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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

In re:
MANSTONE COUNTERTOPS LLC,

Debtor.

Chapter 11
(Jointly Administered)
Case No. 2:09-bk-26913-SSC
Case No. 2:09-bk-32033-SSC
(Not for Publication- Electronic Docketing
ONLY)

MEMORANDUM DECISION

In re:
DAVID R. ROBINSON
CHELLEE C. ROBINSON

Debtor.

I. PRELIMINARY STATEMENT

This matter comes before the Court on a “First and Final Fee Application for Payment of Compensation to Counsel for Manstone Countertops LLC” and “First and Final Fee Application for Payment of Compensation to Counsel for David and Chellee Robinson” filed with the Court on November 20, 2012 by Robert M. Cook. These fee applications were filed per the Court’s Minute Entry Order on October 10, 2012, after the chapter 11 trustees were appointed in each case. Several objections followed from the appointed chapter 11 trustees, a

1 B. Whether Attorney Cook may be compensated for work prior to court approval and subsequent
2 to his removal.

3 C. Whether Attorney Cook’s fees are reasonable.
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6 IV. DISCUSSION

7 **A. Mr. Cook’s Failure to Disclose the Earned Upon Receipt Provision in the**
8 **Fee Agreement with Debtors**

9 The objecting parties argue that Mr. Cook failed to disclose that the retainers he
10 received prior to the petition were flat fees, earned upon receipt. Indeed, while Mr. Cook’s
11 employment applications disclose that he had received a retainer of \$25,000 in each case, the
12 applications do not state that they were flat fees. In fact, Mr. Cook lists the hourly rates for
13 himself and his legal assistants, indicating that he would bill on an hourly basis. More
14 importantly, nowhere on the employment application does Mr. Cook indicate that the \$25,000
15 retainers were earned upon receipt. Nonetheless, Mr. Cook claims for the first time in his fee
16 applications—filed nearly three years after the cases were originally filed— that the \$25,000
17 retainers received in each case were “flat fee[s] earned upon receipt.”

18 Section 329 requires counsel for the debtor to file with the court a statement of
19 compensation paid or agreed to be paid made within one year before the filing of the petition for
20 services related to the case. When applying for fees, the applicant must disclose “the precise
21 nature of the fee arrangement, and not simply identify the ultimate owner of the funds.” In re
22 Park-Helena Corp., 63 F.3d 877, 881 (9th Cir. 1995). An attorney must also comply with
23 Bankruptcy Rule 2014, which requires professionals to disclose “all...connections with the
24 debtor, creditors, [or] any other party in interest,” and with 11 U.S.C. § 327(a), which requires
25 that the professional be disinterested. The Code defines a “disinterested” person as one that
26 “does not have an interest materially adverse to the interest of the estate or of any class of
27 creditors or equity security holders, by reason of any direct or indirect relationship to, connection
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1 with, or interest in, the debtor ..., or for any other reason.” 11 U.S.C. § 101(14)(C).

2 Failure to disclose fully relevant information related to a retainer may result in a
3 denial of all requested fees, even if the failure to disclose is negligent or inadvertent. Park-
4 Helena Corp., 63 F.3d at 882; In re Lewis, 113 F.3d 1040, 1045 (9th Cir. 1997). Failure to
5 disclose critical information to the Court deprives the Court of an opportunity to make an
6 informed decision and frustrates the disclosure provisions of Section 329 and Bankruptcy Rule
7 2016. In re Crimson Investments, N.V., 109 B.R. 397, 401 (Bankr. D. Ariz. 1989). Even when
8 there is no actual harm to the estate, the bankruptcy system itself is harmed by a professional’s
9 failure to make required disclosures. In re LSS Supply Inc., 247 B.R. 280, 283 (Bankr. D. Ariz.
10 2000).

