 U.S.C. § 329(a) and Federal Rule of Bankruptcy Procedure 2016(b)—noted the procedural history, recited the requirements of § 329, included a block quotation of all of § 329, explained that the court is authorized to scrutinize such fees for reasonableness, and included a block quotation of all of Rule 2016(b). Case 10–35624, Dkt. 60 (8/24/16). She was ordered to file the supplemental statement by September 12, 2016.

Upon review of Ms. Henderson's supplemental Rule 2016(b) statement that revealed nothing but "contingency," this court entered a second order—Order that Dennise Henderson File Copy of Contingency Fee Agreement and Justify Agreement Under 11 U.S.C. §§ 329(b) and 362(k)(1)—in which it was explained that contingency fee agreements are subject to § 329(b) review for reasonable value of services. It also noted that it is unclear whether a contingency fee agreement is consistent with the attorneys' fee structure set forth in § 362(k)(1). She was ordered to file by September 23, 2016, a copy of her contingency fee agreement and to "provide an explanation justifying the agreed contingency fees as, first, representing the reasonable value of services within the meaning of § 329(b) and, second, how her contingency fee agreement is consistent with the attorneys' fee structure set forth in 11 U.S.C. § 362(k)(1)." Case 10–35624, Dkt. 70 (9/14/16).

Ms. Henderson responded by filing her Supplemental Briefing Regarding Attorneys' Fees. She acknowledged that the court has "authority under 11 U.S.C. § 329(b) and Federal Rule of Bankruptcy Procedure 2017(b) to order a debtor's attorney to return any attorneys' fees that exceeded the reasonable value of services provided." She noted that § 330 sets out the standard for determining reasonableness under § 329. And she asserted:

> it was never the intent of counsel to exceed the reasonable compensation under the [B]ankruptcy [C]ode. By separate declaration, I will file a time billing with the actual time expended and will only seek the lesser of the contingency fee agreement or the reasonable hourly rate times the number of hours expended consistent with the Lodestar method.

Case 10–35624, Dkt. 73 (9/23/16).

Next, she filed a Declaration of Dennise Henderson on Attorneys Fees and Costs in which she claimed 207.56 hours spent on the § 362(k)(1) adversary proceeding at a rate of $300.00 per hour (= $62,268), together with costs for depositions, transcripts, and trial binders of $6,606.55 for a total of $68,874.55. Case 10–35624, Dkt. 75 (9/26/16).

Based on this written exchange, this court concluded that the notice and opportunity for hearing requirement had been satisfied and that, in view of her concession that she was not seeking a contingen-

cy greater than $68,874.55, further concluded that no actual hearing was needed.

Ms. Henderson now claims that it was always her intent to collect from the Sundquists the full amount of her contingency to the extent that it exceeded lodestar compensation.

3

[40] The counsel statements required by § 329(a) and Rule 2016(b) must include "full, candid, and complete" disclosure. Neben & Starrett v. Chartwell Fin. Corp. (In re Park–Helena), 63 F.3d 877, 882 (9th Cir. 1995), citing with approval, In re Plaza Hotel Corp., 111 B.R. 882, 883 (Bankr. E.D. Cal. 1990).

[41] Ms. Henderson's filed statement asserted that she did not intend to collect more than reasonable compensation and that she "will only seek the lesser of the contingency fee agreement or the reasonable hourly rate times the number of hours expended consistent with the Lodestar method," which she then fixed at $68,874.55.

She did not disclose that, as she now says, she always intended to enforce the full contingency against the Sundquists. If accurate, then the disclosure to the court was materially defective because it did not disclose full relevant information.

[42] The law of the Ninth Circuit established in Park–Helena that "even a negligent or inadvertent failure to disclose full relevant information may result in denial of all requested fees" in the discretion of the court. Park–Helena, 63 F.3d at 882.

The record admits of two possibilities, each of which would, in the court's discretion, justify complete denial of attorneys' fees. If the undisclosed intention to enforce the full contingency is not a recent fabrication, then there was a failure to disclose full relevant information for which all fees may be denied. If the undisclosed intention is a recent fabrication, then counsel has lied to the court in a declaration and papers filed in opposition to this motion for which sanctions are appropriate on a variety of theories. Either way, this court has the discretion to deny all fees.

III

[43] Ms. Henderson waived and renounced her right to claim for additional compensation on quantum meruit or any other theory in her responses to this court's request that she justify her contingency fee agreement under § 329(b) and § 362(k)(1).

First, she filed a statement saying: "it was never the intent of counsel to exceed the reasonable compensation under the [B]ankruptcy [C]ode. By separate declaration, I will file a time billing with the actual time expended and will only seek the lesser of the contingency fee agreement or the reasonable hourly rate times the number of hours expended consistent with the Lodestar method." Case 10–35624, Dkt. 73 (9/23/16).

Second, she filed a Declaration in which she claimed 207.56 hours spent on the § 362(k)(1) adversary proceeding at a rate of $300.00 per hour (= $62,268), together with costs for depositions, transcripts, and trial binders of $6,606.55 for a total of $68,874.55. Case 10–35624, Dkt. 75 (9/26/16).

She cannot now claim more.

IV

[44] Quantum meruit principles are not available to rescue counsel from cancellation of her contingency fee contract and the consequences of not disclosing her secret intent to enforce the contingency fee for a sum greater than a lodestar award.

[45] Under state law, the voiding of a contingency fee contract disentitles the attorney to any fee greater than a "reasonable" fee. Cal. Bus. & Prof. Code § 6147(b) ("failure to comply with any provision of this section renders the agreement voidable at the option of the plaintiff, and the attorney shall thereupon be entitled to collect a reasonable fee").

[46] Viewed as a matter of federal law, the equitable remedy of quantum meruit is not available following the denial of fees as a remedy for not complying with § 329(a) and Rule 2016(b). One who has not complied with the Code and Rules lacks the requisite clean hands. Law Offices of Ivan W. Halperin v. Occidental Fin. Group, Inc. (In re Occidental Fin. Group, Inc.), 40 F.3d 1059, 1063 (9th Cir. 1994), citing with approval, DeRonde v. Shirley (In re Shirley), 134 B.R. 940, 944–45 (9th Cir. BAP 1992).

[47] Nor is quantum meruit available to counsel in state court following denial of fees by a bankruptcy court. The Bankruptcy Code and the Federal Rules of Bankruptcy Procedure operate to preempt and preclude compensation on state-law theories not recognized by the Code and Rules.

[48] As explained in Shirley, an attorney who has been denied fees in bankruptcy court may not pursue an alternative remedy in state court: "to allow such a reading would be to circumvent the operation of provisions of the Code and Rules concerning the employment of professionals and the payment of fees in connection with bankruptcy cases." Shirley, 134 B.R. at 944, cited with approval, Occidental Fin. Grp., 40 F.3d at 1063.

The California courts would agree that they should defer to the federal courts in such circumstances. The California Third District Court of Appeal ruled in the Sundquists' state-court appeal that a wrongful foreclosure action premised solely on violation of the bankruptcy automatic stay is a matter of exclusive federal jurisdiction. It follows that the state court would regard a fee dispute deriving from that particular dispute as also within federal jurisdiction.

Even if state-law quantum meruit is not preempted and precluded, this court determines, as a finding of fact, that the quantum merited, i.e. the "reasonable" fee under either federal or state law, by Ms. Henderson is $70,000.00.

V

Ms. Henderson is threatening various actions in state court against the Sundquists, their successor counsel, and Bank of America for fees that "far exceed" $70,000.00 and for remedies, including punitive damages, under California's Uniform Voidable Transactions Act.

All such actions would constitute collateral attacks on this court's § 329(b) judgment that $70,000.00 is "reasonable" compensation for Ms. Henderson. All of the predicate facts are so inextricably intertwined with the § 362(k)(1) action that the bankruptcy court's judgment cannot be escaped other than by way of appeal. Miles v. Okun (In re Miles), 430 F.3d 1083, 1088–91 (9th Cir. 2005) (§ 303(i) damages remedy preempts state tort claims); Maitland v. Mitchell (In re Harris Pine Mills), 44 F.3d 1431, 1437–38 (9th Cir. 1995) (postpetition state law claims inextricably intertwined with bankruptcy sale); Gonzales v. Parks, 830 F.2d 1033, 1035–37 (9th Cir. 1987) (bankruptcy preempts state law abuse of process claims).

[49] Collateral attacks attempting to tunnel back on this court's § 329(b) judgment are within § 1334(b) jurisdiction because this court has jurisdiction to interpret and enforce its orders. Travelers Indemnity Co. v. Bailey, 557 U.S. 137, 151, 129 S.Ct. 2195, 174 L.Ed.2d 99 (2009).

Original federal subject-matter jurisdiction persists over § 329(b) matters as "arising under" the bankruptcy case. 28 U.S.C. § 1334(b).

Armed with original federal jurisdiction, the defendants in any such action would be entitled to remove them under the Bankruptcy Removal Statute. 28 U.S.C. § 1452(a). In short, they would come right back here to be adjudicated.

[50] The proper course for Ms. Henderson to challenge this court's § 329(b) judgment determining "reasonable" compensation to be $70,000.00 is to continue to appeal that order pursuant to regular federal appellate procedure. 28 U.S.C. § 158. She already has filed a notice of appeal, which will become effective when final judgment is entered. Fed. R. Bankr. P. 8002(b)(2). She is welcome to avail herself of that opportunity.

VI

The question becomes what to do. Acting pursuant to § 329(b) and relying on her representations to the court in connection with her § 329(a) and Rule 2016(b) disclosures and Rule 2017 response that her full lodestar fees were $68,874.55 and that she wanted the "lesser" of that sum or her agreed contingency fee, the court awarded Ms. Henderson $70,000.00. It was persuaded that $70,000.00 was generous in light of the quality of work and that any greater amount would exceed the reasonable value of services. To avoid ambiguity, and acting consistent with her representation that she wanted the "lesser" of contingency or lodestar, it cancelled the contingency fee agreement as permitted by § 329(b).

Now she reveals that she always secretly intended to collect the full contingency from the Sundquists. That revelation puts her in the cross-hairs of the Ninth Circuit Park–Helena doctrine that gives this court discretion to deny all fees. Park–Helena, 63 F.3d at 882. Her statements under § 329(a) and Rules 2016(b) and 2017 were anything but "full, candid, and complete."

She has been litigating in a manner that equates with an effort to sabotage the settlement her former clients have achieved. It is one thing to assert an attorneys' lien, which was unnecessary in view of this court's mandatory injunction requiring the Sundquists to pay her $70,000.00. It is quite another thing overtly to try to create hold-up value to extort a settlement by creating delay and by threatening voidable transfer litigation and punitive damages against successor counsel, former clients, and the settling defendant. That conduct tempts the court to invoke Park–Helena to set off against the $70,000.00 all fees and expenses incurred by the Sundquists in fending off her demands for "far more" than the "reasonable" $70,000.00.

Nevertheless, the fact remains that counsel undertook a representation that other lawyers declined. She stood up for the Sundquists. In the tradition of lawyers who find themselves needing to act as amateur psychologists to clients in emotion-charged situations, she held their hands and comforted them through the process. She may have flailed in water over her head in competition with a strong-swimming defense, but at least the facts were on her side. While there is much to be criticized about the quality of, and omissions in, her litigation presentation, it was adequate—barely adequate—to enable this court to discern the just result.

Accordingly, this court will exercise its discretion to refrain from using Park–Helena to reduce the $70,000.00 to zero or to some intermediate sum.

The Sundquists remain under a mandatory injunction to pay Ms. Henderson $70,000.00 from their recovery, enforceable by contempt. As the asserted lien is unnec-

essary in view of the mandatory injunction, the lien will be expunged in its entirety.

* * *

In short, this court has authority and jurisdiction to limit counsel's fees under § 329(b) to the "reasonable" amount of $70,000.00. Although abstention over the fee dispute would be permissible, this court exercises its discretion to retain jurisdiction. Under § 329(b), the "reasonable" value of services rendered by debtor's counsel is $70,000.00. Although counsel did not disclose her fee arrangements in the "full, candid, and complete" manner required by law, this court exercises its discretion to leave untouched its $70,000.00 award. Proceedings in the nature of attempts to garner from other courts fees in excess of $70,000.00 are nevertheless matters of original federal jurisdiction per Judicial Code § 1334(b) as "arising under" the Bankruptcy Code and will be subject to removal to this court per Judicial Code § 1452.

This opinion contains findings of fact that supplement findings made and reported at Sundquist, 566 B.R. at 570–621.

An order will issue expunging the subject lien.

IN RE VEGAS MANAGEMENT, LLC, JFL Venture Fund IV, LLC, Debtors.

Case No.: 8:16–bk–04856–KRM, Case No.: 8:16–bk–04857–KRM

United States Bankruptcy Court, M.D. Florida.

Signed October 24, 2017

Filed October 25, 2017

Background: Following auction sale of debtor's real property, real estate broker moved for allowance of commission as administrative expense of estate.

Holding: The Bankruptcy Court, K. Rodney May, J., held that while real estate broker may have brought Chapter 7 debtor's property to attention of principal of company which was high bidder at auction sale of property conducted by auctioneer hired by trustee, and to which property was ultimately sold, broker was not "procuring cause" of sale to this company, and was not entitled to real estate commission as administrative expense.

Motion denied.

1. Brokers ⚷53

Under Florida law, in order to be the "procuring cause" of real estate sale and thus to be entitled to commission, broker must show that he called the potential purchaser's attention to the property, and that it was through his efforts that sale was consummated.

See publication Words and Phrases for other judicial constructions and definitions.

2. Brokers ⚷57(2)

Under Florida law, real estate broker is entitled to compensation if he brought the parties together and a sale is effectuated as result of his efforts, even though the seller interrupts those negotiations and sells directly to the purchaser at a price lower than what the broker was authorized to offer.

3. Brokers ⚷56(3)

Under Florida law, real estate broker does not need to be involved in continuous negotiations with the parties in order to be entitled to commission in connection with sale, if broker was intentionally excluded from the parties' negotiations.

upon an assessment of the culpability of the individual party based on the circumstances of the case.

Finally, the Court will not decide whether it is authorized by the Bankruptcy Code or rules to appoint a monitor or whether such an appointment is tantamount to the appointment of a master, a remedy unavailable in bankruptcy cases pursuant to Rule 9031. It does find, however, that given its rulings on the primary substantive and procedural questions and that the motion to dismiss has been denied only with respect to the few proofs of claim filed in the underlying bankruptcy cases, administration of whatever remedy the Court might order, if it were something beyond disallowance of the claim, is insufficiently complex to warrant the appointment of a monitor.

For all these reasons, the Court grants the motion to dismiss insofar as it relates to Counts I, II, III and VI and denies the motion to dismiss as to Counts IV and V.

IN RE: Thomas M. GRABANSKI and Mari K. Grabanski, Debtors.

Bankruptcy No. 10–30902

United States Bankruptcy Court, D. North Dakota.

Signed 10/24/2017

Background: Creditors sought to compel debtors' attorney to disgorge compensation that he had allegedly received from companies wholly owned by the debtors for legal work allegedly performed in connection with case, as allegedly being in excess of that which the court had found reasonable. Attorney objected, inter alia, on ground that court lacked jurisdiction to consider disgorgement request after underlying bankruptcy case was dismissed, and that creditors did not have standing to seek disgorgement.

Holdings: The Bankruptcy Court, Thad J. Collins, J., held that:

(1) bankruptcy court had jurisdiction, even after debtors' bankruptcy case was dismissed, over request by creditors to order debtors' attorney to disgorge compensation that he allegedly received in excess of that approved as reasonable;

(2) creditors had standing to seek disgorgement;

(3) prior determination by North Dakota state court as to whether party with alleged security interest in funds transferred to debtors' attorney could set that transfer aside on fraudulent transfer avoidance theory was not res judicata on whether transfer, allegedly being in payment for services that attorney provided in connection with bankruptcy case, represented compensation in excess of that which bankruptcy court had approved as reasonable;

(4) *Rooker-Feldman* doctrine did not apply;

(5) debtor's attorney failed to show that fee payments which he received, during pendency of debtors' bankruptcy case, from companies wholly owned by the debtors were not for services performed "in connection with" bankruptcy case; and

(6) attorney's delay, misrepresentations, and continued reliance on arguments that bankruptcy court had already rejected, in opposing request that he be directed to disgorge compensation in excess of reasonable value of his services, was such as to warrant award of

reasonable attorney fees to creditors prosecuting disgorgement request.

Ordered accordingly.

1. Bankruptcy ⚷2057

Bankruptcy court had jurisdiction, even after debtors' bankruptcy case was dismissed, over request by creditors to order debtors' attorney to disgorge compensation that he allegedly received for his work in connection with case in excess of that approved as reasonable by court, regardless of length of time that case had been dismissed, and regardless of whether bankruptcy court had specifically retained jurisdiction over disgorgement issue in case dismissal order. 11 U.S.C.A. § 329.

2. Bankruptcy ⚷3204

Creditors of estate, who would share in any additional distribution to creditors made possible by bankruptcy court's ruling on whether debtors' attorney should be directed to disgorge compensation allegedly received for his work in connection with case in excess of that approved as reasonable, had standing to seek disgorgement. 11 U.S.C.A. § 329.

3. Bankruptcy ⚷2159.1

Term "party in interest," as used in bankruptcy statute authorizing parties in interest to appear and be heard on any issue arising in Chapter 11 case, is to be construed broadly, in order to allow parties affected by Chapter 11 case to appear and be heard. 11 U.S.C.A. § 1109(b).

See publication Words and Phrases for other judicial constructions and definitions.

4. Bankruptcy ⚷3204

Even assuming that creditors did not have standing to seek disgorgement of compensation allegedly received by debtors' attorney for his work in connection with case, bankruptcy court had independent duty to review attorney's fees and to address whether disgorgement was proper.

5. Federal Courts ⚷3045(6)

Federal courts must give state court judgments the same preclusive effect as they would receive under law of the state in which judgment was rendered, so that state law determines preclusive effect in federal litigation of earlier state court judgment. 28 U.S.C.A. § 1738.

6. Judgment ⚷584, 713(2)

Under North Dakota law, res judicata is a doctrine that prohibits relitigation of claims or issues which were raised or could have been raised in prior action between same parties or their privies, and which were resolved by final judgment in court of competent jurisdiction.

