IN THE UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF IDAHO

IN RE	)	
	)	
ALEX R. SMITH,	)	**Case No. 03-21502**
	)	
Debtor.	)	**MEMORANDUM OF**
	)	**DECISION RE:**
	)	**COMPENSATION (DEAN)**
_____	)	

INTRODUCTION

Before the Court is the chapter 7 trustee's special counsel's Application for Allowance of Compensation, Doc. No. 111 (the "Application"), and an objection thereto, Doc. No. 118 (the "Objection"). The dispute was presented at hearing on April 26, 2005. The Court has reviewed the arguments of the parties, the record, and applicable authorities. It determines that the Objection will be overruled and the Application will be granted. This Decision constitutes the Court's factual findings and legal conclusions. Fed. R. Bankr. P. 9014, 7052.

BACKGROUND AND FACTS

On September 17, 2003, Alex Smith ("Debtor") filed a voluntary chapter 13 petition. The chapter 13 trustee, C. Barry Zimmerman, sought approval of the employment of Charles R. Dean, Jr. ("Special Counsel"), to represent the interests

of Debtor and the bankruptcy estate in certain litigation (the "State Court Action"). *See* Doc. Nos. 7, 8. The application made it clear that Special Counsel was employed on a contingency fee basis. *See* Doc. No. 7 at Ex. B. (Attorney-Client Contingent Fee Retainer Agreement).

By an order entered on October 27, 2003, the Court approved the trustee's employment of Special Counsel. *See* Doc. No. 31. That order recited that "Fees and costs shall be paid as per the Fee Agreement entered into by the parties, and upon prior approval of this Court." *Id.*

On December 23, 2004, the Court denied Debtor's request to convert the case to chapter 11 and instead converted it to a chapter 7 liquidation. *See* Doc. No. 60. The chapter 13 trustee, Mr. Zimmerman, was appointed as the chapter 7 trustee ("Trustee").

Trustee sought approval of his employment of general counsel, William Appleton, *see* Doc. Nos. 66, 68, and also requested that the employment of Special Counsel be continued. *See* Doc. No. 67. Trustee noted that the litigation Special Counsel was handling was continuing as of the time of the conversion, and that "Mr. Dean will render professional services as set for [*sic*] the arrangement for compensation previously filed. Final compensation will be presented to the Court for approval." *Id.* Trustee asked that Special Counsel's "continuing employment be approved." *Id.*

An objection was made to that request. *See* Doc. No. 69.[1] In addition to his briefing, *see* Doc. No. 75, the objector expressed his concerns at a hearing on March 9, 2004. *See* Doc. No. 128 (April 26, 2005 minute entry to which the transcript of the March 9, 2004 hearing is attached) (hereafter "Transcript").

In brief, the objector was concerned that the role of Trustee's general counsel (Appleton) would be usurped by Special Counsel because the State Court Litigation, prosecuted by Special Counsel, sought to realize on the value of assets of the estate, including Debtor's equity interests in several corporations and other litigation claims. This, the objector argued, required analysis of Special Counsel's employment under § 327(a) rather than § 327(e) and thereunder presented questions of his lack of disinterestedness. Further, the objector expressed concern that, should Debtor's interests in the corporations be liquidated in the context of the litigation, Special Counsel would be seeking compensation under the Fee Agreement based on the value of those interests in addition to the value of other recoveries in the litigation. *See generally* Doc. No. 75 at 4-6, Transcript at 2-4.[2]

Trustee's general counsel advised the Court that the litigation was likely needed to liquidate the equity positions, given the nature of this case. Transcript at

---

[1] The objection was filed by creditor Joe Orsi. He was represented by the attorneys who represented the adverse parties in the litigation Special Counsel was handling for Debtor's estate.

[2] The objector raised some other concerns as well. However, they are not material to the present issues.

4-7. He supported the continuation of Special Counsel's employment notwithstanding the concerns raised by the objector. *Id.*

Special Counsel noted at that hearing

> And I would reemphasize something that Mr. Appleton just said and that is the trustee in this situation, in this case is free to sell any of the admitted assets of the estate wholly independent of the fee agreement that I currently have with the trustee and Alex Smith.
>
> If they sell his stock in Dave Smith Motors, that's fine. If they sell his stock in Frontier Leasing and Sales, that's fine. If they sell his membership interest in River Management, that's fine. That doesn't give rise to some claim by me under a fee agreement because what my fee agreement says is recovery based on the litigation. It is not simply recovering an admitted asset of the estate.