11 Generally, a retainer taken by a debtor's attorney for services to be rendered
12 during a bankruptcy case is to be held in trust for the debtor, except to the extent that attorneys'
13 fees are allowed by the Court pursuant to Bankruptcy Code Sections 330 and 331 governing
14 compensation. Crimson, 109 B.R. at 402. Pursuant to Arizona law and the Arizona Rules of
15 Professional Conduct, property held by an attorney for the client's benefit is held in trust and
16 must be segregated. Matter of Carragher, 157 Ariz. 219, 756 P.2d 316, 319 (1988); ER 1.15,
17 Rule 42, Rules of the Supreme Court of Arizona. Therefore, a retainer received pre-petition is
18 generally estate property held in trust for the benefit of the estate. Crimson, 109 B.R. at 402. The
19 Arizona Rules of Professional Conduct also allow an attorney to charge a flat fee retainer or a
20 non-refundable retainer. Arizona Bar Ethics Op. 10–03 (June 2010); see also Arizona Bar Ethics
21 Op. 99–02 (April 1999). Nonetheless, in the context of bankruptcy, a bankruptcy court must still
22 make the determination that the debtor’s counsel is a disinterested party pursuant to § 327 and
23 that the terms and conditions of the employment are reasonable pursuant to § 328.

24 In this case, Attorney Robert Cook filed his employment application on behalf of
25 Manstone on November 11, 2009 and filed his application on behalf of the Robinsons on
26 December 18, 2009. In each of these applications, Mr. Cook disclosed that he had received
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1 \$25,000 prior to the filing of the case, but he failed to fully explain the nature of these payments
2 by omitting the fact that they were flat fees, earned upon receipt. Moreover, Mr. Cook listed
3 hourly billing rates, which indicated a fee arrangement whereby Mr. Cook would hold the
4 retainer in trust and apply for compensation with the Court. The applications also included
5 verified statements signed by Mr. Cook and notarized, attesting that Mr. Cook did not hold any
6 interests adverse to the estate. This statement was made in spite of the fact that Mr. Cook became
7 a creditor of the estate by virtue of the earned-upon-receipt nature of the funds received prior to
8 the petition date. For instance, Section 101(10)(A) states that a creditor is someone that has a
9 claim against the debtor. Section 101(5) states that a claim is a “right to payment,” whether
10 reduced to judgment, liquidated, unliquidated, fixed, matured, unmatured, disputed or
11 undisputed, etc. Although the earned-upon-receipt retainer allowed Mr. Cook to place the funds
12 in his operating account, if properly disclosed, it also triggered the Court’s requirement to review
13 the compensation “earned” to determine whether it was reasonable under Sections 328 and 329.
14 Because of Mr. Cook’s improper disclosure that he was disinterested and that he would be
15 applying for compensation during the course of the bankruptcy proceeding, he deprived the
16 Court of the ability to review and determine the reasonableness of the compensation, including
17 the earned-upon-receipt retainer that he received at the commencement of the cases.

18 Moreover, as discussed more fully in Part B of this decision, it appears that Mr.
19 Cook performed substantial pre-petition services for the Debtors that were not disclosed. In the
20 Manstone case, Mr. Cook rendered pre-petition services in the amount of \$3,560. In the
21 Robinson case, Mr. Cook rendered pre-petition services in the amount of \$10,857.50. The Court
22 would expect that these services would be paid in full, at the time of filing, in the ordinary course
23 of business to eliminate any argument that Debtors’ counsel received a preference. If Debtors’
24 counsel had an earned-upon-receipt retainer, there should have been a discussion of the payment
25 of these pre-petition services, so that the Court could determine the reasonableness of the
26 compensation requested. Mr. Cook’s improper disclosure forces the Court to conclude that Mr.

1 Cook had substantial unpaid pre-petition services in each case, at the time he received the
2 earned-upon-receipt retainers, creating a preference and adverse interest as to each estate.

3 In response to the objections of his fee applications, Mr. Cook argued that the fee
4 agreements were proper because, although the fees were earned upon receipt, the agreements
5 provided that they were refundable upon request by the debtors or by order of the court. This
6 argument misses the mark. In 2009, when Mr. Cook first applied for employment on behalf of
7 the debtors, the Court should have been able to determine whether Mr. Cook was a disinterested
8 party or had an adverse interest to the estates, as well as assess the reasonableness of the fee
9 arrangement. As noted, the Court could have assessed whether the substantial pre-petition
10 payments constituted a preference that would make Mr. Cook a creditor of the estate or have an
11 adverse interest to the estate. Such an inquiry goes to the heart of whether counsel should be
12 employed in any case. Regardless of Mr. Cook's belief that the fee arrangements were proper,
13 his failure to disclose fully the nature of the arrangements at the time of his employment
14 applications—and failure to update the Court for the three years thereafter while the cases were
15 pending—deprived the Court of a meaningful opportunity to conduct such an analysis. Therefore,
16 the Court denies all compensation of fees based on this lack of disclosure and orders Mr. Cook to
17 disgorge the \$25,000 retainer received in each case.