7. Judgment ⚷540

Under North Dakota law, four elements must be present for application of res judicata: there must be (1) a final decision on the merits in an initial action by court of competent jurisdiction, (2) a second action must involve the same parties or their privies, (3) an issue in second action must have been actually litigated, or should have been litigated, in the first action, and (4) there must be an identity of the causes of action.

8. Judgment ⚷678(2)

"Privity" exists, of kind sufficient for application of res judicata under North Dakota law, if a person in second lawsuit is so identified in interest with a party to prior action that he represents the same legal right.

See publication Words and Phrases for other judicial constructions and definitions.

9. Judgment ⚷828.16(4), 828.21(2)

Prior determination by North Dakota state court as to whether party with al-

leged security interest in funds transferred to debtors' attorney could set that transfer aside on fraudulent transfer avoidance theory was not res judicata on whether transfer, allegedly being in payment for services that attorney provided in connection with bankruptcy case, represented compensation in excess of that which bankruptcy court had approved as reasonable, which attorney could be ordered to disgorge; requisite identity of parties and of issues was lacking, as party moving for disgorgement had not appeared in earlier state court action, nor did state court address issue of what was reasonable compensation for attorney's work in bankruptcy case, as issue that was exclusively for bankruptcy court. 11 U.S.C.A. § 329.

10. Courts ⚷509.2, 509.4

Basic theory of the *Rooker-Feldman* doctrine is that only the United States Supreme Court has jurisdiction to review state court decisions, so federal district courts generally lack subject matter jurisdiction over attempted appeals from state court judgments.

11. Courts ⚷509.2

Rooker-Feldman doctrine is confined to cases brought by state court losers complaining of injuries caused by state court judgments rendered before district court proceedings commenced and inviting district court review and rejection of those judgments.

12. Courts ⚷509.2

Rooker-Feldman doctrine does not otherwise override or supplant preclusion doctrine or augment the circumscribed doctrines that allow federal courts to stay or dismiss proceedings in deference to state court actions; *Rooker-Feldman* doctrine does not otherwise override or supplant preclusion doctrine or augment the circumscribed doctrines that allow federal courts to stay or dismiss proceedings in deference to state court actions.

13. Courts ⚷509.2

Four requirements must be met for application of the *Rooker-Feldman* doctrine: (1) federal court plaintiff must have lost in state court, (2) the plaintiff must complain of injuries caused by state court judgment, (3) the plaintiff must invite district court review and rejection of that judgment, and (4) the state court judgment must have been rendered before the district court proceedings commenced.

14. Courts ⚷509.3(6)

Rooker-Feldman doctrine did not apply to prevent bankruptcy court from addressing whether debtors' attorney should be required to disgorge payments, as compensation which he allegedly received for his work in connection with bankruptcy case, and which was in excess of compensation approved by bankruptcy court as reasonable, though some of this alleged compensation came from payment that had been challenged in state court, after debtors' bankruptcy filing, as actually or constructively fraudulent to creditors of third party making the payment; parties moving for disgorgement were not challenging propriety of state court's fraudulent transfer ruling or asking bankruptcy court to review or reverse it, and the bankruptcy fee proceedings commenced long before state court action. 11 U.S.C.A. § 329.

15. Bankruptcy ⚷3179

Phrase "in connection with such a case," as used in bankruptcy statute requiring an attorney representing debtor in bankruptcy case to disclose any fees received for services performed "in connection with such a case," is broadly interpreted to include any services that affect bankruptcy estate. 11 U.S.C.A. § 329(a).

See publication Words and Phrases for other judicial constructions and definitions.

16. Bankruptcy ⚷3179

To determine whether attorney's services are "in connection with" the bankruptcy case, such that attorney will have to disclose the compensation that he received for such services, bankruptcy courts apply an objective standard: if it can be objectively determined that the services rendered, or to be rendered, by attorney have, or will have, an impact on bankruptcy case, then such services are "in connection with" the bankruptcy case. 11 U.S.C.A. § 329(a).

See publication Words and Phrases for other judicial constructions and definitions.

17. Bankruptcy ⚷3181

Debtor's attorney failed to show that fee payments which he received, during pendency of debtors' bankruptcy case, from companies wholly owned by the debtors were not for services performed "in connection with" debtors' bankruptcy case, such that attorney could be required to disgorge these fee payments to the extent that total compensation which attorney received was in excess of reasonable value of his services. 11 U.S.C.A. § 329(b).

18. Bankruptcy ⚷3179

Disgorgement of fees is appropriate sanction for attorney's failure to comply with his or her fee disclosure obligations under bankruptcy statute and Bankruptcy Rule. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016.

19. Bankruptcy ⚷3171

Decision to reduce fees, deny fees or order disgorgement of fees under bankruptcy statute governing debtors' transactions with their attorneys is within sound discretion of bankruptcy court. 11 U.S.C.A. § 329.

20. Bankruptcy ⚷3171, 3179

While bankruptcy courts may exercise discretion to award or deny fees for attorney's failure to disclose, they should deny them when attorney, by his inadequate disclosure, fails to comply with the Bankruptcy Code and Rules. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016.

21. Bankruptcy ⚷3179, 3192

Bankruptcy court had to order debtors' attorney to disgorge compensation that he received in excess of reasonable value of his services, especially given attorney's failure to properly disclose this compensation. 11 U.S.C.A. § 329; Fed. R. Bankr. P. 2016.

22. Bankruptcy ⚷3192

Obligation of debtors' attorney to disgorge compensation that he received in excess of what had been found to be reasonable fee for his services by bankruptcy court had to be reduced to extent that attorney had already paid back a portion of this excess compensation as result of state court fraudulent transfer avoidance action or as result of court-approved settlements that he had previously reached with United States Trustee and case trustee. 11 U.S.C.A. § 329(b).

23. Bankruptcy ⚷2187

Courts have inherent power to levy sanctions in response to abusive litigation practices.

24. Bankruptcy ⚷2187

Court's inherent power to sanction is very powerful, and therefore must be exercised with restraint and discretion.

25. Bankruptcy ⚷2187

Primary aspect of court's inherent power to levy sanctions is the ability to fashion an appropriate sanction for conduct which abuses the judicial process.

26. Bankruptcy ⚷2187

Attorney's delay, misrepresentations, and continued reliance on arguments that bankruptcy court had already rejected, in opposing request that he be directed to disgorge compensation in excess of reasonable value of his services, was such as to warrant award of reasonable attorney fees to creditors prosecuting disgorgement request, in exercise of bankruptcy court's inherent power to levy sanctions for abusive litigation practices. 11 U.S.C.A. § 329(b).

Vickie L. Driver, Husch Blackwell LLP, Dallas, TX, DeWayne Johnston, Johnston Law Office, Grand Forks, ND, for Debtors.

RULING ON DISGORGEMENT AND SANCTIONS

THAD J. COLLINS, U.S. BANKRUPTCY JUDGE, SITTING BY DESIGNATION

These matters came before the Court for hearing in Fargo, North Dakota on a number of filings related to the compensation of Debtors' counsel Attorney DeWayne Johnston and Johnston Law Office P.C.[1] Sean Foss appeared for Interested Parties John and Dawn Keeley ("the Keeleys"). David Thompson appeared for DeWayne Johnson and Johnston Law Office P.C. ("Johnston"). After hearing arguments, the Court took these matters under advisement. The parties did not offer evidence or testimony at the hearing. The parties relied entirely on the lengthy record already developed on these issues. The parties filed post-hearing briefs. This is a core proceeding under 11 U.S.C. § 157(b)(2).

STATEMENT OF THE CASE

Johnston received compensation for his work in connection with this bankruptcy beyond what the Court approved as reasonable. The Keeleys argue that Johnston received $262,301.50 (or possibly $567,801.50 depending on treatment of a $300,000 payment) even though the Court approved only $37,013.76. The Keeleys ask the Court to order Johnston to disgorge the difference between what he received and what was approved—$262,301.50 or possibly $526,787.74.

Johnston argues that the Court cannot order him to disgorge fees related to this case. He argues: that the Court does not have jurisdiction over his fees because the Court dismissed the bankruptcy; that the Keeleys do not have standing to request disgorgement; that res judicata and the Rooker–Feldman doctrine preclude disgorgement; and that fees paid to him beyond the Court-approved amount were not for work done "in connection with" this case. He argues that, even if the Court could order disgorgement, he has already returned much of the money at issue through settlements and other litigation. The Court rejects Johnston's legal arguments, finds that his disputed fees were paid in connection with this case, that his fees exceeded the reasonable amount previously approved, and that he failed to properly disclose and explain the fees. The Court orders him to disgorge $44,887.74 in fees.

BACKGROUND AND FACTS

This case has a long and complicated history. The Court has previously outlined

1. The Honorable Thad J. Collins, Chief United States Bankruptcy Judge for the Northern District of Iowa, sitting by designation.

the history of this bankruptcy in its April 12, 2013, Memorandum and Order dismissing the bankruptcy. See Doc. 572 at 2–24. This history contained many examples of Debtors' delays and misrepresentations to the Court and creditors. See id. The Court noted that it had "bent over backwards to give Debtors every possible benefit of the doubt" during the bankruptcy. Id. at 31. The Court concluded that Debtors had "made no realistic effort to confirm a plan of reorganization," "failed to provide accurate bankruptcy schedules upon which parties could rely," and "willfully failed to abide by orders of the Court and to appear before the Court in proper prosecution of their case." Id. at 30–31. The Court dismissed the bankruptcy with prejudice.[2] Id. at 32.

Since that time, the disputes in the case have been almost entirely about Johnston's compensation for his work representing Debtors during the bankruptcy. Specifically, the parties have disputed whether Johnston properly disclosed all the compensation he received and whether he was entitled to that compensation. What follows is a detailed review of the dispute over Johnston's compensation.

In general, throughout these proceedings, the Keeleys, and other creditors, sought disclosures from Johnston about his compensation. They eventually sought disgorgement of compensation based on evidence that he received compensation related to the bankruptcy that the Court had not approved.

For his part, Johnston maintained that he received compensation in connection with this case only if the Court approved it. He has argued that fees paid to him from Debtors' wholly owned entities for work for those entities was not "in connection with" this bankruptcy and concludes that those fall outside his disclosure duties in this Court. The Court has repeatedly rejected that argument. He asserted that any mistakes were innocent and that he acted in good faith.

The Court has already issued three opinions related to Johnston's fees. The Court issued the first two of those opinions on the same day. In re Grabanski, Bankr. No. 10-30902, 2013 WL 1702416 (Bankr. D.N.D. Apr. 19, 2013) (Order on Final Application for Compensation); In re Grabanski, Bankr. No. 10-30902, 2013 WL 1702415 (Bankr. D.N.D. Apr. 19, 2013) (Order on Motion to Show Cause).

In its Order on Final Application for Compensation, the Court addressed Johnston's final fee application, which requested $43,845.41 in fees and expenses. In re Grabanski, 2013 WL 1702416, at *3. The Court noted that it had previously awarded Johnston $34,013.67 in fees, but had completely denied two later interim applications for $23,853.62 and $41,651.41 because there had been no progress in the case during the time covered by those interim applications. Id. at *2–3.

In ruling on Johnston's final fee application, the Court outlined the troubled history of the bankruptcy and said, "[I]t is hard to find much or any of the services or expenses contained in Attorney Johnston's Application for Final Compensation aimed at reorganization." Id. at *9. The Court concluded that Johnston was entitled to only $3,000 in addition to his initial interim award—for a final and total fee award of $37,013.76. Id.

In its Order on Motion to Show Cause, the Court addressed the Keeleys' Motion

2. Debtors would later file bankruptcy in the Eastern District of Texas—Bankruptcy No. 13–41818.

for Order to Show Cause and For Contempt. In re Grabanski, 2013 WL 1702415. That Motion was based on evidence that Johnston failed to disclose all the compensation he received for work in connection with the bankruptcy. Id. at *1–3. The evidence at that time showed that, despite having previously disclosed only $15,000,[3] "Johnston ... received at least $205,400 from Debtors or partnerships that are entirely owned by Debtors and/or under Debtors' control." Id. at *3. The Court said:

> Debtors' and Johnston's responses to all these requests for disclosure has basically been that the compensation approved to date is all the compensation he has gotten on this case. He suggests that the other money coming to him—from entities related to or owned by the Grabanskis—[is] not relevant because those entities are not in bankruptcy. This response has left great confusion about where a significant sum of money has gone. The disclosure requirement is not limited to amounts the Court has approved. The law requires disclosure of sums paid to an attorney representing a debtor "in connection with" a bankruptcy case. 11 U.S.C. § 329(a). As noted above, this section is broadly interpreted in favor of disclosure.
>
> The disclosures Attorney Johnston has made and his explanations for why he has not disclosed other payments are inadequate and do not meet the requirements of the Bankruptcy Code. He has received payments "in connection" with Debtors' case and/or closely related entities and failed to disclose them. The disclosures Debtors have made—after being directed to do so by the Court—have left open more questions than they have answered.

Id. at *4 (paragraph omitted). The Court then specifically ordered Johnston:

> to disclose all compensation, including monetary funds, property or other compensation, received from Debtors or related entities, including but not limited to G & K Farms, Texas Family Farms, MTM Farms, Grabanski Grain, LLC, the Keeley and Grabanski Land Partnership and any other entity in which Debtors have an interest, if such receipt was made after one year before the date of filing. The disclosure must include the date and amount of the payments and the payor of the compensation. It must also specifically address whether the compensation has been earned. If it has been earned, the disclosure must include the nature of the services provided and a description of the proceeding in which they were incurred, particularly in proceedings not held before this Court. If the compensation is unearned, the remaining balance of the compensation and the location where the compensation is currently being held must be disclosed.

Id. The Court denied the Keeleys' request for attorney's fees and sanctions at that time, but noted that the Keeleys' could renew those arguments and requests after Johnston made his full disclosure. Id. at *5.

On June 5, 2013, Johnston's filed his Disclosure of Compensation. Doc. 578. The Keeleys, joined by Choice Financial Group and PHI Financial Services ("Choice" and "PHI," respectively), creditors in the case, objected to Johnston's disclosure and Johnston responded to those objections.

3. Notably, Johnston disclosed the $15,000 in compensation only after the Court specially ordered Johnston to follow § 329 and disclose his compensation. Doc. 375, entered December 14, 2011 (granting United States Trustee's Motion to Compel Attorney to File Disclosure of Compensation Paid or Promised).

Docs. 590, 591, 593, 598 and 599. The Keeleys argued that Johnston's Disclosure of Compensation failed entirely to comply with the Court's order. The Keeleys asked the Court to order Johnston to comply and to produce his billing and IOLTA trust account records. The Keeleys also sought disgorgement and payment of their attorney's fees.

On July 26, 2013, the Court held a hearing on the disclosure and objections and took the matter under advisement. The Keeleys filed a supplemental objection and Johnston replied. Docs. 603 and 605.

On October 27, 2014, the Court entered an Order addressing Johnston's disclosure of compensation. Doc. 608. The Order again detailed the case's history, relevant facts, and the parties' positions. Id. at 2–12. In the Order, the Court referred to Johnston's disclosure, doc. 578—as Johnston referred to it—"the Accounting." Id. at 4. The Court found, "The Accounting does not satisfy the requirements of the [Court's April 19, 2013 order requiring Johnston to disclose his compensation]." Id. at 15. The Court noted that the Accounting failed to clarify many important aspects of compensation disclosure—in particular, "whether larger lump sums were received, and if so, how many, and whether there is or was ever unearned compensation remaining in Johnston's IOLTA trust account"; "how lump sum payments were applied, particularly the $170,400 received on October 11, 2011"; "whether Johnston has separate trust accounts for Debtors and each of their related entities or whether legal fees for all are paid from one trust account"; and "whether there are funds in any of these trust accounts." Id. at 15. The Accounting also failed to provide detailed information about "who made payments ..., when those payments were made, the amount of those payments, and how those payments were dissipated or held." Id. at 15–16. The Court noted other deficiencies in the Accounting and discrepancies between the Accounting and other documents Johnston filed. Id. at 16–20. The Court concluded that, "[T]he Accounting does not comply with the Court's order entered on April 19, 2013." Id. at 20.

The Court further noted:

> Throughout Debtors' case, Johnston has been evasive in making disclosures regarding compensation and has only done so after prompting by other parties and orders of the Court. Debtors' case was filed in July 2010, and Johnston has yet to file a full disclosure. When he has made disclosures, the information contained in them, including the Accounting, has been speculative and caused concern for the Court. The disclosures have also been inconsistent.
>
> Additionally, Johnston continues to argue that compensation received from Debtors' related entities was not received "in connection with["] Debtors' case even though the Court rejected that argument in its previous order. The Accounting failed to satisfy the Court's directives and has left the Court questioning how Johnston received compensation.

Id. at 20–21.

The Court did not order Johnston to disgorge fees at that time like the Keeleys requested. Id. at 21 ("The Court finds disgorgement of compensation and payment of attorneys' fees is not warranted at this time—but will be considered if full and satisfactory compliance is not forthcoming immediately."). Instead, the Court found that "full disclosure of Johnston's billing records and his IOLTA trust account bank statements is appropriate now" and that such disclosure would "provide clarity on these issues." Id. at 21–22. "This is the Johnston Law Firm's last chance to clarify

the numerous issues that are discussed above. The failure to comply will almost certainly result in Sanctions and Disgorgement." Id. at 24.

The Court ordered Johnston to file an amended accounting along with his billing records and IOLTA trust account statements. Id. at 24. The Court ordered Johnston to file redacted IOLTA trust account statements with payments from Debtors and any of their related entities left unredacted. Id. at 24. The Court also ordered the United States Trustee to file a response to Johnston's disclosure with "a statement of the United States Trustee's position on the sufficiency of the disclosure." Id. The United States Trustee's office had taken a passive position on Johnston's compensation.