Transcript at 7-8. Debtor, through his counsel Savi Grewal, supported Special Counsel's continued employment and Trustee's request. *Id*. at 8-9.

In further argument, the objector expressed concern that, should the Trustee, independent of Special Counsel, sell equity interests of Debtor, Special Counsel would nonetheless seek compensation under the Fee Agreement for this "recovery." *Id*. at 9-10. The suggestion that he would make such a claim was flatly rejected, with Special Counsel noting that it would be "silly" for him to so contend. *Id*. at 10.

The Court overruled the objection and approved Trustee's request for continuation of Special Counsel's employment. In doing so, it noted that the approval was granted under § 327(e), rejecting the argument that it must effectively be under § 327(a) given the nature of the assets of the estate and the

nature of the litigation. Transcript at 11-12. The Court noted that Trustee retained the right to liquidate some or all Debtor's equity positions independent of the litigation, and that he had the assistance of general counsel, Mr. Appleton, in such regards. *Id*. at 12.

An order was entered granting Trustee's request. *See* Doc. No. 82. It noted that "[T]he Court's findings of fact and conclusions of law were made orally on the record." *Id.* No specific reference is made in the order to either § 327(e) or to § 328. However, as noted, the Court specifically found at hearing that the employment was under § 327(e).

Furthermore, the Court stated, in regard to the possibility of facts developing that could have an impact on whether Special Counsel remained qualified and what he might be paid:

> I've also evaluated the adverse interest, Rule 11 [and] the malpractice claims and find them not persuasive under the circumstances. Those are matters that either ordinarily arise in litigation or can be addressed by this Court in dealing with fee issues later. I have to note that there are a number of tools available. Mr. Dean I think probably is aware of this. If not, Mr. Appleton's got some additional discussion and education to give him. [I][3] have the ability under 328 of the Code to allow compensation different than compensation provided for under the agreement [i]f upon the completion of the employment it appears that such terms and conditions

[3] The Transcript indicates "they" rather than "I" which this Court believes to be a mistranscription of what it said.

> have been [improvident[4]] in light of developments and not capable of being fully anticipated at today's date. That's a tool.

Transcript at 14.

An initial attempted mediation of the State Court Action was unsuccessful, following which the Trustee accepted, subject to Court approval, a settlement offer from the state court defendants and filed a Notice of Sale and Compromise of Claim. *See* Doc. No. 88 (the "First Settlement"). The First Settlement reflected Trustee's intent and request that he be allowed to sell all the estate's interests in Dave Smith Chevrolet Oldsmobile Pontiac Cadillac, Inc. ("Dave Smith Motors"); Frontier Leasing & Sales, Inc. ("Frontier"), and River Management, LLC ("River") and "any related or affiliated entities" and to settle the estate's claims in the State Court Action for the sum of $2,000,000, with $1,000,000 to be paid immediately upon Court approval, and with a promissory note providing the remaining $1,000,000, bearing interest at 4.73% per annum and payable in monthly installments in the amount of $10,475.07.[5]

Following hearing and briefing, the Court issued on February 25, 2005, its Memorandum of Decision denying approval of the First Settlement. *See* Doc. No. 103. The State Court Action was scheduled to go to trial in May, 2005. A second

---

[4] The Transcript indicates this word was inaudible, and the Court has inserted what was said.

[5] There were other terms and conditions. They are explained at length in this Court's Memorandum of Decision denying approval of the First Settlement. *See* Doc. No. 103.

mediation session was held, resulting in a universal settlement agreement. On March 28, 2005, Trustee, now moving through Special Counsel, asked for approval of this new agreement (the "Second Settlement"). *See* Doc. No. 113. Among other things, the Second Settlement increased the immediately payable cash component from $1,000,000 to $1,400,000, and it changed the $1,000,000 unsecured note into a $1,400,000 irrevocable trust for Debtor's benefit. Several other changes and modifications were made as well. *Id.* The Court, at hearing on April 26, 2005, approved the Second Settlement.

