UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In re

MIANO SAMS'SONS ENTERPRISES,
INC. d/b/a OLD MAN RIVER Case No. 97-17101

Debtor

Before the Court is the Debtor's application to approve the employment of its attorney. Such employment would require retroactive approval because the case was filed on November 12, 1997, and the application to employ was dated January 23, 1998, and was not heard until March 18, 1998. The United States Trustee opposes the Debtor's application, questioning the source of payment of Debtor's attorneys fees and whether the Debtor has shown the "excusable neglect" necessary for retroactive approval of employment of counsel. The Court has approved his representation prospectively, pending this decision.

There are three issues before the Court with respect to Mr. Fiorella's representation of the Debtor in this case:

(1) May Mr. Fiorella keep several thousands of dollars that he received as payment in connection with this case, from the party who is expected to fund the Debtor's reorganization (of presently unknown benefit to unsecured creditors), which receipt was not disclosed until after the U.S. Trustee discerned that the Debtor had received and disbursed such

funds without authority?

(2) May he continue to represent the Chapter 11 Debtor despite having been so compensated?

(3) May his application be approved retroactively in light of *In re Piecuil,* 23 B.R. 888 (Bankr. W.D.N.Y. 1992)?

I

Mr. Fiorella argues that the payment of his fees by an investor of the Debtor does not cause him to have "an interest materially adverse to the Debtor."

Although Mr. Fiorella relies heavily on *In re Kliegel*, 189 B.R. 874 (E.D.N.Y. 1995), that case has no application here. In *Kliegel*, counsel's dual representation of the debtor and the postpetition lender was fully disclosed in the retention application and was approved without objection. Section 328 was at issue there, not § 327. Here we have opposition to such dual representation, and that opposition is sustained.

I will not approve such representation in the absence of extraordinary circumstances that favor unsecured creditors in the case. Even if the payment from the financier had been disclosed (and I will chalk up the failure to disclose it to a good faith belief that it need

not be disclosed[1]), creditors trust that integrity will be upheld here; they cannot be assured of such integrity when the Chapter 11 Debtor's counsel, who is supposed to be counseling the Debtor's principal to obtain the best possible deal from the financier for creditors in the case, is also receiving payment from the financier. (The same would be true if the "adversary" were a purchaser of assets of the Chapter 11 estate, rather than a financier.)

Although it is easy to argue that what is commonly known in Chapter 11 jargon as an "angel" is never adverse to the estate, and that anything that the Debtor's counsel might do to encourage an "angel" is always good for creditors, there is a point at which the argument is fallacious at best, and disingenuous at worst. When it gets to the point that the "devil is in the details," the Debtor's counsel must be unequivocally urging detail that favors creditors, not the financier. Furthermore, there must never be a monetary incentive for a debtor's counsel to avoid seeking an even more generous "angel." It is beyond cavil that when the client is broke and the "angel" is footing counsel's bill, such an incentive is present, unless the money is going to the estate, and unless counsel will only seek allowance for the work he or she is doing for the Debtor.

If Mr. Fiorella wishes to keep the payment he received from the financier, he shall withdraw from representation of the Debtor and shall forfeit all compensation that he has received or would otherwise claim from the Debtor's estate.

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[1]Attention is called to the very recent felony convictions of a Milbank Tweed attorney for failure to disclose representation of a creditor's principal when obtaining employment of the debtor in the Bucyrus Erie Chapter 11 case.

II

If Mr. Fiorella wishes to continue to represent the Debtor he must return the payment to the financier and refuse any further payment other than as allowed by this Court.

III

As to the retroactive approval of Mr. Fiorella's employment, this writer disagrees with ¶ 11 of Mr. Fiorella's affidavit of 3/23/98. He states therein that "Deponent does not nor has never [sic] represented the investors herein nor any creditors of the Debtor. Deponent only represents the Debtor's estate."

For the reasons set forth in Section I above, that representation splits a hair far too thin; when one takes funds from an investor to represent a debtor who otherwise has no funds to pay, one does not only represent the Debtor's estate. (Indeed, we have yet to see how any of this will benefit creditors as opposed to the Debtor's current owner.)

Mr. Fiorella consequently fails to satisfy that prong of *Piecuil* that requires that he show that his representation would have been approved if approval had been timely sought. In

light of the fact that he was paid by the investor to file the petition, a timely application would not have been approved.[2] (Indeed, it is quite likely that this writer would not have approved the employment that another judge did approve in *Kliegel*, that eventually led to the § 328 decision cited by Mr. Fiorella.)

CONCLUSION

Regardless of what he elects to do as to the moneys received directly or indirectly from the investor, Mr. Fiorella may not receive retroactive appointment as attorney for the Debtor. If he wishes to continue to represent the Debtor, he must return the monies to the investor and forfeit any claim to compensation for any work done heretofore. (A secret agreement to the contrary would constitute a felony under 11 U.S.C. § 152.)

If he instead elects to rest satisfied with only what he has already received from the investor, he is immediately disqualified as counsel and the Debtor shall promptly obtain other counsel. He shall decide by writing filed on or before April 10, 1998.

A final word as to disclosure. Disclosure can be everything. This writer has

[2]The proper way to have handled this matter would have been for the investor to put up a retainer, for counsel to disclose that source on his rule 2016(b) statement, and for counsel to make application for fees in due course, only under 11 U.S.C. § 330 or § 331.

approved otherwise unthinkable representation in highly specialized circumstances, when conflicts were fully disclosed, heard, and ruled upon, in advance. Such circumstances have included a debtor's inability to obtain other competent counsel on terms that benefit creditors, and the presence of issues that require special expertise not possessed by other local counsel who also are not similarly conflicted. Bring the potential conflicts promptly before the Court, and they might not prove to be a problem. Further, if it would be detrimental to creditors not to be flexible, the Court will be flexible within the limits of its discretion. (But only if the detriment to unsecured creditors is "clear.")

SO ORDERED.

Dated: Buffalo, New York
March 31, 1998

/s/ Michael J. Kaplan
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U.S.B.J.