On November 11, 2014, Johnston filed his new Disclosure of Compensation, and supporting documents, including his IOLTA trust account statements. Docs. 610, 611, and 612 ("Final Disclosure"). On December 23, 2014, the United States Trustee filed its response to Johnston's Final Disclosure, as ordered. Doc. 613. The United States Trustee's response went through what it found to be the twelve issues that the Court had specifically addressed and required Johnston to answer and clarify in its October 27, 2014 Order. Id. at 3–8. The United States Trustee analyzed whether the Final Disclosure met the requirements of the order. Id. The United States Trustee noted that Johnston violated 6 of his duties as counsel for the Debtors: "Counsel failed to accurately disclose the amount and source of the compensation to be paid in connection with the bankruptcy case, as required by § 329"; "Counsel failed to disclose his connections to related entities and monies received in his application for employment as required under § 327 and Bankruptcy Rule 2014"; "Counsel paid himself without first obtaining court approval as required by § 330"; "Counsel's disclosures filed with the Court are incomplete, inconsistent and contradictory"; "Counsel failed to segregate estate funds from funds provided by related entities and failed to disclose that third parties were contributing funds to pay for services provided to the bankruptcy estate"; and "The accounting contains unexplained gaps." Id. at 11–12. The United States Trustee recommended that the Court order counsel to "disgorge the fees paid by the estate" and "sanction counsel by awarding the objecting creditors' attorney's fees in this matter." Id. at 13.

Johnston filed an objection to the United States Trustee's response in which he sought to clarify certain issues. Doc. 622. The United States Trustee then filed a Second Response to Disclosure replying to Johnston's clarifications. Doc. 626. The United States Trustee recommended, based on Johnston's response, "that the Court issue an order to show cause why it should not issue sanctions or disgorge the fees paid in the case." Id. at 13.

The Keeleys also filed a brief responding to Johnston's Final Disclosure in which they "reiterate[d] their request for disgorgement of all attorney fees received by attorney Johnston and Johnston Law Firm beyond the $34,013.76 previously approved by this Court." Doc. 625 at 15. The Keeleys also asked for "an award of attorney fees . . . for being the primary party pursuing this issue, having filed multiple motions and objections to draw out the true nature of the compensation received by Johnston." Id.

On February 26, 2015, the Court held a hearing on the Final Disclosure and ruled that it was still inadequate. Doc. 627. The next day, the Court entered an Order Setting Show Cause Hearing. Doc. 628. That order said, "At [the February 26, 2015] hearing, the Court determined that the

Disclosure of Compensation was inadequate and/or raised serious questions about the Johnston Law Firm's compliance with the Bankruptcy Code." Id. The Court scheduled the show cause hearing for April 9, 2015. Id.

Johnston appealed the show cause order to the United States District Court for the District of North Dakota. Doc. 629. The District of North Dakota noted that the appeal involved an interlocutory order, and as such, Johnston needed leave of the Court to appeal. Id. at 1–2. The District Court denied leave to appeal the interlocutory order and remanded to this Court. Id. at 3.

Johnston then filed a motion to vacate the order to show cause. Doc. 641, 643. Johnston argued that the Court did not have jurisdiction or authority to hold the show cause hearing or order him to disgorge fees. In particular, Johnston argued: (1) "The Court is barred from reviewing the $170,400 SURE payment by G & K Farms/TFF to Johnston Law by the Rooker–Feldman Doctrine"; (2) "The Order to Show cause, as it stands, is in violation of Johnston Law's due process rights as Johnston Law has not been given the necessary notice of specific allegations against Johnston Law"; (3) "The Court cannot review all the payments made to Johnston Law by the Grabanskis and their entities, as the majority of the payments are barred by res judicata or are outside the Court's jurisdiction"; (4) "Until the Court finds that all of the proceedings impacted the bankruptcy, the Court lacks jurisdiction to review payments made to Johnston Law Office for services provided outside this bankruptcy"; (5) "The Court is barred by res judicata from reviewing the $170,000 SURE payment, as the issue has already been adjudicated in a state court proceeding involving PHI, Choice, and Johnston Law"; (6) "The Court cannot reconsider any alleged bankruptcy violations by Johnston Law, as this Court issued a final order following the prior Order to Show Cause denying disgorgement and fees for violations of the bankruptcy code"; (7) "The Court cannot utilize Rules of Civil Procedure § 60(a) to amend its prior judgment"; and (8) "Creditors PHI, Choice Financial, the Texas Trustee, and the Keeleys do not have standing to contest payments to Johnston Law as these parties do not have a direct interest in disgorged funds." Id. passim. Johnston asked the Court to vacate the order to show cause based on these arguments. Id. at 49.

On April 9, 2015, the Court held a hearing on the order to show cause and Johnston's motion to vacate the order to show cause. Doc. 644. At that hearing, the parties informed the Court that Johnston and the United States Trustee had reached a settlement agreement with Johnston that called for Johnston to pay $15,000 to the Debtors' new bankruptcy estate in Texas. Based on this new information, the Court continued the show cause hearing indefinitely.

In the meantime, Johnston also entered into a settlement agreement with Mark Weisbart, the Chapter 7 Trustee in Debtors' Texas bankruptcy. In re Grabanski, Bankr. No. 13–41818, doc. 173 (Bankr. E.D. Tex. June 23, 2015). Trustee Weisbart had brought an avoidance action against Johnston. Id. at 3. Trustee Weisbart sought return of $23,350 in property that Debtors transferred to Johnston after this Court dismissed Debtors' bankruptcy. Id. Johnston and the Chapter 7 Trustee settled this action with the Trustee releasing the claims in exchange for Johnston paying Trustee $30,000. Id. The Bankruptcy Court for the Eastern District of Texas approved the settlement. In re Grabanski, Bankr. No. 13–41818, doc. 177 (Bankr. E.D. Tex. July 20, 2015).

On September 28, 2015, this Court held a status conference on the show cause hearing. At that hearing, the Court set a deadline for parties to respond to Johnston's motion to vacate the show cause hearing.

That same day, the Court entered an order approving the settlement between Johnston and the United States Trustee. Doc 649. Under that settlement, Johnston was to pay $15,000.00 to Debtors, care of the Chapter 7 Trustee in their previously filed and currently pending bankruptcy in the Eastern District of Texas. Id. at 2. Under the terms of the settlement, that payment would "satisfy and exonerate Johnston Law Office, P.C., and/or attorney DeWayne Johnston of any further claim under 11 U.S.C. § 329 or Federal Bankruptcy Rule 2016 for a turnover of fees, or 'disgorgement' of fees, or for sanctions, by the UST." Id. at 3. On January 9, 2016, Johnston filed a notice of compliance, stating that he had made the $15,000 settlement payment. Doc 662.

The Keeleys continued to pursue this matter after the settlement with the UST. The Keeleys had previously filed their reply to Johnston's motion to vacate the order for show cause hearing. Doc. 652. In that reply, the Keeleys argued that they had standing to pursue disgorgement under 11 U.S.C. § 1109(b). Id. at 2. The Keeleys also argued that they had a direct pecuniary interest in the funds because they are being pursued on debts from their partnership with Debtors and, to the extent fees are disgorged and sent to the Grabanski's Texas bankruptcy estate, they are creditors in that bankruptcy. Id. at 3–4. The Keeleys continued to press for further action from the Court.

On October 23, 2015, the Court held a hearing on these matters. At that hearing, the Court made the following comments to counsel for the Keeleys, with respect to the disclosure of compensation:

> [W]hen the U.S. Trustee is satisfied, I'm usually satisfied, and [if] you have some pretty good reasons to tell me why the U.S. Trustee being satisfied on the disclosure of compensation, as the watch dog over the whole thing, is not sufficient and we need to look at this a little more closely, then I'm open to that. But what I'm looking at here is, I think, your real objection is to Mr. Johnston having compensation out of this case to the extent that he thinks he wants compensation.... [So this is] really sort of better suited for having him file a final fee application and we take up whether he's entitled to the fees or not.

Doc. 671 at 10. After hearing comments and arguments, the Court said:

> I think the disclosure [of] compensation issue is largely taken care of from my perspective. I don't want to make a big summary decision here with the exception of whether [the Keeleys] are entitled to fees for pushing it along..... But I'm very comfortable saying that we're going to vacate the order to show cause. We're going to continue to have the disclosure of compensation issue before the court based largely on the need to resolve the fees.

Id. at 23–24. Consistent with these comments, the Court vacated the order to show cause and ordered Johnston to file a final fee application. Docs. 659 and 660.

On January 9, 2016, Johnston filed what was docketed as Reference Final Fee App at Docket No. 552 and Corresponding Order at Docket No. 580. Doc. 661. In that filing, Johnston references and incorporates his Application for Final Compensation and the Court's Memorandum and Order on Final Application for Compensation, in which the Court awarded Johnston $37,013.76 in compensation. Id. Johnston

purported to file this document to fulfil the Court's October 27, 2015 (Doc. 660) order that he submit an application for final compensation. All told, this indicated that Johnston would seek no additional compensation.

While this was pending in this Court, PHI was pursing Johnston and Choice in North Dakota state court for about $170,400 in SURE payments that G & K had received and sent to Johnston. PHI argued that the SURE payments were subject to its security interest and sought return of the $170,400 from Johnston as a fraudulent or avoidable transfer. The trial court found:

> [T]he $24,225.37 transferred to [Merlyn] Grabanski[ ] . . . was a fraudulent transfer and PHI was entitled to recover that amount from Johnston. The court also found the $150,000 payment was fraudulent, but found G & K received reasonably equivalent value for the transfer. The court allowed Johnston to retain $35,000 of the remaining funds, which the court found equaled the value of legal services provided to G & K, but voided the remaining $115,000. A judgment with interest totaling $167,203.24 was entered in favor of PHI.

PHI Fin. Servs., Inc. v. Johnston Law Office, P.C., 874 N.W.2d 910, 914, reh'g denied (Mar. 28, 2016).

The parties appealed. On January 26, 2016, the North Dakota Supreme Court reversed the trial court on the $20,424.37 transfer, finding that Johnston was not liable because he was "merely the conduit for the transfer" to Merlyn Grabankski. Id. at 917. The North Dakota Supreme Court also reversed on the issue of prejudgment interest on the $115,000 SURE payment. Id. at 921.

The North Dakota Supreme affirmed the trial court on the remaining issues, agreeing that $115,000 of the $150,000 SURE payment was subject to PHI's security interest but that Johnston could retain $35,000 for legal fees. Id. at 920. On remand, the North Dakota district court entered an amended judgment in favor of PHI against Johnston in the principle amount of $115,000, plus interest.

On February 27, 2017, this Court held a hearing on all matters not yet fully adjudicated. The notice for that hearing listed 17 docket entries related to the procedural history recounted above—including Johnston's disclosure of compensation, objections thereto, and Johnston's final fee application—as matters that the Court would consider and act on. Doc. 667. At their core, these filings raise issues about whether the Court should order Johnston to disgorge or turn over any additional money paid in fees to him, if so how much, and whether additional sanctions are warranted. The Court had previously told the Keeleys they would need to provide compelling arguments for the Court to consider disgorgement further. The Keeleys provided such arguments.

ARGUMENTS

The Keeleys argue that, based on Johnston's Final Disclosure, he received $262,301.50 (and possibly $563,801.50) in fees or compensation for his representation of Debtors in their bankruptcy and other matters. The Keeleys point to eight payments in Johnston's disclosure to show that he received $262,301.50:

- $15,000 on July 15, 2015 as an initial retainer
- $20,000 on November 9, 2010 from Texas Family Farms
- $20,000 on May 9, 2011 from Merlyn Grabanski
- $150,000 on October 14, 2011 from G & K Farms' SURE refund

- $20,400 on November 3, 2011 from G & K Farms' SURE refund
- $8,167.04 on April 15, 2011 from Debtors
- $5,384.46 on November 9, 2011 from Debtors
- $23,350 on July 19, 2013 from Debtors in the form of certain property

The Keeleys further point out that Johnston's IOLTA trust account statements filed as part of the disclosure contain two additional unredacted deposits: one for $1,500 and one for $300,000. Under the Court's previous orders, Johnston was to file redacted IOLTA trust account statements, but leave payments he received from other related entities in connection with Johnston's work in Debtors' bankruptcy unredacted. The Keeleys argue that, because Johnston left the $1,500 and $300,000 deposits unredacted, he concedes that these payments were for work in connection with the bankruptcy. The Keeleys conclude that if the $1,500 and $300,000 deposits are payments in connection with the bankruptcy, then Johnston has received a total of $563,801.50 in compensation.

This Court has already ruled that $37,013.76 is the limit of Johnston's allowable compensation. The Keeleys conclude that Johnston received $225,287.74 (and possibly $526,787.74) beyond that limit. The Keeleys ask the Court to order Johnston to disgorge or pay over this amount. The Keeleys also ask the Court for attorney's fees for pursuing this matter over several years.

Johnston does not dispute that he received the payments outlined above (he does not address the $1,500 and $300,000 deposits). Johnston primarily relies on legal arguments that the Court cannot order disgorgement or return of the payments he received as fees: that the Court does not have jurisdiction over the bankruptcy because it dismissed the bankruptcy, that the Keeleys do not have standing to seek disgorgement because they do not have a direct pecuniary interest, that res judicata bars disgorgement because this Court has already addressed his fees, and that res judicata and the Rooker–Feldman doctrine bar disgorgement of the SURE payments because they have already been addressed in the North Dakota State Court litigation. See PHI Fin. Servs., Inc. v. Johnston Law Office, P.C., 874 N.W.2d 910 reh'g denied (Mar. 28, 2016). Johnston concludes that the Court cannot order him to disgorge the fees as a matter of law.

Johnston argues that, even if the Court could legally order some disgorgement of fees, he has already effectively turned over or returned most of the funds the Keeleys now seek. Johnston returned $180,400 through settlements and as a result of the North Dakota Supreme Court ruling and judgment. He returned the $15,000 retainer payment through his settlement agreement with the United States Trustee. He returned the $30,000 in value he received from Debtors through his settlement with Trustee Weisbart in Debtors' subsequent Texas bankruptcy.

The Keeleys find no merit in Johnston's legal arguments. They argue that the Court still has ancillary jurisdiction over Johnston's fees, that they have standing because they continue to be creditors in the Debtors' Texas bankruptcy, and that res judicata and the Rooker–Feldman doctrine do not apply to this case because—although the North Dakota rulings may address the underlying funds—they did not address Johnston's entitlement to those funds under bankruptcy law.

The Keeleys only partially address Johnston's arguments about the amount of fees that the Court can or should order disgorged. They do not address the effect

of Johnston's' settlements with the United States Trustee and with Trustee Weisbart. They also do not address the North Dakota trial court's finding that Johnston transferred $20,424.37 from the $20,400 SURE payment to Merlyn Grabanski. They do admit, however, that the $115,000 North Dakota judgment in favor of PHI may reduce the proper disgorgement amount by $115,000.

CONCLUSIONS OF LAW AND ANALYSIS

I. Legal Bars to Disgorgement and Fee Award

Johnston argues that Court does not have the authority to order him to disgorge some or all of the fees. Johnston argues that the Court does not have jurisdiction to order disgorgement because the Court has dismissed the bankruptcy; that the Keeleys do not have standing to request disgorgement or fees; that res judicata bars disgorgement here; and that the Rooker–Feldman doctrine also bars disgorgement here. The Keeleys disagree on all points. The Court will address these arguments in turn.

A. Jurisdiction

[1] Johnston argues that the Court no longer has jurisdiction to order disgorgement of any fees. Johnston argues that the Court lost jurisdiction when it dismissed the bankruptcy. Johnston argues that, to have retained ancillary jurisdiction over his fees, the Court needed to say so in the dismissal order. For support, Johnston cites Iannini v. Winnecour, 487 B.R. 434, 439 (W.D. Pa. 2012) ("Courts may determine the propriety of compensation in an underlying bankruptcy case post-dismissal by explicitly retaining jurisdiction..... where the court does not explicitly retain such jurisdiction, the court thereafter presumptively lacks jurisdiction over the issue."). Johnston notes that the Keeleys initially sought disgorgement before the Court dismissed the bankruptcy and that the Court did not explicitly retain jurisdiction over the issue. Johnston concludes that the Court lost jurisdiction when it dismissed the case without expressly retaining jurisdiction.

The Keeleys disagree. They argue that the Court still has "ancillary jurisdiction" over the case, which includes jurisdiction over attorney's fees. The Keeleys cite In re Petrovic, 560 B.R. 312, 315 (Bankr. N.D. Ill. 2016) ("A bankruptcy court ... has ancillary jurisdiction to examine the fees of counsel for a debtor under section 329 post-dismissal.").

The Court has already addressed this issue in a previous ruling in this case and found that it continued to have post-dismissal jurisdiction over Johnston's fees:

> Despite the dismissal of a case, the Court continues to have jurisdiction over fee requests and compensation. In re Garris, 496 B.R. 343, 354 (Bankr. S.D.N.Y. 2013); In re Dixon, Bankr. No. 06-10988PM, 2007 WL 1073862, at *1 (Bankr. D. Md. Feb. 9, 2007); In re Hughes, Bankr. No. 05-00488, 2006 WL 3019556, at *1 (Bankr. D.C. Oct. 20, 2006); In re Fox, 140 B.R. 761, 762 (Bankr. D.S.D. 1992). "The Court has an independent duty to review and evaluate attorney compensation disclosure and requests, regardless of dismissal.["] In re Burroughs, Bankr. No. 12-81073-TRC, 2012 WL 5053054, at *3 (Bankr. E.D. Okla. Oct. 18, 2012). "The allowance of fees is a core matter under 28 U.S.C. § 1334(b).["] In re Garris, 496 B.R. at 354 (citing In re Brown, 371 B.R. 486, 494 (Bankr. N.D. Okla. 2007)). The Brown court held that "[t]he Court's jurisdiction to review such fees is not dependent on whether the status of the case stands as open, closed, pending, or

dismissed.' Id. (quoting In re Brown, 371 B.R. at 494) (alteration in original).

This jurisdiction includes considerations made by the Court pursuant to § 329. See In re Burroughs, 2012 WL 5053054, at *3; In re Dixon, 2007 WL 1073862, at *1; In re Hughes, 2006 WL 3019556, at *1; In re Henderson, 360 B.R. 477, 484 (Bankr. D.S.C. 2006). Section 329 requires attorneys to disclose compensation paid for services rendered in connection with a bankruptcy case. 11 U.S.C. § 329(a). There is no timing requirement provided in § 329 with regard to when the compensation is paid or when the services are rendered. Accordingly, payments made after dismissal for services rendered in connection with a bankruptcy case fall within the purview of § 329 and the Court's jurisdiction.

Doc. 608 at 23–24. The Court relied on this conclusion when it ordered Johnston to turn over his IOLTA trust account statements and billing records. Id. at 24. The length of time since dismissal is irrelevant. The Court thus rejects Johnston's argument that it no longer has jurisdiction to order disgorgement under § 329.