On March 28, Special Counsel filed his Application seeking compensation based on the prior orders of the Court approving his employment and under the Fee Agreement. He claims fees should be calculated at "33.3% of the gross amount of [the] settlement reached." *Id.* at 1.[6]

Special Counsel indicates, however, that he does not seek the fee calculated against certain aspects of the settlement, specifically the debts paid or forgiven by the defendants and settling parties (who released claims of some $288,000 as a part of the agreement), certain income guaranteed to Debtor, and certain rent assistance to be paid to Debtor. *Id.* at 2. He also agrees to treat fees of Debtor's guardian ad litem (Mr. Annis) and of Debtor's bankruptcy counsel (Ms. Grewal) as costs of

[6] The Fee Agreement provides for a fee of 33.3% of gross recovery if settlement is reached prior to 30 days before the first date the case is set for trial. *See* Doc. No. 7 at Ex. B. The successful mediation here occurred in early March, and the State Court Action was scheduled for trial in May.

litigation under the Fee Agreement, and would calculate the contingency fee only on the $2,800,000 settlement amount (cash and trust) net of these fees and Special Counsel's own out of pocket costs. He asserts that the $2,800,000.00 is thus reduced by $27,202.50, and he calculates a 33.3% fee of $923,341.57 on the $2,772,797.50 net settlement balance. *Id.*

The sole objection to this Application comes from Debtor through "specially appearing counsel."[7] The Objection raises several contentions. The two primary ones are:

a. That Special Counsel calculated fees based on all amounts recovered in the Second Settlement, including the value of the "sale" of Debtor's equity positions as well as "tort-type" damages, and that "[t]o the extent amounts recovered relate to liquidation of property of the estate, [Special Counsel] has previously stated, and the Court has recognized, that [Special Counsel] would assert no claim to fees." Doc. No. 118 at Attach. 1 (Memorandum in Support of Objection), page 1. The Objection seeks a "fair and reasonable allocation" of the amounts received in settlement for the equity positions and the amounts received for tort damages, with a concomitant reduction in Special Counsel's fees. *Id.* at page 2.

[7] Debtor's counsel is Ms. Grewal. She raised no objection on Debtor's behalf. The "specially appearing counsel" indicate they were retained solely for purposes of making the objection.

b. That the fees sought by Special Counsel should be reviewed under § 330(a) for "reasonableness" rather than evaluated under § 328, in part because the order approving Special Counsel's employment did not "explicitly" state that compensation was under § 328(a). *Id.* at page 3-5.[8]

DISCUSSION AND DISPOSITION

Unlike the vast majority of fee disputes presented to this Court, sustaining the Objection here will not have an impact on creditors of this estate. The cash component of the Second Settlement is $1,400,000.00. Even if Special Counsel is allowed the $923,341.57 in fees and $17,949.76 in costs requested, $458,708.67 would be available. The Court is advised and has no reason to doubt this amount is more than sufficient to pay all known and projected administrative expenses in the chapter 7 case; all known and currently projected administrative expenses in the chapter 13 case prior to conversion; all priority claims other than administrative expenses; all creditor claims, with interest; and still leave funds to be returned to Debtor. *See generally* § 726(a)(1) through (6), § 726(b) (describing order of distribution of property of the estate).[9] The debate is essentially between

[8] Multiple and varied arguments are advanced, and the Court has evaluated them all. The Court concludes that all the additional arguments flow, to a greater or lesser degree, from the two main contentions set out above. To the extent not specifically addressed in this Decision, objections are determined to lack merit and are overruled.

[9] The Court acknowledges that certain tax issues remain potentially at issue. The record is not sufficiently developed for the Court to comment further on them.

Special Counsel and Debtor.[10] While this might be viewed by some as a dispute best reserved for nonbankruptcy venues, the fact that Special Counsel was employed by this Court and will be paid from property of the estate clearly makes it otherwise.

A. Special Counsel was employed under § 328(a) and the Fee Agreement

Section 328(a) allows the Court to approve the employment of a professional "on any reasonable terms and conditions . . . including on a retainer, on an hourly basis, or on a contingent fee basis." There is no doubt whatsoever that Special Counsel was employed on a contingency fee basis.

The initial application, Doc. No. 7, so indicates. It attached the Fee Agreement which clearly provides for a contingency fee. The order first approving Special Counsel's employment, Doc. No. 31, quoted earlier, indicates that "[f]ees and costs shall be paid as per the Fee Agreement entered into by the parties, and upon prior approval of this Court." The post-conversion pleadings changed nothing; Trustee sought approval of the "continuation" of the employment. No suggestion was made that the basis of employment or the proposed method of compensation was to be altered at all.

The Objection argues that the absence of direct and express reference to

---

[10] Recall, no creditors objected to Special Counsel's Application.

§ 328(a) in the Court's orders requires the fee agreement be set aside in favor of an analysis of the requested fees under § 330(a). The contention is based on *Circle K Corp. v. Houlihan, Lokey, Howard & Zuikin, Inc. (In re Circle K Corp.)*, 279 F.3d 669 (9th Cir. 2002), but, in advancing the arguments in this case, Debtor misreads and overly aggressively interprets that decision.