18 **B. Attorney Cook May Not Be Compensated for Services Performed Outside**
19 **the Approved Employment Period**

20 There are other reasons to deny the compensation requested by Mr. Cook. Mr.
21 Cook billed the debtors for significant fees and expenses both before court approval of his
22 employment as well as subsequent to his removal. Bankruptcy courts in the Ninth Circuit
23 possess equitable power to approve retroactively a professional's valuable but unauthorized
24 services. In re Atkins, 69 F.3d 970, 973-74 (9th Cir. 1995). However, retroactive approval
25 should be limited to situations in which "exceptional circumstances" exist. *Id.* To show
26 "exceptional circumstances," the professional must 1) satisfactorily explain its failure to seek
27 prior judicial approval, and 2) demonstrate that their services benefitted the estate in a significant

1 There is yet a third basis to deny any recovery by Mr. Cook. Even looking only at
2 the fees requested by Mr. Cook during the time of his employment as counsel for the debtors, the
3 Court finds that the fees listed in Mr. Cook’s applications are unreasonable. Section 330 provides
4 that a court may award “reasonable” compensation to a professional person employed under
5 § 327 for “actual, necessary services rendered.” 11 U.S.C. § 330(a)(1) (2013). A court may
6 award compensation that is less than the amount of compensation requested. § 330(a)(2). To
7 determine the amount of reasonable compensation, § 330(a)(3) provides that the court must:

8 [C]onsider the nature, the extent, and the value of such services,
9 taking into account all relevant factors, including—
10 (A) the time spent on such services;
11 (B) the rates charged for such services;
12 (C) whether the services were necessary to the administration of,
13 or beneficial at the time at which the service was rendered toward
14 the completion of, a case under this title;
15 (D) whether the services were performed within a reasonable
16 amount of time commensurate with the complexity, importance,
17 and nature of the problem, issue, or task addressed; and
18 (E) whether the compensation is reasonable based on the
19 customary compensation charged by comparably skilled
20 practitioners in cases other than cases under this title.

21 § 330(a)(3). Section 330(a)(4)(A) outlines when compensation should not be allowed. A
22 bankruptcy court examines the circumstances and manner in which services are performed and
23 results achieved to determine a reasonable fee. In re Garcia, 335 B.R. 717, 724 (B.A.P. 9th Cir.
24 2005). In making that determination, a court should consider the following questions:

- 25 (a) Were the services authorized?
26 (b) Were the services necessary or beneficial to the administration of the estate at the
27 time they were rendered?
28 (c) Are the services adequately documented?
 (d) Are the fees [requested] reasonable, taking into consideration the factors set forth in
 section 330(a)(3)?
 (e) In making the determination, the court must consider whether the professional
 exercised reasonable billing judgment.

Id. A court shall not allow compensation for unnecessary duplication of services, or services that
were not reasonably likely to benefit the debtor’s estate or necessary to the administration of the
case. § 330(a)(4)(A).

 The United States Trustee and the chapter 11 Trustees objected to the

1 reasonably of the fees requested by Mr. Cook on numerous grounds, including double
2 billing, excessive time expended, fees for work that is non-legal in nature, excessive rates, and
3 lack of competence. The Court agrees. After a thorough review of both fee applications, the
4 Court is hard pressed to approve any of the fees requested. Each application demonstrates
5 numerous billing errors, requests to be compensated on numerous occasions for the mere
6 downloading of files, the inability of counsel to prepare even basic plans of reorganization that
7 could be approved by the Court, the inability of counsel to draft disclosure statements that
8 contained adequate information, and the inability of counsel to provide services of any benefit to
9 the estates. As a result, the Court requires the disgorgement of the retainer of \$25,000 in each
10 case.

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12 V. CONCLUSION

13 Based upon the foregoing, the Court concludes that Mr. Cook has not provided a
14 basis to be compensated as counsel for the Debtors. His applications for attorneys' fees are
15 denied. Mr. Cook shall turn over the sum of \$25,000 in the Manstone estate, and the sum of
16 \$25,000 to the Robinson estate. The U.S. Trustee shall lodge an appropriate form of order.

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18 DATED this 26th day of March, 2013.

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22 Honorable Sarah Sharer Curley
23 United States Bankruptcy Judge

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26 **BNC to NOTICE**