B. Standing

[2] Johnston next argues that the Keeleys, the only parties still pressing this issue, do not have standing to seek disgorgement. Johnston argues that, in order to have standing, the aggrieved party must demonstrate that it has a direct pecuniary interest in the outcome of the proceeding. Johnston argues that the Keeleys have made no such showing. Johnston concludes that the Keeleys do not have standing to seek disgorgement.

The Keeleys disagree and note that they were creditors in this bankruptcy and in the Grabanski's ongoing bankruptcy in Texas. The Keeleys argue that if the Johnston disgorged fees go to the Debtors' Texas bankruptcy estate, the Keeleys will receive a portion of any disbursement from the estate as creditors. The Keeleys argue that this shows that they have a pecuniary interest in disgorgement.

[3] Section 1109(b) provides:

A party in interest, including the debtor, the trustee, a creditors' committee, an equity security holders' committee, **a creditor**, and equity security holder, or any indenture trustee, **may raise and may appear and be heard on any issue in a case under this chapter**.

11 U.S.C. § 1109(b). This section "is to be construed broadly, in order to allow parties affected by a chapter 11 case to appear and be heard." In re Sandpoint Cattle Co., LLC, 556 B.R. 408, 417 (Bankr. D. Neb. 2016) (internal quotation marks omitted) (quoting In re Alpha Nat. Res. Inc., 544 B.R. 848, 854 (Bankr. E.D. Va. 2016)).

[4] The Court finds that the Keeleys were creditors in this bankruptcy and continue to be creditors in the Texas bankruptcy and thus have standing to seek disgorgement of Johnston's fees. They have set out a pecuniary interest in the funds—if the disgorged fees go to the Debtors' Texas bankruptcy estate, the Keeleys will be able to take part in any distribution as creditors. Moreover, even if they did not have standing, "the Court has an independent duty to review fee applications." Id. at 417 (finding that the Court could address whether disgorgement was proper even if the creditor did not have standing). Even if the Keeleys did not have standing, the Court may explore the issue sua sponte.

C. North Dakota Supreme Court Ruling on SURE Payments

Johnston argues that, at a minimum, the Court cannot order him to disgorge the compensation he received in the form of

the $20,400 and $150,000 SURE payments because the North Dakota Supreme Court has already addressed these payments. The North Dakota Supreme Court ruled that Johnston was a mere-conduit for the $20,400 SURE payment, which he simply transferred to Merlyn Grabanski, and that Johnston could retain $35,000 of the $150,000 SURE payment for his work representing G & K farms. PHI Fin. Servs., Inc. v. Johnston Law Office, P.C., 874 N.W.2d 910, 914, 917, 920–21 reh'g denied (Mar. 28, 2016). The Court awarded PHI Financial Services the remaining $115,000 of the SURE payment because of its security interest in the SURE payments. Id. at 922.

Johnston argues that the principles of res judicata and the Rooker–Feldman doctrine now preclude the Court from addressing the SURE payments. He asserts that the North Dakota Supreme Court has already fully addressed how the money should be treated. In particular, he argues that the Keeleys are attempting to void the North Dakota Supreme Court's ruling that he was entitled to retain $35,000 of the $150,000 SURE payment for his working representing G & K Farms.

The Keeleys disagree. The Keeleys do not dispute that the state court had jurisdiction over PHI's claims and entered a final judgment on those claims. The Keeleys argue, however, that the state court action did not involve the same cause of action or the same parties. The Keeleys note that they were not a party to the state court action and that the state court action did not address Johnston's entitlement to the funds under the Bankruptcy Code. Similarly, the Keeleys argues that the Rooker–Feldman doctrine does not apply because they were not parties to the state court action and are not attacking the state court judgment.

The Court will address these issues in turn—first res judicata, then the Rooker–Feldman doctrine.

i. Res Judicata

[5, 6] "Under the Full Faith and Credit Act, 28 U.S.C. § 1738, federal courts must give to a state-court judgment the same preclusive effect as would be given that judgment under the law of the State in which the judgment was rendered." Finstad v. Beresford Bancorporation, Inc., 831 F.3d 1009, 1013 (8th Cir. 2016) (internal quotation marks omitted) (quoting Migra v. Warren City Sch. Dist. Bd. of Educ., 465 U.S. 75, 81, 104 S.Ct. 892, 79 L.Ed.2d 56 (1984). "North Dakota long has defined res judicata as a 'doctrine that prohibits the relitigation of claims or issues that were raised or could have been raised in a prior action between the same parties or their privies and which was resolved by final judgment in a court of competent jurisdiction.' " In re Athens/Alpha Gas Corp., 715 F.3d 230, 235–36 (8th Cir. 2013) (quoting Hofsommer v. Hofsommer Excavating, Inc., 488 N.W.2d 380, 383 (N.D. 1992)).

[7, 8] The Supreme Court of North Dakota has adopted a four-element standard to determine whether res judicata applies:

> there must be (1) "[a] final decision on the merits in the first action by a court of competent jurisdiction," (2) "the same parties, or their privies," in the second action as in the first, (3) an issue in the second action that was "actually litigated" or that "should have been litigated in the first action," and (4) "[a]n identity of the causes of action."

Id. at 236 (quoting Missouri Breaks, LLC v. Burns, 791 N.W.2d 33 (N.D.2010)). "Privity exists if a person is so identified in interest with another that he represents the same legal right." Id. at 237 (quoting Simpson v. Chicago Pneumatic Tool Co., 693 N.W.2d 612, 616 (N.D. 2005)).

[9] Here, res judicata does not apply. The parties are not the same and the issues are not the same. The Keeleys did not participate in the previous litigation nor are they in privity with PHI. Although Johnston alleges that the Keeleys and PHI are in privity, there is nothing in the record to support that allegation. PHI and the Keeleys do not "represent the same legal right"—PHI pursued the SURE payments in the North Dakota litigation based on its security interest, while the Keeleys are pursing disgorgement of fees as creditors in Debtors' bankruptcy.

Moreover, the issue Johnston seeks to preclude here is not the same as the issue in the North Dakota litigation. The North Dakota Supreme Court ruling addressed the payments as fraudulent or voidable transfers. PHI Fin. Servs., Inc., 874 N.W.2d 910 passim. Whether the transfers to Johnston were avoidable or fraudulent is not the same issue as whether he received compensation beyond what the Court approved as reasonable for his work in connection with the bankruptcy. The North Dakota Supreme Court did not address Johnston's entitlement to fees as Debtors' counsel. Only this Court has jurisdiction to decide the proper amount of Johnston's compensation for his work under 11 U.S.C. § 329 and whether he has exceeded the allowable amounts such that he must disgorge fees.

The North Dakota Supreme Court's ruling on whether PHI was entitled to return of the SURE payments under North Dakota fraudulent transfer law does not bar this Court from considering disgorgement of unreasonable compensation under 11 U.S.C. § 329 under the doctrine of res judicata.[4]

ii. Rooker–Feldman

[10–12] "As established by the Rooker–Feldman doctrine, federal district courts do not possess subject matter jurisdiction over challenges to state court decisions." Christ's Household of Faith v. Ramsey Cty., 618 F.Supp.2d 1040, 1043 (D. Minn. 2009). "The basic theory of the Rooker–Feldman doctrine is that only the United States Supreme Court has been given jurisdiction to review a state-court decision, so federal district courts generally lack subject-matter jurisdiction over attempted appeals from a state-court judgment." Friends of Lake View Sch. Dist. Incorporation No. 25 of Phillips Cty. v. Beebe, 578 F.3d 753, 758 (8th Cir. 2009) (internal quotation marks omitted). The Supreme Court said:

> The Rooker–Feldman doctrine ... is confined to cases of the kind from which the doctrine acquired its name: cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments. Rooker–Feldman does not otherwise override or supplant preclusion doctrine or augment the circumscribed doctrines that allow federal courts to stay or dismiss proceedings in deference to state-court actions.

Exxon Mobil Corp. v. Saudi Basic Indus. Corp., 544 U.S. 280, 284, 125 S.Ct. 1517, 161 L.Ed.2d 454 (2005).

[13] "[A]fter Exxon Mobil there are four requirements for the application of the Rooker–Feldman doctrine: (1) the federal court plaintiff must have lost in state court, (2) the plaintiff must complain of

4. Although the North Dakota Supreme Court's ruling does not legally bar this Court from addressing Johnston's compensation from the SURE payments, the rulings do affect, as a practical matter, the amount of money that Johnston now retains as a part of his compensation for work in connection with the case. See Part III.

injuries caused by a state court judgment, (3) the plaintiff must invite district court review and rejection of that judgment, and (4) the state court judgment must have been rendered before the district court proceedings commenced." Christ's Household of Faith, 618 F.Supp.2d at 1044 (citing Skit Intern., Ltd. v. DAC Techs. of Arkansas, Inc., 487 F.3d 1154, 1156–57 (8th Cir. 2007)).

[14] Here, the Keeleys were not a part of the North Dakota state litigation. They claim no injury from the North Dakota Supreme Court's ruling. The Keeleys are not asking the Court to review or reverse the North Dakota Supreme Court's ruling. That ruling addressed whether G & K's transfer of SURE payments to Johnston were fraudulent transfers—not proper bankruptcy compensation. Finally, these bankruptcy fee proceedings commenced long before the state court proceedings. The Rooker–Feldman doctrine does not apply here. This Court has jurisdiction to order Johnston to disgorge compensation under § 329.

II. Disgorgement/Return of Payments

Bankruptcy Code § 329 provides:

(b) **Any attorney representing a debtor** in a case under this title, or in connection with such a case, whether or not such attorney applies for compensation under this title, **shall file with the court a statement of the compensation paid** or agreed to be paid, if such payment or agreement was made after one year before the date of the filing of the petition, **for services rendered** or to be rendered in contemplation of or **in connection with the case** by such attorney, **and the source of such compensation**.

(c) **If such compensation exceeds the reasonable value of any such services**, **the court may** cancel any such agreement, or **order the return of any such payment, to the extent excessive, to—**

(1) **the estate**, if the property transferred—

(A) would have been property of the estate; or

(B) was to be paid by or on behalf of the debtor under a plan under chapter 11, 12, or 13 of this title; **or**

(2) **the entity that made such payment**.

11 U.S.C. § 329. The Eighth Circuit Bankruptcy Appellate Panel has said:

> The test under § 329 measures reasonable value of the services provided by the attorney. To the extent that the fees due or paid are not reasonable in light of the services provided, the court may cancel the fee agreement or order disgorgement. The court, having determined fees to be unreasonable, may order the fees returned to the estate if the source of the paid fees would have been property of the estate and only to the extent that the fees are excessive.

Schroeder v. Rouse (In re Redding), 247 B.R. 474, 478 (8th Cir. BAP 2000).

Here, Johnston's disclosures reveal that he has received $262,301.50 (and potentially $563,801.50) in compensation from entities wholly-owned by or closely related to Debtors. Johnston has argued throughout these proceedings, however, that most of this compensation was paid for work that was not "in connection with the case" and thus did not need to be disclosed. Johnston has asserted that these large fee payments were for non-bankruptcy work for separate entities that the Debtors owned.

[15, 16] The Court has already rejected this argument and found that he must disclose fees for work done for Debtors' wholly-owned entities as compensation "for services rendered ... in connection with the case." Doc. 608 at 20–21. "The phrase 'in connection with' has been broadly interpreted to include any services that affect the bankruptcy estate." Charity v. NC Fin. Sols. Of Utah, LLC (In re Charity), Bankr. No. 16–31974–KLP, Adv. No. 16–03121, 2017 WL 3580173, at *24 (Bankr. E.D. Va. Aug. 15, 2017) (collecting cases). A recent case has laid out how the "in connection with" standard applies:

> To determine whether services are "in connection with" the bankruptcy case, courts apply an objective standard: "[I]f it can be objectively determined that the services rendered or to be rendered by the attorney have or will have an impact on the bankruptcy case," then such services ... have been rendered in connection with the bankruptcy case.
>
> Attorney Durell argues most of the fees he received were categorically not for services "in connection with" a bankruptcy case, because the services he rendered would have occurred regardless of the Debtors' bankruptcy filing. This argument underestimates the broad application of the phrase "in connection with" and understates the extent to which the legal services he rendered, during the pendency of the bankruptcy case, were intertwined with the interests of the bankruptcy estate. All services Attorney Durell rendered after May 20, 2015 were in connection with the bankruptcy case since he was representing the Debtors while their bankruptcy case was pending. Furthermore, based on the record, it is indisputable that the so-called non-bankruptcy legal services were for litigation that was crucial to the Debtors' attempts to reorganize under Chapter 13 and cannot be disentangled from the bankruptcy legal work. Based on these considerations, the relevant case law, the extensive reach of the phrase "in connection with," and Attorney Durell's failure to establish facts to the contrary, the Court finds all fees paid to Attorney Durell from May 20th forward were for services rendered in connection with the bankruptcy case.

In re Frye, 570 B.R. 21, 29 (Bankr. D. Vt. 2017) (citations omitted). The same court also concluded that the source of the payments does not change the analysis:

> Attorney Durell argues fees paid by third parties are not subject to disclosure requirements. However, the language of § 329(a) provides otherwise. It requires a debtor's attorney to disclose the source of payments received, regardless of what that source is: An attorney representing a debtor ... shall file with the court a statement of the compensation paid or agreed to be paid ... for services rendered or to be rendered in contemplation of or in connection with the case by such attorney, **and the source of such compensation**. The bankruptcy court may order the disgorgement of any payment made to an attorney representing the debtor in connection with a bankruptcy proceeding, irrespective of the payment's source.

Id. at 30–31 (citations omitted) (quotation marks omitted) (emphasis in original).

[17] This reasoning applies here and the Court (again) rejects Johnston's arguments that the disputed payments were not for work done "in connection with the case." Over the many years and multiple proceedings in the bankruptcy, Johnston has provided no satisfactory explanation how and why his work for these "separate entities"—companies wholly-owned by Debtors—was not "in connection with" the case. Johnston has never made any show-

ing to meet these standards or made any persuasive argument—despite having multiple opportunities to do so—that the money he received over and above the $37,013.76 was not "for services rendered . . . in connection with" the case. In fact, the record shows that the compensation at issue was most likely for work "in connection with the case." Like counsel in Frye, Johnston "understates the extent to which the legal services he rendered, during the pendency of the bankruptcy case, were intertwined with the interests of the bankruptcy estate." Id. at 29. The Court gives this argument no further consideration.

Under the clear terms of § 329, "If such compensation exceeds the reasonable value of any such services, the court may . . . order the return of any such payment . . . ." Thus, "To the extent that the fees due or paid are not reasonable in light of the services provided, the court may cancel the fee agreement or order disgorgement." In re Redding, 247 B.R. at 478.

Here, Johnston received compensation in connection with the bankruptcy that exceeds the reasonable value of his services. The Court has already determined that the reasonable value of Johnstons' services was $37,013.76. In re Grabanski, 2013 WL 1702416, at *9 ("His compensation for Debtors' case is limited to $34,013.76 that the Court previously awarded . . ., with the additional $3,000 awarded here, for a total of 37,013.76."). Johnston's disclosures reveal that he has received $262,301.50 (and potentially $563,801.50) in compensation for work done "in connection with" this case. Thus, Johnston's compensation for work done "in connection with the case" exceeds the reasonable value of his work by at least $225,287.74.

[18, 19] Moreover, "It is well settled that disgorgement of fees is an appropriate sanction for failure to comply with the disclosure requirements of section 329 and Rule 2016." In re Sandpoint Cattle Co., LLC, 556 B.R. 408, 426 & n.10 (Bankr. D. Neb. 2016) (The Honorable Shon Hasting, Chief United States Bankruptcy Judge for the District of North Dakota, sitting by designation) (collecting cases). "Filing incomplete or inaccurate disclosures also may be grounds for sanctions, including disgorgement." Id. at 427. "The decision to reduce fees, deny fees or order disgorgement of fees under section 329 is within the sound discretion of the bankruptcy court." Id. at 426. "Many courts, perhaps the majority, punish defective disclosure by denying all compensation." In re Kowalski, 402 B.R. 843, 848 (Bankr. N.D. Ill. 2009).

[20] When an attorney violates the Bankruptcy Code and Rules in the Eighth Circuit, however, Chief Judge Hastings has concluded that the Court **must** order the attorney to disgorge excessive fees:

> Although bankruptcy courts may exercise discretion to award or deny fees for failure to disclose, they should deny them when an attorney fails to comply with the Bankruptcy Code and rules. The Eighth Circuit Court of Appeals has held that, where a debtor's attorney has failed to comply with the statute and the rules, subsequent fee applications **should** be denied and the funds received **should** be ordered returned to the estate. It is worthy of note that the Eighth Circuit used the word should and not the word may, thereby giving a strong indication that disgorgement of the fees received is the expected and proper remedy to be applied.

In re Sandpoint Cattle Co., LLC, 556 B.R. at 427 (internal quotation marks omitted) (quoting In re Redding, 251 B.R. 547, 552–53 (Bankr. W. D. Mo. 2000)).

[21] Here, the Court has already found that Johnston's disclosures were "inadequate and do not meet the requirements of the Bankruptcy Code." In re Grabanski, 2013 WL 1702416 at *4. The Court repeats those findings here. Johnston did not follow the Bankruptcy Code's disclosure requirements. He repeatedly failed to disclose completely and accurately his fees in connection with the case. He disclosed fees only after the Court specifically ordered him to do so. And even after the Court expressly ordered him to disclose as the Code required, his disclosures were incomplete, inaccurate, and confusing.

Under § 329 and Eighth Circuit caselaw, the Court must order Johnston to disgorge fee payments he received that exceed the reasonable value of his work.

III. Disgorgement Amount

[22] Johnston argues that, even if disgorgement is appropriate, $225,287.74 is not the proper amount. Johnston argues that his two settlements related to fees and the North Dakota Supreme Court judgment already effectively returned some of the disputed payments or show that he no longer possesses the disputed payments.