Circle K set the stage this way:

> This appeal presents the question of how a professional employed in the course of a Chapter 11 bankruptcy proceeding can be assured that its fees will be reviewed under the standards of 11 U.S.C. § 328, rather than § 330. Section 328(a) permits a professional to have the terms and conditions of its employment pre-approved by the bankruptcy court, such that the bankruptcy court may alter the agreed-upon compensation only "if such terms and conditions prove to have been improvident in light of developments not capable of being anticipated at the time of the fixing of such terms and conditions." In the absence of preapproval under § 328, fees are reviewed at the conclusion of the bankruptcy proceeding under a reasonableness standard pursuant to 11 U.S.C. § 330(a)(1).

279 F.3d at 671. The court of appeals held that:

> unless a professional's retention application unambiguously specifies that it seeks approval under § 328, it is subject to review under § 330. As a matter of good practice, the bankruptcy court's retention order should likewise specifically confirm that the retention has been approved pursuant to § 328 so as to avoid any ambiguity. The absence of such a specific reference in the bankruptcy court's order, however, would not of itself automatically override the retention application's invocation of § 328.

Id. In a footnote, the court elaborated "Our point is merely that if a professional's application cites § 328 and the bankruptcy court's order otherwise makes clear that

the retention has been approved pursuant to § 328, we will consider § 328 to apply even if the retention order does not specifically reference that section." *Id.* at n.2.

After considering the applications and orders at issue in that case, the court summarized its holding again:

> In this Circuit, unless a professional is unambiguously employed pursuant to § 328, its professional fees will be reviewed for reasonableness under § 330. To ensure that § 328 governs the review of a professional's fees, a professional must invoke the section explicitly in the retention application. Preferably, the retention order would specify that section as well.

Id. at 674. Again the court elaborated through a footnote:

> Once again, we encourage bankruptcy courts to identify clearly which statutory provision applies to a professional's retention. Of course, failure to cite either § 330 or § 328 is not fatal, as the context of the retention order should ordinarily make clear which provision is applicable.

Id. at n.5.

In the Court's view, there is no ambiguity at all in the method and basis of Special Counsel's retention.[11] It was based on the contingency fee agreement attached to and expressly referred to in the first application, Doc. No. 7. The

---

[11] Unlike the instant case, an ambiguity did exist in *Circle K*. There the financial advisors to the unsecured creditors committee were employed under a retainer agreement providing for a fee of $100,000 per month plus expenses. The agreement acknowledged it was subject to court approval and that "[a]ll fees so paid remain subject to subsequent Bankruptcy Court approval in a final fee application to be submitted to the Court." Neither the application nor order mentioned § 328. The bankruptcy court reviewed the fees under § 330, and even stated, following an intermediate remand from the district court, that its intent had been to approve the retention under § 330. Under the circumstances there, it was entirely possible that the retention was under § 330, and the monthly payments were subject to later review for reasonableness. Here, the compensation basis was never ambiguous: it was at all times a contingency fee.

Order approving his employment, though not citing § 328, stated that "[f]ees and costs shall be paid as per the Fee Agreement entered into by the parties, and upon prior approval of this Court."

When the post-conversion continuation of employment of Special Counsel came before the Court, there was no suggestion at all that the terms and conditions of employment would be changed. To the contrary, it was at all times characterized as a "continuation" of the earlier approved employment. In fact, the understanding that the contingency fee agreement was the basis upon which Special Counsel would be compensated was directly at issue under the Orsi objection, and was argued extensively at the March 9 hearing. In passing on the objection, this Court specifically invoked § 328 and recited the language of that section. *See* Transcript at 14.

Finally, lest there be any confusion or debate about the Court's intent in approving the employment of Special Counsel, it was done on a contingency fee basis under § 328(a) of the Code. That was its intent at the time employment was initially approved and, as seen in the Transcript, this was its intent at the time of the continuation.

Circle K, fairly read, does not support Debtor's arguments. The absence of direct citation to § 328(a) in the order, though obviously now regretted by the Court as such a citation likely would have mooted this debate, does not have the

talismanic effect Debtor believes it to have. The section citation need not be invoked if the actions of the Court are otherwise clear. In this case, they are.[12]

B. The developments in the case do not provide reason or cause to vary the operation of the Fee Agreement

Now that it is clear that compensation flows under § 328(a) and not § 330, the Court must determine whether it should allow compensation different from that provided for under the terms and conditions in the agreement on the basis that such terms and conditions have proven to be improvident in light of developments not capable of being anticipated at the time Special Counsel's employment was approved. *See* § 328(a).