As stated in Section I, Johnston's disclosures reveal that he received $262,301.50 (and potentially $563,801.50) in compensation related to this case. In particular, he received the following payments for services rendered in connection with the case:

- $15,000.00 on July 15, 2015 as an initial retainer
- $20,000 on November 9, 2010 from Texas Family Farms
- $20,000 on May 9, 2011 from Merlyn Grabanski
- $150,000 on October 14, 2011 from G & K Farms' SURE refund
- $20,400 on November 3, 2011 from G & K Farms' SURE refund
- $8,167.04 on April 15, 2011 from Debtors
- $5,384.46 on November 9, 2011 from Debtors
- $23,350 on July 19, 2013 from Debtors in the form of certain property

Johnston argues that the following payments, however, can no longer be considered part of his compensation in this case:

- $15,000 returned as a part of his settlement with the United States Trustee. Doc. 649.
- $20,400 SURE payment from G & K Farms, which the North Dakota state Court litigation determined that he sent to Merlyn Grabanski. PHI Fin. Servs., Inc., 874 N.W.2d 910 at 914 ("Johnston transferred $24,225.37 from the Trust account to Merlyn Grabanski . . . .").
- $115,000 of the SURE payment from G & K farms, which the North Dakota Supreme Court determined was property of PHI, and entered judgment accordingly. Id. at 921. There is nothing in the record to indicate if he has paid this judgment.
- $30,000 returned as a part of his settlement with the Chapter 7 Trustee in the Grabanski's bankruptcy in the Eastern District of Texas. In re Grabanski, Bankr. No. 13–41818, Docs. 173 and 177.

Johnston argues that these funds, which total $180,400, can no longer be included in the amounts that he received as compensation related to the bankruptcy.

The Keeleys do not address these arguments. They note only that the Court may reduce the disgorgement order by $115,000 given the North Dakota Supreme Court's ruling.

> It is well settled that a bankruptcy court may deny an attorney all compensation based upon the failure to satisfy § 329(a) and Rule 2016(b). Full disgorgement of fees is not automatic, and the bankruptcy court has the latitude to tailor a sanction that is appropriate under the unique circumstances of the case. In determining the appropriate type and amount of sanction, the court exercises its discretion and examines the particular facts of the case, including whether any unusual difficulties existed. Additionally, the sanction should be carefully tailored to be sufficient to punish the misconduct but no more than is reasonably necessary to deter the culpable conduct.

In re Frye, 570 B.R. at 31–32 (citations omitted) (internal quotation marks omitted) (alteration omitted).

Based on the record, the Court will reduce the amount that Johnston must disgorge by $180,400. Johnston was originally paid at least $262,301.50 by Debtors and entities related to Debtors. Through Johnston's' settlements, he has sent a total of $45,000 to the Grabanski's bankruptcy estate in their Texas bankruptcy. The North Dakota ruling found that he no longer has the $20,400 SURE payment because he sent it to Merlyn Grabanski. The North Dakota ruling also found $115,000 SURE payment was subject to PHI security interest—as a result, Johnston now has paid or must pay that money to PHI.

Thus, Johnston currently has $81,901.50 in compensation remaining from his work in connection with this bankruptcy. After subtracting the $37,013.76 in compensation the Court approved as reasonable, he has still been overpaid—in amounts never properly explained—by at least $44,887.74. The Court thus orders Johnston to disgorge $44,887.74 and pay it to the Debtors' new bankruptcy estate.

The Keeleys have also identified two additional payments totaling $301,500 reflected on Johnston's IOLTA account statement that need to be addressed. These two payments are not redacted, and the Keeleys argue this indicates these payments may in fact be connected to Johnston's work in this case. The Court concludes that, if these payments were for work done in connection with the case, Johnston must also disgorge that money and pay it over to the Debtors' new bankruptcy estate. The Court will give Johnston the opportunity to explain the $301,000. Given Johnston's history of misleading and incomplete disclosures, the Court orders Johnston to file, within 30 days of this ruling, evidence showing the source of the $300,000 and $1,500 payments. Johnston must also report whether those payments were made in connection with the case as discussed above.

IV. Sanctions

[23–25] "Courts have an 'inherent power ... to levy sanctions in response to abusive litigation practices.' " Crooked Creek Corp. v. Primebank (In re Crooked Creek Corp.), 533 B.R. 274, 281 (Bankr. N.D. Iowa 2015) (quoting Roadway Exp., Inc. v. Piper, 447 U.S. 752, 765, 100 S.Ct. 2455, 65 L.Ed.2d 488 (1980)). "A court's inherent power to sanction is very powerful, and therefore must be used with restraint and discretion." Id. (citing Chambers v. NASCO, Inc., 501 U.S. 32, 44, 111 S.Ct. 2123, 115 L.Ed.2d 27 (1991)). "A primary aspect of that discretion is the ability to fashion an appropriate sanction for conduct which abuses the judicial process." Id. (internal quotation marks omitted) (quoting Chambers, 501 U.S. at 44, 111 S.Ct. 2123).

[26] The extensive history of the litigation on these issues case reflects Johnston's abusive litigation practices: delay, misrepresentation, and continued reliance

on arguments that the Court has already rejected. These practices—beyond the excessive fees and failure to disclose—resulted in prolonged litigation and increased cost. This cost was born primarily by the Keeleys. As the Court noted on the record in a prior hearing, when the United States Trustee is satisfied on a fee issue that is usually strong indication that no meritorious issues remain. It turns out that was not the case here.[5] Without the work of Keeleys' counsel pursuing this matter, it is quite possible that Johnston would retain the disputed fees. The Court finds that an appropriate sanction for Johnston's abusive litigation practices in this case is the amount of the Keeleys' reasonable attorney's fees for their work pursuing disgorgement.

CONCLUSION

WHEREFORE, the Court orders Johnston to disgorge $44,887.74 in fees to the Chapter 7 Trustee in the Grabanski's bankruptcy in the Eastern District of Texas—Bankruptcy No. 13–41818.

FURTHER, the Court orders Johnston to file a disclosure showing the source of the unreacted $300,000 payment and $1,500 payments on this IOLTA trust account within 30 days of this ruling.

FURTHER, the Court sanctions Johnston in the amount of the Keeleys' reasonable attorney's fees for their work pursing disgorgement. The Keeleys' have 21 days to file a formal fee application for fees and expenses incurred in the pursuit of disgorgement.

5. In reviewing the voluminous record in this case, the Court is reminded that the United States Trustee took an inexplicably passive approach to fees—participating only when ordered by the Court.

Section 522). *See, e.g.*, *In re Conklin*, Case 17-16247 MER, ECF No. 43 at *5, n. 27; *In re Eubanks*, 581 B.R. 583, 589-90 (Bankr. S.D. Ill. 2018) (court could not use Section 105(a) equitable powers to add similar conditional language to 100% Chapter 13 payment plan that was otherwise confirmable under Section 1325, even though the debtors were not committing all of their projected disposable income; proposed language added requirements for confirmation not otherwise found in Sections 1325(a) or (b)); *Martinez v. Viegelahn (In re Martinez)*, 581 B.R. 486, 497 (W.D. Tex. 2017) (similar conditional language contravened the debtors' express rights under Section 1329(a) to modify their Chapter 13 plan).

As noted by Judge Romero in *Conklin*, Trustee is not wholly without recourse in this situation; the good faith requirement of Section 1325(a)(3) is incorporated into any post-confirmation modification analysis pursuant to Section 1329(b)(1). *In re Conklin*, Case 17-16247 MER, ECF No. 43 at *6. "If, in the future, the undesirable scenario identified by the Trustee ... comes to pass, the Court may deny modification upon finding the result would significantly reduce the distribution to creditors, especially if the modification is based on circumstances which could have been reasonably foreseen prior to confirmation." *Id.*

With respect to Trustee's suggestion of requiring concurrent distribution to general unsecured creditors, Section 1322(b)(4) permits – but does *not* require – concurrent distribution. Without reaching the issue of whether Section 1325(b)(1)(B) contemplates concurrent distribution to unsecured creditors as Trustee contends, compliance with Section 1325(b)(1)(B) is not required because the Plan complies with the alternative under Section 1325(b)(1)(A).

Only a debtor may propose a Chapter 13 plan. 11 U.S.C. § 1321. Section 1325(a) mandates the Court "shall confirm a plan" if it meets the requirements stated therein. 11 U.S.C. § 1325(a). The Court finds the Plan meets the requirements of Section 1325(a) and was proposed in good faith as required by Section 1325(a)(3). In addition, the Plan complies with Section 1325(b)(1)(A). The Court will not impose additional provisions or conditions upon the Plan that are not required under the Bankruptcy Code under the circumstances of this case.

Accordingly, it is

HEREBY ORDERED that the Chapter 13 Trustee's Objection to the Plan is OVERRULED; and it is

FURTHER ORDERED Debtors shall file a Verification of Confirmable Plan with in fourteen (14) days.

IN RE: Leroy Sylvester CARR, Debtor.

Case No.: 8:13-bk-11921-CPM

United States Bankruptcy Court,
M.D. Florida,
Tampa Division.

Signed October 12, 2018

Filed 10/16/2018

Background: After attorney was suspended by the Florida Supreme Court, United States Trustee (UST) filed expedited motion seeking the suspension of attorney and his law firm from the practice of law in the United States Bankruptcy Court for the Middle District of Florida.

Holdings: The Bankruptcy Court, Catherine Peek McEwen, J., held that:

(1) it was appropriate to indefinitely suspend attorney from the practice of law in the district, and

(2) attorney's law firm would be prohibited from providing any further bankruptcy assistance services or acting as a debt relief agency.

Ordered accordingly.

1. Bankruptcy ⟹3030

When adopted, local bankruptcy rules constitute a material requirement of title 11 or the Federal Rules of Bankruptcy Procedure, for purposes of the section of the Bankruptcy Code governing restrictions on debt relief agencies. 11 U.S.C.A. § 526(c)(2)(C); 28 U.S.C.A. § 2075.

2. Attorney and Client ⟹59.13(7), 60

Following attorney's suspension by the Florida Supreme Court, it was appropriate to indefinitely suspend attorney from the practice of law in the United States Bankruptcy Court for the Middle District of Florida; after his suspension, attorney became ineligible to practice in the bankruptcy court, attorney failed to notify his bankruptcy clients, opposing counsel, trustees, or the bankruptcy court that he was ineligible to practice law in Florida, and attorney failed to attend a mortgage mediation in a pending Chapter 13 case and to notify any party to that mediation of his suspension. U.S.Dist.Ct. Rules M.D.Fla., Rule 2.01; U.S.Bankr.Ct. Rules M.D.Fla., Rules 2090-1(a), 2090-1(e), 2090-2(b).

3. Attorney and Client ⟹60

Attorney's suspension from The Florida Bar was grounds alone to suspend him from appearing before the bankruptcy court. U.S.Dist.Ct.Rules M.D.Fla., Rule 2.01; U.S.Bankr.Ct.Rules M.D.Fla., Rules 2090-1(a).

4. Bankruptcy ⟹3030

Following attorney's suspension by the Florida Supreme Court, attorney's law firm would be prohibited from providing any further bankruptcy assistance services or acting as a debt relief agency; with the indefinite suspension of attorney to provide legal services to his clients in bankruptcy, his law firm, a debt relief agency, failed to comply with the restrictions and material requirements set forth in the section of the Bankruptcy Code governing debt relief agencies, such that the contracts for bankruptcy assistance services in 14 pending cases were void and unenforceable by firm, and it would have constituted unjust enrichment for firm to retain funds paid to it by assisted persons or, alternatively, firm's negligent or intentional failure to comply with the Code rendered it liable for a refund of all fees, costs, and expenses, and actual damages. 11 U.S.C.A. §§ 526(a)(1), 526(a)(3), 526(c)(1), 526(c)(2)(A), 526(c)(2)(C).

5. Bankruptcy ⟹2402(1)

Although law firm of attorney who had been suspended by the Florida Supreme Court filed for Chapter 7 relief six days after the hearing leading to the order indefinitely suspending attorney from the practice of law in the United States Bankruptcy Court for the Middle District of Florida, the bankruptcy court's entry of the suspension order did not violate the automatic stay in the firm's case based on the "government regulatory exception" to the stay. 11 U.S.C.A. § 362(a)(4).

6. Bankruptcy ⟹2124.1

Bankruptcy court may wield its inherent power over the lawyers who practice before it.

Kevin E. Paul, Stopa Law Firm, Tampa, FL, for Debtor.

Kimberly McIntyre, Bradenton, FL, for Trustee.

ORDER INDEFINITELY SUSPENDING ATTORNEY MARK PHILIP STOPA AND PROHIBITING THE DEBT RELIEF AGENCY F/K/A STOPA LAW FIRM, P.A., N/K/A STAY IN MY HOME, P.A. FROM PROVIDING ANY BANKRUPTCY ASSISTANCE SERVICES OR ACTING AS A DEBT RELIEF AGENCY

Catherine Peek McEwen, United States Bankruptcy Judge

THIS CASE came on for hearing on September 26, 2018, at 3:30 p.m., on the United States Trustee's Expedited Motion Seeking Relief Relating to the Florida Supreme Court's Suspension of Attorney Mark Philip Stopa, and Seeking Additional Relief.[1] In the motion, the U.S. Trustee alleges that Stopa and his law firm should be immediately suspended because Stopa became ineligible to practice law in the State of Florida; [2] stopped providing bankruptcy assistance services to his chapter 13 clients; failed to notify this Court, the trustees, opposing parties, or his bankruptcy clients that he was ineligible to practice; and has subsequently filed a petition for disciplinary revocation with the Florida Supreme Court.[3] For the reasons set forth below, this Court concludes that it is appropriate to indefinitely suspend Stopa and his law firm, Stopa Law Firm, P.A., n/k/a Stay In My Home, P.A., from the practice of law in the United States Bankruptcy Court for the Middle District of Florida.

As background, Stopa was admitted to The Florida Bar on April 23, 2002.[4] Afterwards, Stopa was admitted to the United States District Court for the Middle District of Florida and admitted to practice before this Court. Since being admitted to this Court, Stopa has appeared in 104 bankruptcy cases and one adversary proceeding. Of those cases, as of the date of the hearing, 14 were pending,[5] with two chapter 13 cases still unconfirmed.[6] This Suspension Order will address only the 12 pending chapter 13 cases. This is because the agreed upon services associated in the chapter 7 case would generally have been completed upon the entry of the debtors' discharge, and the foreclosure defense services Stopa provided the debtor-in-possession in the chapter 11 case are best addressed in that specific case under 11 U.S.C. §§ 327-331.

In the 12 pending chapter 13 cases, the debtors constitute assisted persons,[7] and Stopa's law firm constitutes a debt relief agency.[8] In July 2018, while 16 of his bankruptcy cases were still open, the Florida

1. Doc. No. 133.

2. *The Florida Bar v. Stopa*, SC18-1197; *see also The Florida Bar v. Stopa*, SC17-1428; and *The Florida Bar v. Stopa*, SC 16-1727.

3. *In re Petition for Disciplinary Revocation*, SC18-1332.

4. https://www.floridabar.org/directories/find-mbr/?barNum=& fName=mark & 1Name=stopa

5. *See In re Mastromarino*, 8:17-bk-03841-MGW; *In re Martin*, 8:17-bk-02892-RCT; *In re Areias*, 8:17-bk-01142-CPM; *In re Wagner*, 8:17-bk-00312-CPM; *In re Falkner*, 8:16-bk-04019-CPM; *In re Perez*, 8:14-bk-08620-CPM; *In re Carr*, 8:13-bk-11921-CPM; *In re Phillos*, 8:13-bk-09519-RCT; *In re Gacon*, 9:13-bk-15297-FMD; *In re Elgamil*, 6:17-bk-03374-CCJ; *In re White*, 6:15-bk-09973-KSJ; *In re Eckert*, 6:14-bk-13539-ABB; *In re Hart*, 6:14-bk-11737-CCJ; *In re Neel*, 6:13-bk-15600-CCJ.

6. *In re Martin*, 8:17-bk-02892-RCT; *In re Areias*, 8:17-bk-01142-CPM.

7. 11 U.S.C. § 101(3).

8. 11 U.S.C. § 101(12A).

Supreme Court, acting on an emergency petition for suspension filed by The Florida State Bar, entered an emergency order suspending Stopa from the practice of law.[9] Further, Stopa failed to attend a mortgage mediation in a pending chapter 13 case and failed to notify any party to that mediation of his suspension.[10]

[1–3] Because he was suspended from the practice of law in Florida, Stopa became ineligible to practice in this Court. Bankruptcy Local Rule 2090-1(a)[11] requires that "an attorney who wishes to appear or be heard as counsel for another . . . must first be admitted to practice in the United States District Court for the Middle District of Florida pursuant to Rule 2.01." District Court Local Rule 2.01, in turn, requires attorneys admitted to practice in the Middle District of Florida to be members of good standing with The Florida Bar. Upon being suspended, Stopa is required to notify the Clerk of this Court of such disciplinary action.[12] Likewise, the Florida Supreme Court ordered Stopa to provide notice of his suspension to all of his clients, opposing counsel, and courts.[13] But Stopa failed to notify his bankruptcy clients, opposing counsel, trustees, or this Court that he was ineligible to practice law in Florida. Stopa's suspension from The Florida Bar is grounds alone to suspend Stopa from appearing before this Court.[14]

[4] The U.S. Trustee is seeking additional relief from the debt relief agency, Stopa Law Firm, P.A., n/k/a Stay In My Home, P.A. With the suspension of Stopa to provide legal services to his clients in bankruptcy, the debt relief agency, Stopa Law Firm, P.A., n/k/a Stay In My Home, P.A., has failed to comply with the restrictions and material requirements codified at 11 U.S.C. §§ 526(a)(1) and 526(a)(3). Due to that, the contracts for bankruptcy assistance services are void and unenforceable by anyone other than the client-assisted person.[15] As the contracts are void and unenforceable by the debt relief agency, it would constitute unjust enrichment were the debt relief agency to retain funds paid to it by the assisted person. Alternatively, because the debt relief agency negligently or intentionally failed to comply with §§ 526(a)(1) or 526(a)(3) with respect to a bankruptcy case, the debt relief agency would be liable for the refund of all fees, costs, expenses, and actual damages.[16] And finally, these 14 pending bankruptcy cases demonstrate a clear and consistent pattern

9. *See* fn. 2.

10. Mediator's Report, (Doc. No. 39, *In re Areias*, 8:17-bk-01142-CPM).

11. This Court promulgates its Bankruptcy Local Rules in accordance with Federal Rule of Bankruptcy Procedure 9029. And, when adopted, the Bankruptcy Local Rules constitute "a material requirement of [title 11] or the Federal Rules of Bankruptcy Procedure." *See* 11 U.S.C. § 526(c)(2)(C), *see also* 28 U.S.C. § 2075.

12. Bankr. L.R. 2090-1(e) and 2090-2(b).

13. Emer. Order Suspension, para. b, *The Florida Bar v. Stopa*, SC18-1197, 2018 WL 3617619 (Fla., Jul.27, 2018).

14. On September 14, 2018, the Clerk of this Court entered paperless entries in the PACER dockets for the pending cases associated to Stopa, terminating Attorney Stopa as a result of the suspension by the Florida Supreme Court.

15. 11 U.S.C. § 526(c)(1).

16. 11 U.S.C. § 526(c)(2)(A); see also 11 U.S.C. § 526(c)(2)(C) (liability for a debt relief agency who "intentionally or negligently disregarded a material requirement of this title or the Federal Rules of Bankruptcy Procedure applicable to such agency").

or practice of violating § 526.[17]

Upon a review of this Court's records as a whole, this Court is satisfied that the U.S. Trustee has met his burden of proof and persuasion and is satisfied that an order suspending Stopa and prohibiting the debt relief agency from providing any further bankruptcy assistance services or acting as a debt relief agency. Accordingly, it is

ORDERED:

1. The United States Trustee's Expedited Motion Seeking Relief Relating to the Florida Supreme Court's Suspension of Attorney Mark Philip Stopa, and Seeking Additional Relief, (Doc. No. 133), is **GRANTED** as follows:

2. Under Bankruptcy Local Rule 2090-2, the admission of Attorney Mark Philip Stopa, Fla. Bar No. 550507, to appear or be heard as counsel for another in any case or proceeding in this Court is **INDEFINITELY SUSPENDED.** As Attorney Stopa has been ineligible to practice law in the State of Florida since August 26, 2018, this **SUSPENSION** is effective immediately upon the entry of this Order.

3. Attorney Stopa and Stopa Law Firm, P.A., n/k/a Stay In My Home, P.A., shall not:

a. Accept any new bankruptcy clients;

b. Appear or be heard as counsel for another in any case or proceeding in this Court;

c. Act as a personal representative in any bankruptcy matter or in connection with any bankruptcy case or proceeding for any estate, a guardian, trustee, or counsel to any fiduciary for any estate, guardian, or trustee;

d. Counsel, represent, or provide any other means of assistance or representation of any person in any potential matter governed under the jurisdiction of the Bankruptcy Code and Rules;

e. Prepare, draft, ghost-write, assist in the preparation or drafting, or file any papers, pleadings, or petitions to be used or filed in any bankruptcy court, except for any filings made by and for Mark Philip Stopa acting *in propria persona*;

f. Engage in any conduct constituting bankruptcy assistance as defined under the Bankruptcy Code and Rules, without regard to whether any compensation, payment, or other valuable consideration has been or will be agreed upon, waived, paid, or otherwise; and

g. Act or engage in any conduct as a bankruptcy petition preparer or debt relief agency as governed under 11 U.S.C. §§ 110 or 526-28.

4. Attorney Stopa and the law firm, Stopa Law Firm, P.A., n/k/a Stay In My Home, P.A., is **DISQUALIFIED** from his representation of any Debtor; any and all bankruptcy assistance services contracts between Attorney Stopa, the law firm; and the Debtor-clients are **VOID**, and any fees for services are **FINALLY DISAPPROVED** in the bankruptcy cases: *In re Mastromarino*, 8:17-bk-03841-MGW; *In re Martin*, 8:17-bk-02892-RCT; *In re Areias*, 8:17-bk-01142-CPM; *In re Wagner*, 8:17-bk-00312-CPM; *In re Carr*, 8:13-bk-11921-CPM; *In re Phillos*, 8:13-bk-09519-RCT; *In re Gacon*, 9:13-bk-15297-FMD; *In re Elgamil*, 6:17-bk-03374-CCJ; *In re White*, 6:15-bk-09973-KSJ; *In re Eckert*, 6:14-bk-13539-ABB; *In re Hart*, 6:14-bk-11737-CCJ; *In re Neel*, 6:13-bk-15600-CCJ.

5. Attorney Stopa shall provide a copy of this Suspension Order to all of his bank-

17. 11 U.S.C. § 526(c)(5).

ruptcy clients, assisted persons, or prospective assisted persons that had pending bankruptcy files at any time on or after July 27, 2018. Within 30 days of the entry of this Suspension Order, Attorney Stopa shall provide proof of service of a copy of this Order upon his clients to the Clerk of this Bankruptcy Court, the United States Trustee, and The Florida Bar.

6. Attorney Stopa shall cooperate with any duly appointed Inventory Attorney or successor attorney in the proper protection of the Debtor-client(s)' rights and interest in the pending bankruptcy cases.

[5, 6] 7. In accordance with 11 U.S.C. § 526(c)(5), Attorney Stopa and the law firm, Stopa Law Firm, P.A., n/k/a Stay In My Home, P.A., jointly and severally, shall pay $12,000.00 in civil penalties to the U.S. Trustee, calculated at $1,000.00 for each pending chapter 13 bankruptcy case in which Stopa failed to comply with 11 U.S.C. § 526 or disregarded the material provisions of the Bankruptcy Code, Rules, and Local Rules.[18]

8. Attorney Stopa is prohibited from seeking reinstatement of his privilege to practice before this Court for **SIX YEARS** from the entry date of this Suspension Order.

9. After the expiration of this Suspension Order's ban on his readmission, Attorney Stopa may seek to reinstate his privilege to practice before this Court upon a clear showing of rehabilitation, compliance, and fitness to practice bankruptcy law. Reinstatement of Attorney Stopa is conditioned upon Attorney Stopa demonstrating that he:

a. Has provided this Court with a copy of this Suspension Order in his application for reinstatement;

b. Served the U.S. Trustee by U.S.P.S. or personal delivery service with a copy of his application for reinstatement;

c. Is a member in good standing with The Florida Bar;

d. Is admitted to the United States District Court for the Middle District of Florida;

e. Has complied with 11 U.S.C. § 526(c)(1) and (2) by refund and reimbursement to the chapter 13 debtor(s) for all fees, charges, costs, expenses, and actual damages in the 14 cited cases above where he either misrepresented the services that he would provide the debtor(s) or failed to provide the services that he informed the debtor(s) he would provide to them under the chapter 13 "soup-to-nuts" presumptively reasonable no-look fee provisions;[19]

f. Has complied with 11 U.S.C. § 526(c)(5)(B) and paid a $12,000.00 civil penalty to the United States Trustee; and

18. The Court takes notice that Stay In My Home, P.A. f/k/a Stopa Law Firm, P.A. filed Chapter 7 Case No. 8:18-bk-08436-RCT six days after the hearing leading to this Suspension Order. The Court finds and concludes that the entry of this Suspension Order does not violate the automatic stay in that case based on the exception found in 11 U.S.C. § 362(a)(4). *See Berg v. Good Samaritan Hospital (In re Berg)*, 230 F.3d 1165, 1167-68 (9th Cir. 2000) (sanctions imposed against debtor-attorney fall within government regulatory exception to the stay). More important, this Court "may wield its inherent power over the lawyers who practice before it." *Abdelgalel v. U.S. Atty. Gen.*, 443 Fed.Appx. 458, 462 (11th Cir. 2011) (quoting *Sahyers v. Prugh, Holliday & Karatinos, P.L*, 560 F.3d 1241, 1244 (11th Cir. 2009)).

19. *See* Order Establishing Presumptively Reasonable Debtor's Attorney Fee in Chapter 13 Cases, amendments thereto, and subsequent amended orders in Misc. Proc. No. 07-mp-00002-MGW (Doc. Nos. 31, 33, 35, 37, 38, and 40).

g. Has obtained continuing legal education in the areas of bankruptcy law, bankruptcy practice, law firm management, and ethics sufficient to demonstrate a clear knowledge of the bankruptcy system and the rights and interests of debtors, creditors, and trustees.

10. Should Attorney Stopa seek to be admitted to practice in any other jurisdiction, he shall provide a copy of this Suspension Order in his application to that jurisdiction and serve a copy of his complete admission application to that jurisdiction upon the United States Trustee or United States Bankruptcy Administrator applicable to that jurisdiction.[20]

11. If Attorney Stopa is admitted to any other federal court or jurisdiction, he shall provide a copy of this Suspension Order to the applicable Clerk of Court or administrative and regulatory body.

12. In accordance with 11 U.S.C. §§ 329(b) and 526(c), the Chapter 13 Standing Trustees, Kelly Remick, Laurie Weatherford, and Jon Waage, shall make no further disbursements to Attorney Stopa or his law firm. Any funds that would have been disbursed to Attorney Stopa, if any, shall be disbursed on other allowed claims, which distribution may result in an increased distribution to general unsecured creditors. Refund checks, if any, shall be disbursed, distributed, and delivered directly to the respective debtor(s).

13. The Clerk of this Court shall:

a. **REVOKE** and **TERMINATE** all PACER CM/ECF filing logins and passwords assigned to Attorney Stopa, the law office of Stopa Law Firm, P.A., n/k/a Stay In My Home, P.A., or any para-professional(s) that may have been issued a CM/ECF login and password with filing privileges associated with Attorney Stopa and/or Stopa Law Firm, P.A. n/k/a Stay In My Home, P.A., effective immediately upon the entry of this Order;

b. Indicate in the PACER records that Attorney Stopa's association as an attorney in a case is **TERMINATED**;

c. Record a copy of this Order in her judgment log maintained in accordance with Federal Rule of Bankruptcy Procedure 5003(c); and

d. File a copy of this Order in all pending bankruptcy cases wherein Attorney Stopa is associated as an attorney.

ORDERED.

IN RE: Frank Michael MONGELLUZZI, Debtor.

Angela Welch, Plaintiff,

v.

Regions Bank, Defendant.

Case No. 8:11-bk-01927-CED
Adv. Pro. No. 8:14-ap-653-CED

United States Bankruptcy Court,
M.D. Florida,
Tampa Division.

Signed July 18, 2018

Background: Chapter 7 trustee brought adversary proceeding against bank seeking to avoid and recover alleged fraudulent transfers, alleging debtors' accounts at

20. 28 U.S.C. § 581.

soned that evidence that Morrow unjammed, instead of reloaded, his gun was "not ... mitigating" because "it [was] clear [in either scenario] that he was taking active steps to prepare his gun to continue his murderous rampage." *Id.* We cannot say that the conclusion that the jury would have been unimpressed by a slightly different, but similarly brutal, version of events was unreasonable.

IV. CONCLUSION

We **AFFIRM** the denial of Morrow's petition for a writ of habeas corpus.

WILSON, Circuit Judge, concurring:

In light of our mandatory deference to the Supreme Court of Georgia's decision under the Antiterrorism and Effective Death Penalty Act, I concur with the result in this case. But in my estimation, the Superior Court of Butts County's resolution of the issues presented here was far more thorough and considerate than the resolution reached by the Supreme Court of Georgia in its reversal of the Superior Court's opinion. The Superior Court undertook a searching inquiry into Morrow's childhood, and unequivocally found that Morrow was "the victim of a series of rapes" while he was growing up in the New York area. It in turn concluded that trial counsel's failure to conduct a proper investigation into his life there rendered their performance deficient and prejudiced the outcome of Morrow's case. The Superior Court also found, after a careful examination into testimony and details about the crime scene, that trial counsel's failure to hire an independent crime scene expert was deficient and prejudicial to Morrow.

We should not subject a habeas petitioner to death if he has not been accorded the thorough review of an ineffective assistance of counsel claim that is contemplated under our Constitution. See U.S. Const. amend. VI ("In all criminal prosecutions, the accused shall enjoy the right ... to have the Assistance of Counsel for his defence."). I fear that, in Morrow's case, the result we have reached is based on the Supreme Court of Georgia's unwillingness to grapple with the intricacies of his case. Namely, here we are faced with the short shrift trial counsel gave not only to Morrow's time in New York and New Jersey and the sexual abuse that occurred there, but also to the thought of hiring a crime scene expert that supported Morrow's version of the crimes. It is hard to ignore that there could have been a recognizable impact on at least one member of the jury. Therefore, I concur in the result only.

Loyd P. CADWELL, Individually and on behalf of All Others Similarly Situated, Plaintiff–Appellant,

v.

KAUFMAN, ENGLETT & LYND, PLLC, Defendant–Appellee.

No. 17-10810

United States Court of Appeals, Eleventh Circuit.

March 30, 2018

Background: Client brought action against law firm that provided bankruptcy-related advice, alleging that law firm violated the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) by instructing him to pay his bankruptcy-related legal fees using a credit card. The United States District Court for the Middle District of Florida, No. 6:16-cv-00662-

PGB-KRS, Paul G. Byron, J., 2017 WL 5307898, granted law firm's motion to dismiss for failure to state a claim. Client appealed.

Holding: The Court of Appeals, Newsom, Circuit Judge, held that client stated claim under BAPCPA section prohibiting debt relief agency from advising clients to incur more debt to pay for bankruptcy-related legal services.

Reversed and remanded.

1. Statutes ⚷1156

Courts disfavor interpretations of statutes that render words or clauses superfluous.

2. Bankruptcy ⚷3030

Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) section prohibiting debt relief agency from advising assisted person or prospective assisted person to incur more debt to pay an attorney for bankruptcy-related legal services does not contemplate that such prohibited advice be given for invalid purpose designed to manipulate bankruptcy process; rather, it only aims to prevent attorney misconduct in advising client-debtor to take out additional debt to pay attorney. 11 U.S.C.A. § 526(a)(4).

3. Bankruptcy ⚷3030

Client stated claim under Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) section prohibiting debt relief agency from advising assisted person or prospective assisted person to incur more debt to pay an attorney for bankruptcy-related legal services, where he alleged that law firm that represented him in bankruptcy-related legal proceeding instructed him to pay initial retainer and all subsequent payments by credit card. 11 U.S.C.A. § 526(a)(4).

4. Bankruptcy ⚷3030
Constitutional Law ⚷2041

Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) section prohibiting a debt relief agency, including a law firm, from advising a client to incur more debt to pay for bankruptcy-related legal services does not improperly restrict attorney-client communications, in violation of the First Amendment; rather, it merely prohibits law firms from giving their clients affirmative advice to incur more debt in order to pay for bankruptcy-related representation, and it does not prevent law firms from discussing with debtors potential options and their legal consequences. U.S. Const. Amend. 1; 11 U.S.C.A. § 526(a)(4).

Appeal from the United States District Court for the Middle District of Florida, D.C. Docket No. 6:16-cv-00662-PGB-KRS

Bryan Keith Mickler, Law Offices of Mickler & Mickler, LLP, Jacksonville, FL, for Plaintiff–Appellant.

Shane Haselbarth, Marshall Dennehey Warner et al Law Office, Philadelphia, PA, Adam C. Herman, Marshall Dennehey Warner Coleman & Goggin, Orlando, FL, for Defendant–Appellee.

Jennifer Utrecht, U.S. Department of Justice, Civil Division, Appellate Staff, Charlene Goodwin, U.S. Department of Justice, Office of the Solicitor General, Mark B. Stern, U.S. Attorney General's Office, Washington, DC, for Intervenor.

Before ED CARNES, Chief Judge, NEWSOM, and SILER,* Circuit Judges.

* Honorable Eugene E. Siler, Jr., United States Circuit Judge for the Sixth Circuit, sitting by designation.

NEWSOM, Circuit Judge:

This case arises under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, which, among other things, amended federal law to impose new requirements and prohibitions on professionals who assist with the preparation of bankruptcy petitions. The provision specifically at issue here, 11 U.S.C. § 526(a)(4), provides in relevant part that a "debt relief agency"—including a law firm that provides bankruptcy-related services—"shall not . . . advise" a debtor "to incur more debt in contemplation of such person filing a case under this title or to pay an attorney or bankruptcy petition preparer a fee or charge for services performed as part of preparing for or representing a debtor in a case under this title." In *Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 130 S.Ct. 1324, 176 L.Ed.2d 79 (2010), the Supreme Court unanimously concluded that Section 526(a)(4)'s first prohibition—on advice to incur additional debt "in contemplation of" a bankruptcy filing—requires proof that the advice was given for an invalid purpose designed to manipulate the bankruptcy process. This case presents the question whether the statute's second prohibition—on advice to incur debt to pay for a lawyer's bankruptcy-related representation—likewise entails an invalid-purpose requirement. We hold that it does not and that, as relevant here, an attorney violates Section 526(a)(4) if he instructs a client to pay his bankruptcy-related legal fees using a credit card.

I

Loyd Cadwell consulted with the law firm of Kaufman, Englett & Lynd ("KEL") about the possibility of filing a Chapter 7 bankruptcy petition.[1] Following the initial meeting, Cadwell entered into an agreement that obligated him to pay $1700 in attorneys' fees "for representation in [his] Chapter 7 Bankruptcy case." The agreement contained an addendum establishing a schedule that required immediate payment of a $250 retainer, a second $250 installment shortly thereafter, and then, after that, four monthly installments of $300 apiece. According to Cadwell's complaint, "KEL instructed [him] to pay the initial retainer and all subsequent payments by credit card." As directed, Cadwell paid the initial retainer and the next three installments using two different credit cards.

After terminating his relationship with KEL, Cadwell filed this action under 11 U.S.C. § 526(a)(4), which, as already explained, states that a law firm "shall not . . . advise" a client "to incur more debt in contemplation of such person filing a case under this title or to pay an attorney" for bankruptcy-related legal services. KEL moved to dismiss Cadwell's complaint, arguing (1) that he hadn't stated a claim on which relief could be granted and (2) that even if he had, Section 526(a)(4) is unconstitutional because it improperly restricts KEL's attorney-client communications. The district court granted KEL's motion. "[W]ithout more," the court held, "the mere advice to use credit cards to pay for legal fees does not violate" Section 526(a)(4). Rather, based on its reading of the Supreme Court's decision in *Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 130 S.Ct. 1324, 176 L.Ed.2d 79 (2010), the district court concluded that Section 526(a)(4) only "prohibits a debt relief agency from advising a debtor to

1. Because Cadwell's appeal follows the district court's dismissal of his complaint for failure to state a claim, we accept as true the facts alleged in the complaint and draw all reasonable inferences in Cadwell's favor. *See, e.g., Hill v. White*, 321 F.3d 1334, 1335 (11th Cir. 2003).

incur additional debt for an invalid purpose." Because Cadwell had "alleg[ed] no facts that would" support an inference "that KEL acted with an improper purpose or with an intent to manipulate the bankruptcy system," the district court held that he had failed to state a viable claim under the statute. Having done so, the district court found it unnecessary to address KEL's First Amendment challenge.