Having reviewed all submissions and arguments, and the entirety of the record, the Court cannot reach the conclusion that § 328(a)'s standard for altering the method of compensation has been met.

Debtor argues that Trustee's lack of effort to independently market Debtor's equity positions somehow qualifies as a development not anticipated at the time Special Counsel's employment was approved. *See* Doc. No. 118 at

[12] One other point: Debtor was a participant throughout this matter. The original application to employ Special Counsel was advanced with the assistance of Debtor's attorney, Mr. Garbrecht. The continuation of Special Counsel's employment generated no objection by Debtor, then represented by Ms. Grewal. The Court strongly questions the propriety of Debtor now raising the § 328 arguments through his new, "specially appearing" counsel. However, as the Objection is not well taken on the merits, and because the Court deems it appropriate to further explain its prior orders in light of the suggestion that *Circle K* was violated, it need not reach the possible issues of Debtor's standing to object or judicial estoppel.

Attach. 1 (Memorandum), page 6-7. However, at all times the litigation included claims for the value of those interests as well as claims for damages for actions taken in connection with those interests. *See* Doc. No. 7 at Ex. A (copy of first amended complaint). The possibility of a settlement that dealt with the transfer of those interests was reasonably capable of being anticipated. The Court finds it hard to believe that Debtor should now be heard to say "Well, I assumed that the trustee would try harder to sell the corporate stock and LLC membership, separate and apart from the litigation Mr. Dean was prosecuting, and reduce the amount of the fee I'd have to pay Mr. Dean. How was I to know the trustee wouldn't do that?"

In point of fact, the issue of such "separate" sale by Trustee *was* raised. This occurred at the time of hearing on the continuation of employment in March, 2004. The portions of that hearing, set out earlier, make it exceedingly clear, at least to this Court, that no fee would be claimed by, or owed to, Special Counsel if Trustee found a buyer for some or all of the equity positions and sold them outside the state court litigation process.

In addition, Trustee through Mr. Appleton articulated a view that the lawsuit was most likely necessary to effect a "sale" of those assets, and that the assets might not be capable of separate or independent marketing. *See* Transcript at 5-6. Knowing this, and knowing therefore that there might not be a "separate"

sale, Trustee still urged the approval of employment under the contingency fee arrangement. Debtor appeared at that hearing through his counsel and raised no objection.

That the ultimate resolution of the litigation might include conveyance of Debtor's equity interests to the state court defendants was not beyond anticipation. A "universal" settlement of the disputes here existing might not have been possible, or at least very likely, without it. Special Counsel's efforts resulted resolution in the realization of value from both the litigation and the equity interests. The Fee Agreement applies.

Finally, the Court specifically rejects Debtor's characterization that Special Counsel "previously stated, and the Court has recognized, that [special counsel] would assert no claim to fees" to the extent the amounts recovered in the litigation related to liquidation of property of the estate. Doc. No. 118 at Attach. 1, page 1. The characterization is belied by what was actually said by both Special Counsel and the Court, as quoted above.

CONCLUSION

Based on the foregoing and the entirety of the record in this case, the Court concludes that the Objection is not well taken, and it will be overruled. Special Counsel's Application, Doc. No. 111, will be granted and approved under § 328(a). The Court will enter an order in accord with this Decision.

DATED: May 12, 2005

TERRY L. MYERS
CHIEF U. S. BANKRUPTCY JUDGE

CERTIFICATE RE: SERVICE

A "notice of entry" of this Decision, Order and/or Judgment has been served on Registered Participants as reflected by the Notice of Electronic Filing. A copy of the Decision, Order and/or Judgment has also been provided to non-registered participants by first class mail addressed to:

William M. Appleton
Attorney at Law
924 Sherman Avenue
Coeur d'Alene, ID 83814

Alex R. Smith #63340
ICIO-B1
Hospital Drive North #23
Orofino, ID 83544

Bruce A. Anderson
ELSAESSER JARZABEK ANDERSON MARKS
ELLIOTT & McHUGH
1400 Northwood Ct., Suite C
Coeur d'Alene, ID 83814

Case No. 03-21502-TLM (Alex R. Smith)

Dated: May 12, 2005

/s/Jo Ann B. Canderan
Judicial Assistant to Chief Judge Myers