On appeal, Cadwell contends that the district court erred in faulting him for failing to allege that KEL acted with an "invalid" (or "improper") purpose. At least as it pertains to a lawyer's advice to his client to incur debt to pay legal fees, Cadwell insists, Section 526(a)(4)'s text admits of no such requirement. KEL responds that the district court correctly interpreted the statute to impose an invalid-purpose element, but that even if Cadwell had stated a claim, the statute violates the First Amendment. Our review is *de novo*. *See Batchelor-Robjohns v. United States*, 788 F.3d 1280, 1284 (11th Cir. 2015).

II

As its name suggests, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 was enacted "to correct perceived abuses of the bankruptcy system." *Milavetz*, 559 U.S. at 231–32, 130 S.Ct. 1324. The Act added to the Bankruptcy Code a number of provisions directed at the conduct of bankruptcy professionals. *Id.* Among those provisions is 11 U.S.C. § 526(a), which "establishes several rules of professional conduct for persons qualifying as debt relief agencies," including lawyers. *Id.* at 233, 130 S.Ct. 1324. At issue here is subsection (a)(4), which provides as follows:

> A debt relief agency shall not . . . advise an assisted person or prospective assisted person to incur more debt in contemplation of such person filing a case under this title or to pay an attorney or bankruptcy petition preparer a fee or charge for services performed as part of preparing for or representing a debtor in a case under this title.

11 U.S.C. § 526(a)(4).

The parties here agree that KEL—as a law firm that provides bankruptcy-related advice—qualifies as a "debt relief agency" within the meaning of Section 526(a)(4). *See* Br. of Appellant at 3, 7; Br. of Appellee at 5; *see also Milavetz*, 559 U.S. at 239, 130 S.Ct. 1324. The parties also agree that for purposes of this appeal, Cadwell is an "assisted person or prospective assisted person" under the statute. *See* Br. of Appellant at 7; Br. of Appellee at 5. Finally, and importantly, the parties agree that the statute contains two distinct prohibitions—one about incurring debt in anticipation of bankruptcy filings generally, and the other about incurring debt to pay for bankruptcy-related legal services more specifically. From there, the parties' positions diverge.

A

The parties' central disagreement is over the proper way to parse Section 526(a)(4)'s two prohibitions. For example, where does each prohibition begin and end, and more to the point, does the phrase "in contemplation of"—which the Supreme Court in *Milavetz* construed to require proof that the advice to incur debt was given for an invalid purpose—apply to both prohibitions, or only the first? Unfortunately, the statute contains no punctuation that might help us determine where to place the "hinge" that divides the two prohibitions—which, as it turns out, really matters. We are presented here with three different ways of reading Section 526(a)(4)—one (sort of) suggested by the Supreme Court in *Milavetz*, another proposed by KEL and adopted by the district court, and yet another advocated by Cad-

well. Each locates the hinge in a different place in the text, resulting in three very different meanings. We consider each in turn.

1

Reading No. 1: "A debt relief agency shall not . . . advise an assisted person or prospective assisted person **[1]** to incur more debt in contemplation of such person filing a case under this title or **[2]** to pay an attorney or bankruptcy petition preparer a fee or charge for services performed as part of preparing for or representing a debtor in a case under this title."

One way to parse the statute was suggested (obliquely) by the Supreme Court's opinion in *Milavetz*. There, at the outset of the pertinent portion of its analysis, the Court observed that Section 526(a)(4) "prohibits a debt relief agency from 'advising an assisted person' *either* 'to incur more debt in contemplation of' filing for bankruptcy 'or to pay an attorney or bankruptcy petition preparer fee or charge for services' performed in preparation for filing." 559 U.S. at 239, 130 S.Ct. 1324 (emphasis added and alterations omitted). Under that reading, in which the hinge—the word "either" in the Court's paraphrase—comes before the words "to incur more debt," the statute would separately prohibit advice (1) "to incur more debt in contemplation of" filing for bankruptcy and (2) "to pay an attorney" for bankruptcy-related representation.

That's not an unnatural reading of the statute, at least as a grammatical matter. Under it, both prohibitions would begin (neatly) with infinitives—"to incur" and "to pay." But the interpretation does have a pretty big wart—namely, that it would flatly prohibit *all* advice "to pay an attorney" for bankruptcy-related representation. That makes little sense, it seems to us, particularly in light of other provisions of the Bankruptcy Code that clearly contemplate that attorneys will get paid for bankruptcy-related services. *See, e.g.*, 11 U.S.C. § 329 (requiring attorneys to "file with the court a statement of the compensation paid or agreed to be paid" during the year preceding the petition).[2]

Perhaps not surprisingly, no one here has urged us to adopt this reading of Section 526(a)(4). And we don't think that we are bound by *Milavetz*'s passing suggestion that the statute's second prohibition might be understood to forbid advice "to pay an attorney," because the Court was concerned there only with the first prohibition. *See* 559 U.S. at 239, 130 S.Ct. 1324 ("Only the first of these prohibitions is at issue."). We thus reject any interpretation of Section 526(a)(4) pursuant to which the statute's second prohibition erects a categorical bar on advice to pay bankruptcy attorneys.

2

Reading No. 2: "A debt relief agency shall not . . . advise an assisted person or prospective assisted person to incur more debt in contemplation of **[1]** such person filing a case under this title or **[2]** to pay an attorney or bankruptcy petition preparer a fee or charge for services performed as part of preparing for or representing a debtor in a case under this title."

There is a second way to read Section 526(a)(4), proposed by KEL and adopted by the district court. In essence, KEL

2. *See also Lamie v. United States Trustee*, 540 U.S. 526, 537, 124 S.Ct. 1023, 157 L.Ed.2d 1024 (2004) ("It appears to be routine for debtors to pay reasonable fees for legal services before filing for bankruptcy. . . .").

asserts that the statute prohibits a lawyer from advising his client to incur debt to pay for bankruptcy-related legal services *only* if that advice was given for an "invalid purpose." The district court agreed, reasoning that KEL's invalid-purpose interpretation was compelled by *Milavetz*. We disagree.

The issue in *Milavetz* was whether the first prohibition in Section 526(a)(4)—precluding advice to incur more debt "in contemplation of" a bankruptcy filing—unconstitutionally restricted a law firm's attorney-client communications. In service of its speech-based argument, the firm there contended that Section 526(a)(4)'s first prohibition broadly forbade "not only affirmative advice but also any discussion of the advantages, disadvantages, or legality of incurring more debt." 559 U.S. at 240, 130 S.Ct. 1324. The Supreme Court rejected the firm's expansive interpretation; instead, focusing on the phrase "in contemplation of," the Court concluded that the first prohibition more narrowly prevents an attorney "only from advising a debtor to incur more debt because the debtor is filing for bankruptcy, rather than for a valid purpose." *Id.* at 243, 130 S.Ct. 1324. In so holding, the Court explained that the phrase "in contemplation of" is a term of art historically associated with abusive conduct—basically, advice to "load up" on debt with the expectation of obtaining its discharge in bankruptcy. *Id.* at 244, 130 S.Ct. 1324. Thus, the Court held, the "controlling question" under Section 526(a)(4)'s first prohibition is "whether the impelling reason for advising an assisted person to incur more debt was the prospect of filing for bankruptcy." *Id.* at 243, 130 S.Ct. 1324 (quotation marks and alterations omitted).

We reject the view that *Milavetz*'s invalid-purpose gloss applies here. For starters, *Milavetz* certainly doesn't "directly control[ ]" this case, as KEL asserts. Br. of Appellee at 11. As already explained, *Milavetz* addressed only Section 526(a)(4)'s first prohibition; it said nothing about the second. 559 U.S. at 239, 130 S.Ct. 1324 ("Only the first of these prohibitions is at issue."). Nor, we conclude, does *Milavetz*'s reasoning sensibly apply to the statute's second prohibition. Again, the *Milavetz* Court's conclusion that the statute's first clause prohibits only advice to incur additional debt for an invalid purpose rested on the phrase "in contemplation of." Thus, KEL's *Milavetz*-based argument—pursuant to which the invalid-purpose gloss applies to the second prohibition, as well as the first—would require that we place the hinge after the phrase "in contemplation of." On that construction, the statute would prohibit advice "to incur more debt in contemplation of [1] such person filing a case under this title or [2] to pay an attorney" for bankruptcy-related legal representation.

[1] That interpretation founders for two reasons. Initially, and most obviously, it makes syntactical hash of Section 526(a)(4)'s second prohibition: A lawyer shall not advise his client "to incur more debt in contemplation of . . . to pay an attorney"? Nonsense. *See United States v. Hayes*, 555 U.S. 415, 422, 129 S.Ct. 1079, 172 L.Ed.2d 816 (2009) (rejecting a particular reading of a statute because it was, among other things, "awkward as a matter of syntax"). Moreover, reading the phrase "in contemplation of" to apply to both prohibitions renders the second prohibition essentially meaningless. Under KEL's interpretation, advice to incur additional debt would violate Section 526(a)(4) if *either* (1) the "impelling reason" for the advice is the expectation of bankruptcy discharge, *i.e.*, an invalid purpose, *see Milavetz*, 559 U.S. at 243, 130 S.Ct. 1324, *or* (2) the impelling reason for the advice is

exactly the same, and is thus invalid for the same reason, *and* the debt happens to be incurred to pay an attorney. Under that reading, the second prohibition becomes a mere subset of the first—it has no independent bite. We disfavor interpretations of statutes that render words or clauses superfluous. *See, e.g., Bloate v. United States*, 559 U.S. 196, 209, 130 S.Ct. 1345, 176 L.Ed.2d 54 (2010). We therefore reject KEL's contention that the phrase "in contemplation of"—and thus, *Milavetz*'s invalid-purpose test—applies to Section 526(a)(4)'s second prohibition.

3

> **Reading No. 3**: "A debt relief agency shall not ... advise an assisted person or prospective assisted person to incur more debt **[1]** in contemplation of such person filing a case under this title or **[2]** to pay an attorney or bankruptcy petition preparer a fee or charge for services performed as part of preparing for or representing a debtor in a case under this title."

That leaves us with a third possible—and in our view, the correct—interpretation of Section 526(a)(4). Under this reading, the hinge comes after the phrase "to incur more debt," such that the statute prohibits advice "to incur more debt" either (1) "in contemplation of" a bankruptcy filing or (2) "to pay an attorney" for bankruptcy-related legal services. Unlike the first two interpretations, this one doesn't produce goofy results, defy the usual rules of syntax, or render a phrase meaningless.

[2] Properly interpreted, then, Section 526(a)(4)'s second prohibition forbids lawyers from advising their clients "to incur more debt ... to pay an attorney ... a fee or charge for services performed as part of preparing for or representing a debtor in a case under this title." 11 U.S.C. § 526(a)(4). Importantly, this second prohibition—unlike the first, which is modified by the "in contemplation of" phrase of art that drove the result in *Milavetz*—entails no invalid-purpose requirement. And that, we think, makes perfect sense, because the two prohibitions address different subjects. The first is framed in general terms—it forbids advice "to incur more debt in contemplation of" a bankruptcy filing. That prohibition, read for all it might be worth, could cover both abusive advice (*e.g.*, advice to "load up" on debt just to get it discharged) and salutary advice that would likely inure to the benefit of both debtor and creditor (say, to refinance a mortgage to a better interest rate). As the Supreme Court recognized in *Milavetz*, the "in contemplation of" clause acts as a divining rod of sorts to separate the abusive advice from the salutary. 559 U.S. at 239–43, 248 n.6, 130 S.Ct. 1324.

The second prohibition, by contrast, is aimed at one specific kind of misconduct—in essence, a bankruptcy lawyer saying to his client, "You should take on additional debt to pay me!" That sort of advice is inherently abusive in at least two respects. First, it puts the attorney's financial interest—getting paid in full—ahead of the debtor-client's. If a creditor discovers the timing and reason for the fee-related debt, it could challenge the debt's dischargeability, thereby compromising the debtor's fresh start. *See Milavetz*, 559 U.S. at 245, 130 S.Ct. 1324. Second, it puts the lawyer's own interests ahead of the creditors' in that, while ensuring the lawyer's full payment, it leaves a diminished estate on which creditors can draw. *See id.* Section 526(a)(4)'s second prohibition, then, has no need for any further invalid-purpose gloss, because the advice it targets is, in effect, suspect *per se*.

* * *

We therefore hold that the district court erred in concluding that Cadwell was required to allege that KEL's advice was given for some additional, invalid purpose. Rather, the statute required only that he allege that he was "advise[d] . . . to incur more debt . . . to pay an attorney" for bankruptcy-related legal services.

B

[3] Having determined Section 526(a)(4)'s proper interpretation, we now turn to the question whether Cadwell's allegations state a claim under the statute's second prohibition. It seems clear to us that they do.

Cadwell alleged in his complaint that "KEL instructed [him] to pay the initial retainer and all subsequent payments by credit card." Good enough. First, Cadwell's assertion that KEL "instructed" him to make the payment satisfies the statute's "advise" requirement. *See Milavetz*, 559 U.S. at 246, 130 S.Ct. 1324 (explaining that Section 526(a)(4)'s limit on "advis[ing]" a person to incur more debt "requires professionals . . . to avoid *instructing or encouraging* assisted persons to take on more debt in that circumstance") (emphasis added). Second, Cadwell alleged that he was instructed to make a payment by credit card, an action that necessarily required him to "incur more debt." *See, e.g.*, Webster's Second New International Dictionary 1261 (1959) (defining "incur" to mean "[t]o meet or fall in with, as something inconvenient or harmful; to become liable or subject to; to bring down upon oneself; as to *incur* debt. . . ."). Finally, there is no dispute for purposes of this appeal that the credit card charges were for KEL's representation of Cadwell in a bankruptcy-related legal proceeding.[3]

We therefore have no trouble concluding (as even KEL's attorney ultimately conceded at oral argument[4]) that Cadwell's allegations state a claim under the statute as we have interpreted it.[5]

III

KEL finally contends that even if Cadwell has stated a claim under Section 526(a)(4), that provision is unconstitutional because it improperly restricts KEL's attorney-client communications. KEL's primary argument in that connection is that "[p]rohibiting advice to clients to pay a fee" violates the First Amendment. Br. of Appellee at 24. But as already explained, Cadwell hasn't asserted—and we don't hold—that the statute flatly prevents a lawyer from advising a client to pay legal

3. Because a violation of Section 526(a)(4) is complete when a lawyer gives the advice to incur a debt to pay for bankruptcy-related representation, it doesn't matter that Cadwell might have completed a "Payment Authorization" form indicating that he intended to pay (at least in part) by debit card. In any event, ambiguities in the complaint are construed in Cadwell's favor, *see, e.g., Hill*, 321 F.3d at 1335, and exhibits attached to the complaint demonstrate that Cadwell did in fact make four of his payments via credit card.

4. *See* Tr. of Oral Argument at 15:45 (Q: "Do you agree that if the statute is properly read to say that the debt relief agency shall not advise an assisted person to incur more debt to pay his lawyer, [then] the allegation in paragraph 10 is sufficient under *Twombly* and *Iqbal*?" * * * A: "Yes, it is. . . .").

5. Cadwell's complaint also purports to assert a claim on behalf of a class. As to the class, Cadwell alleged that "KEL collected Chapter 7 retainer fees from the prospective debtor(s) through the charging of a credit/charge card which served to cause the prospective debtor(s) to incur more debt prior to the potential filing of the Chapter 7." The district court didn't address whether the class allegations stated a claim under the statute, and the parties haven't addressed those allegations on appeal. We therefore won't address them either.

fees. We therefore reject any First Amendment argument based on that overbroad reading of the statute.

[4] KEL separately—and more narrowly—contends that "a statutory prohibition on KEL from providing sound legal advice as to how a client may obtain representation from an attorney, pay costs, and navigate the complex world of bankruptcy law is unconstitutional." Br. of Appellee at 24. The Supreme Court considered and dismissed a similar argument in *Milavetz*. Specifically, the Court "reject[ed] . . . [the] suggestion that § 526(a)(4) broadly prohibits debt relief agencies from *discussing* covered subjects instead of merely proscribing affirmative advice to undertake a particular action." 559 U.S. at 246, 130 S.Ct. 1324 (emphasis added and alterations omitted). Rather, the Court explained, the statute "by its terms prevents debt relief agencies only from 'advising' assisted persons 'to incur' more debt," meaning that attorneys "remain free to talk fully and candidly *about* the incurrence of debt in contemplation of filing a bankruptcy case." *Id.* Just so here. Section 526(a)(4) doesn't prevent firms like KEL from discussing with debtors potential options and their legal consequences. It merely prohibits them from giving their clients "affirmative advice" to incur more debt in order to pay for bankruptcy-related representation.[6]

IV

We therefore hold (1) that a debt-relief agency (including a law firm) violates 11 U.S.C. § 526(a)(4) if it advises a client to incur additional debt to pay for bankruptcy-related legal representation, without respect to whether the advice was given for some independently "invalid purpose"; (2) that Cadwell's allegation that KEL instructed him to pay his bankruptcy-related legal bills by credit card states a viable claim under Section 526(a)(4); and (3) that none of the constitutional arguments that KEL has presented to us warrants invalidating the statute on First Amendment grounds.

REVERSED AND REMANDED.

UNITED STATES of America, Plaintiff-Appellant,

v.

Michael LEE, Defendant-Appellee.

Michael Lee, Petitioner-Appellee,

v.

United States of America, Respondent-Appellant.

No. 16-16590, No. 16-16591

United States Court of Appeals, Eleventh Circuit.

April 2, 2018

Background: Federal inmate filed motion to vacate, set aside, or correct sentence. The United States District Court for the

6. Because KEL didn't offer in its brief any other arguments as to why Section 526(a)(4)—as properly interpreted—might violate the First Amendment, we needn't further consider whether the statute, as correctly interpreted, withstands First Amendment scrutiny. *Cf. Milavetz*, 559 U.S. at 248, 130 S.Ct. 1324 ("Because our reading of the statute supplies a sufficient ground for reversing the Court of Appeals' decision, and because [the firm] challenges the constitutionality of the statute, as narrowed, only on vagueness grounds, we need not further consider whether the statute so construed withstands First Amendment scrutiny.").

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF WISCONSIN

In re: Case No.: 18-10019-7

LYDELL JAMES KLUCK and
MARGARET MARIE KLUCK,

Debtors.

MEMORANDUM DECISION

Lydell and Margaret Kluck ("Debtors") filed a voluntary joint chapter 7 petition. Debtors claimed an annuity as exempt. Trustee James Block ("Trustee") objected to the exemption. The parties filed a Joint Stipulation of Facts.

BACKGROUND

Before filing their petition, Mr. Kluck owned, among other assets, a 1974 Plymouth, two parcels of real estate in Marathon County, two parcels of real estate in Portage County, and 6.1% of the shares in A&T Hunting Club, LLC ("A&T"), which owned more than one hundred acres of land in Marathon County.[1]

In the months before filing bankruptcy, the Debtors sold those assets and deposited the sale proceeds of $181,780.00 in an account at Associated Bank. The Debtors transferred $177,000.00 of the proceeds into an account

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[1] The Debtors were the sole owners of the Plymouth. The Debtors' interest in the other assets is described as "joint with non-Debtor(s)." The parties have not asserted this impacts the exemption or objection to it.

formed fifteen days before they filed bankruptcy (the "Prudential Account"). Debtors claim the Prudential Account exempt under Wisconsin exemptions.

The parties stipulate that before the sales, the assets were not the Debtors' homestead or exempt (i) from execution by judgment creditors under Wisconsin law; (ii) under bankruptcy law; or, (iii) from federal or Wisconsin state income taxation.

The Trustee argues the claimed exemption should be disallowed. According to the Trustee, the Prudential Account does not satisfy the requirements of Wis. Stat. § 815.18(3)(j) (the retirement benefits exemption) because the Prudential Account is not tax-deferred. The Trustee also argues distributions under the Prudential Account are not conditioned upon any particular event and so also fail to satisfy the statute.

Debtors respond the Prudential Account provides for distribution because of age and death. They also contend the fact that certain withdrawals were taxable events does not render the Prudential Account non-tax-deferred. The Debtors withdrew certain funds from the account at Associated Bank to pay attorney's fees.

DISCUSSION

I. The exemption under Wis. Stat. § 815.18(3)(j).

Most of a debtor's assets become property of the bankruptcy estate upon commencement of a bankruptcy case. 11 U.S.C. § 541. To help the debtor obtain a fresh start, the Code permits a debtor to exempt from the estate certain interests in property. *Id.* § 522. Exemptions are "part and parcel of the

fundamental bankruptcy concept of a 'fresh start.'" *Schwab v. Reilly*, 560 U.S. 770, 791 (2010). But the right of a debtor to claim property as exempt is not unlimited. The Code limits a debtor's exemptions because every asset claimed as exempt is an asset unavailable to satisfy the claims of creditors. *Id.*

Claimed exemptions are presumptively valid. *See* 11 U.S.C. § 522(l) ("Unless a party . . . objects, the property claimed as exempt . . . is exempt."). An objecting party bears the burden of showing the exemption is not properly claimed. Fed. R. Bankr. P. 4003(c). Once the objecting party produces evidence to rebut the presumptive validity of a claimed exemption, the burden shifts back to the debtor to present evidence demonstrating the exemption is proper. *Elliott v. Weil (In re Elliott)*, 544 B.R. 421, 429 (B.A.P. 9th Cir. 2016).

In Wisconsin, a debtor may choose between the exemption scheme set forth in the Bankruptcy Code and the Wisconsin Statutes. *See* 11 U.S.C. § 522(b). Here, the Debtors elected to claim exemptions under Wisconsin law.

When a debtor claims a state-created exemption, the exemption's scope is determined by state law. *Law v. Siegel*, 571 U.S. 415, 425 (2014). "[I]t is a cardinal rule in Wisconsin that exemption laws must be liberally construed." *In re Woods*, 59 B.R. 221, 224 (Bankr. W.D. Wis. 1986) (citations omitted). "[P]roper construction of the exemption statute requires both an interpretative generosity in favor of the debtors and a simultaneous recognition that the statute reflects a legislative choice to protect certain assets at the expense of others." *In re Woller*, 483 B.R. 886, 890 (Bankr. W.D. Wis. 2012).

The Debtors rely on the Wisconsin retirement benefits exemption. To claim this exemption, the Prudential Account must satisfy Wis. Stat. §§ 815.18(3)(j)1. and 2. The Court takes each requirement in turn.

A. *The Prudential Account satisfies section 815.18(3)(j)2.*

To qualify for the retirement benefits exemption, the account must "compl[y] with the provisions of the internal revenue code [IRC]." Wis. Stat. § 815.18(3)(j)2.a.[2] While the Wisconsin exemption statute does not expand upon this requirement, "Wisconsin bankruptcy courts have uniformly interpreted the exemption as simply requiring that an annuity be tax deferred under" section 72 of the IRC. *Cirilli v. Bronk (In re Bronk)*, 775 F.3d 871, 878 (7th Cir. 2015). *See also In re Vangen*, 334 B.R. 241, 244 (Bankr. W.D. Wis. 2005) ("All that is required for an annuity to be exempt under this section is that it qualify for tax-deferred status under the internal revenue code.").

Generally, gross income includes any amount received as an annuity under an annuity. 26 U.S.C. § 72(a)(1). An important exception is known as the exclusion ratio, which provides that "[g]ross income does not include that part of any amount received as an annuity under an annuity . . . which bears the same ratio to such amount as the investment in the contract . . . bears to the expected return under the contract . . . ." *Id.* § 72(b)(1).

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[2] There are other ways a retirement account can satisfy section 815.18(3)(j)2. The Debtors have not asserted the Prudential Account satisfies any of them. The sole issue the parties raised is whether the Prudential Account satisfies sections 815.18(3)(j)1. and 2.a.

Section 72(s) outlines an important requirement for an annuity to obtain tax-deferred status. It provides:

> (1) In general.—A contract shall not be treated as an annuity contract for purposes of [title 26] unless it provides that—
>
> (A) if any holder of such contract dies on or after the annuity starting date and before the entire interest in such contract has been distributed, the remaining portion of such interest will be distributed at least as rapidly as under the method of distributions being used as of the date of his death, and
>
> (B) if any holder of such contract dies before the annuity starting date, the entire interest in such contract will be distributed within 5 years after the death of such holder.

The Prudential Account provides a death benefit. That benefit is "payable upon the Annuitant's death." The payment will be made within five years if the death occurs before the annuity starting date or as soon after the death as proof of death or payment instructions are received. Thus, the account contract contains the death benefit language required under section 72(s) of the Tax Code.

The Trustee also argues the Prudential Account is not tax-deferred because the Debtors' recent withdrawal from the account was a taxable event. This argument is incorrect. Early withdrawals do not render the principle non-tax-deferred. Funds in the Prudential Account are tax-deferred until *distribution*.

Courts in this Circuit have consistently held that annuities that qualify for tax-deferred status under 26 U.S.C. § 72 satisfy the requirements of section 815.18(3)(j). *Wittman v. Koenig*, 831 F.3d 416, 420 (7th Cir. 2016). The

Prudential Account is tax-deferred and complies with the IRC for purposes of section 815.18(3)(j)2.a.

B. *The Prudential Account satisfies section 815.18(3)(j)1.*

In the end, qualifying under the IRC does not establish the exemption. All the requirements of the exemption statute have to be met.

Turning to the Trustee's second argument, Wisconsin's exemption statute protects certain retirement benefits, including:

> Assets held or amounts payable under any . . . annuity, individual retirement account, [or] individual retirement annuity . . . providing benefits *by reason of* age, illness, disability, death or length of service and payments made to the debtor therefrom.

Wis. Stat. § 815.18(3)(j)1. (emphasis added).

The Debtors concede the Prudential Account does not contain any language referencing length of service, illness, or disability. They argue, however, the Prudential Account provides for distribution "by reason of" age and death.

In *Bronk*, the Seventh Circuit considered the definition of "by reason of," holding:

> The term "by reason of" is synonymous with "because of" or "on account of." It requires a causal connection between the phrase preceding it—"providing benefits"—and the list of factors that comes after it. Accordingly, for any of the listed retirement products, the statute requires that one of the listed conditions triggers payment of benefits.

775 F.3d at 877 (citations omitted). The Seventh Circuit held the account at issue satisfied the requirements of section 815.18(3)(j). The *Bronk* decision states:

> Bronk's annuity begins paying on a fixed date—January 3, 2035—and thus does not pay benefits because of age, length of service, or the onset of an illness or disability. But the annuity also contains a death benefit. That feature brings it under the umbrella of section 815.18(3)(j).

Id. at 878 ("[T]o qualify . . . under subsection (3)(j), an annuity must distribute benefits *because of* or *conditioned on* age, illness, disability, death, or length of service.") (emphasis in original).

The Seventh Circuit's decision in *Bronk* contains little discussion on when death beneficiary language is enough to bring a contract under the Wisconsin retirement benefits exemption. A literal reading of the decision, without more, seemingly implies that *any* language awarding distribution upon the death of the account owner brings the account under the umbrella of section 815.18(3)(j).

Additional analysis applying the exemption to an annuity is in *Wittman.* The Court noted the Wisconsin statutes define annuity in Wis. Stat. § 815.18(2)(am), as "a series of payments payable during the life of the annuitant or during a specific period." *Wittman*, 831 F.3d at 419.

The annuity here provides for monthly payments under two options—either for a specific number of years or for life with a ten-year period certain and any remaining payments to the beneficiary on the death of the annuitant. If no option is selected, the default is the latter option. The earliest available annuity date is three years from the date the annuity was issued. The latest is the first day of the calendar month following the ninety-fifth birthday of the annuitant.

The first three years under the contract are referred to as the accumulation period. The annuity can be surrendered during the accumulation period for the account balance less any tax charges, maintenance fees, and deductions for any optional benefits. Partial withdrawals are also permitted with few limits. Once the balance in the account drops below a certain level, the remaining balance must be withdrawn.

There are differences between the Prudential Annuity and the *Bronk* annuity. The annuity in *Bronk* imposed "surrender charges" and permitted only limited "free withdrawal amounts."[3] Early withdrawals were subject to fees. The distribution options in *Bronk* were more narrow than in this case. But the annuity in both cases each permit early withdrawals. Both have provisions for monthly payments beginning at a specified time.

The Prudential Account contract provides that the earliest available annuity date is three years from the Issue Date of December 20, 2017. At that point Mr. Kluck would be 58 or 59. The latest available annuity date is the first day of the calendar month following his ninety-fifth birthday. Although far in the future, there is a specific mandatory age for payment. The Debtors equate this language to distributions being *conditioned upon* age. While subtle, the distinction is significant. Distributions are not *conditioned upon* Mr. Kluck

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[3] For the *Bronk* annuity contract, *see* adv. no. 10-44, ECF no. 63. The annuity in *Bronk* allowed the debtor to withdraw up to ten percent of the value of the account for free during year one, increasing to twenty percent for each year from that point. Any amounts withdrawn above those percentages were subject to fees of at least four percent during years one through five, with no fees from that point. Adv. no. 10-44, ECF no. 63 at 3B.

reaching any particular age. Rather, distribution must begin *no later than* him reaching the age of ninety-five.

The annuity is structured to provide payments over time. Absent in the record is any evidence of whether the annuity was acquired with retirement in mind.

The Court's duty is to construe exemptions broadly. *See* Wis. Stat. § 815.18(1).

> [T]he Wisconsin Supreme Court explains that: It is well settled that exemption laws must have a liberal construction, within the limits contemplated by the legislature, so as to secure their full benefit to the debtor, in order to advance the humane purpose of preserving to the unfortunate or improvident debtor and his family the means of obtaining a livelihood and thus prevent him from becoming a charge upon the public. *Julius*, 214 Wis. at 649. This principle is now codified in Wis. Stat. § 815.18(1).

Matter of Koenig, No. 14-14446, 2015 WL 4241393 at *3 (quoting *Bronk v. Cirilli*, No. 11–CV–172–WMC, 2012 WL 12012746 at *5 (W.D. Wis. Sept. 28, 2012), *aff'd in part, rev'd in part sub nom. In re Bronk*, 775 F.3d 871 (7th Cir. 2015)).

Nothing in the text of the exemption statute suggests it excludes from subsection (3)(j) annuities that may allow early withdrawals. If the ability to withdraw in circumstances other than at a particular age was disqualifying, then other forms of retirement options might also be excluded from the exemption. For example, withdrawals—in whole or in part—can be made from an IRA before retirement age.

The statute must be read to give reasonable effect to every word. Leaving provisions inoperative should be avoided. The statute is written in the disjunctive—"by reason of age, illness, disability, death *or* length of service." Although the latest annuity date is far in the future, the annuity is still payable because of the age of Mr. Kluck. Under the annuity, Mr. Kluck may take payment starting in three years but must take payment at age ninety-five. Thus, there is an age trigger. Even if, however, the age component was insufficient, there is still a death-based trigger for distribution.

While "[w]e may not 'write exemptions into statutes,' . . . based on this legislative instruction, we must broadly interpret the exemptions the legislature has created." *Wittman*, 831 F.3d at 424 (quoting *In re Geise*, 992 F.2d 651, 656 (7th Cir. 1993)). *See also In re Bogue*, 240 B.R. 742, 746 (Bankr. E.D. Wis. 1999) (quoting *Wisconsin Exemption Statutes-Legislative Update, Annual Bankruptcy Update* (State Bar of Wisconsin), October 1990, at Shapiro-30) ("The revision [of the retirement benefits exemption] is intended to broaden the areas and items that are now exempt . . . ."). If, as here, there are ambiguities in the statute, they must be construed in favor of the debtor.

In the end, whether payable by reason of age or not, the Prudential Account is certainly payable on death. It qualifies under the applicable provisions of the IRC and section 815.18(3)(j). It is, therefore, exempt. The Trustee's objection on the ground the exemption fails to satisfy section 815.18(3)(j) is overruled.

II. Should the exemption be disallowed in whole or in part under section 815.18(10)?

Under the Wisconsin exemption statute, a court may deny an exemption "if, in the discretion of the court having jurisdiction, the debtor procured, concealed or transferred assets with the intention of defrauding creditors." Wis. Stat. § 815.18(10). *See also Woller*, 483 B.R. at 901 ("[A]n otherwise valid exemption may still be denied . . . if the debtor is found to have 'procured, concealed, or transferred assets with the intention of defrauding creditors.'") (quoting *Vangen*, 334 B.R. at 246).

Often, debtors seek to convert non-exempt assets into exempt assets shortly before filing bankruptcy. This is known as "exemption planning." "[E]xemption planning, even bad faith exemption planning[,] does not necessarily justify disallowance" of a claimed exemption. *In re Hurt*, 542 B.R. 798, 802 (Bankr. E.D. Tenn. 2015). "[W]hile debtors are to be permitted to take full use of the available exemptions, their tactics in converting non-exempt property to exempt property on the eve of bankruptcy may trigger adverse consequences if their conduct warrants." *In re Bruski*, 226 B.R. 422, 426 (Bankr. W.D. Wis. 1998). This Court has held:

> Under relevant Seventh Circuit precedent, so-called exemption planning only rises to the level of fraudulent conduct if there is evidence that the debtor committed some act "extrinsic to the conversion" which hinders, delays, or defrauds creditors. . . . The fact that a debtor engages in exemption planning while faced with financial distress is not itself evidence of fraudulent conduct.
>
> After all, the use of exemptions is at least a legitimate form of asset protection, and debtors should only be penalized when they go beyond taking advantage of the exemption laws themselves. . . . [T]here is a difference between creating a

> smokescreen that makes it difficult for creditors to realize on their claims and merely attempting to take advantage of legally available exemptions.

Woller, 483 B.R. at 901–02.

The objection explicitly raises whether the Prudential Annuity satisfies section 815.18(3)(j). While no specific reference is made to section 815.18(10), the objection does say, "That depending on the information the Debtors provide there may not be an exemption under Wisconsin exemptions for the Debtors' Prudential Retirement Annuity . . . allowed under law and therefore the entire exemption must be denied." This, the Trustee argues, is enough to preserve an objection under section 815.18(10).

The parties stipulate that $177,198.50 is the amount of the exemption. They agree the annuity was funded between December 12 and 20, 2017. The bankruptcy was filed January 4, 2018. The source of funds used for the purchase were assets that were not exempt. Each of these facts is be considered for purposes of section 815.18(10).

Additional factors include any misleading contacts with creditors while converting non-exempt assets to exempt assets; the purpose of the conversion of assets; and conveyance for less than fair market value. *Bogue*, 240 B.R. at 750–51. None of these facts are in the record.

The factors are not mere questions of law. Instead, decisions on this statute require consideration of facts. That analysis must be in the context of the policies underlying the Wisconsin retirement benefits exemption. The stated purpose of section 815.18 is:

> This section shall be construed to secure its full benefit to debtors and to advance the humane purpose of preserving to debtors and their dependents the means of obtaining a livelihood, the enjoyment of property necessary to sustain life and the opportunity to avoid becoming public charges.

Wis. Stat. § 815.18(1).

"The court may deny any or all of the exemptions claimed if, in the discretion of the court, the debtor procured, concealed or transferred assets with the intention of defrauding creditors." Wis. Practice Series, *Wisconsin Collection Law*, Robert A. Pasch, 12 WIPRAC § 15.6 (May 2019 Update). If the Trustee wants to pursue an objection on these grounds at the appropriate time, he may so advise the Court. The exercise of discretion will require more presentation of evidence. So, it is premature to decide something not yet before the Court.

CONCLUSION

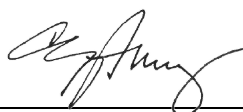
The claimed exemption does satisfy section 815.18(3)(j). The objection on the grounds of this section is overruled.

This decision shall constitute findings of fact and conclusions of law pursuant to Bankruptcy Rule 7052 and Rule 52 of the Federal Rules of Civil Procedure.

A separate order consistent with this decision may be entered.

Dated: June 14, 2019

BY THE COURT:



Hon. Catherine J. Furay
U.S. Bankruptcy Judge