

Property of the Estate
Attorney possessory lien
Attorney compensation

George Nelson, Case No. 04-70024-fra7

7/12/2007 FRA

Unpublished

Debtor's attorney held in his trust account a retainer in the amount of \$31,332. Trustee filed a motion seeking an order requiring the turnover of these funds. The attorney opposed Trustee's motion and renewed his motion for leave to apply the funds toward earned fees exceeding \$40,000.

The attorney fees incurred by Debtor's attorney were incurred while the case was in chapter 11. The bankruptcy court ruled that the funds held by Debtor's attorney were property of the estate, but were subject to the attorney's possessory lien under state law. The court distinguished the present case from In re Dick Cepek, Inc., 339 B.R. 730 (9th Cir. BAP 2006) (case remanded for determination whether there was adequate disclosure by attorney of retainer), by noting that Debtor's attorney had made adequate disclosure of the fact that he held funds in his trust account intended to secure payment of his fees.

The court had previously denied the attorney's motion for an order approving compensation on the grounds that there was a dispute between the Trustee and the Debtor over the Debtor's right to the use of the funds, and the matters should be determined in a single proceeding. The bankruptcy court revisited the issue of fees in the present matter and determined that the attorney was entitled to fees in the amount of \$25,000. Trustee had argued that the attorney should receive minimal fees because the chapter 11 case was hopeless from the onset. The court, however, felt the attorney was entitled to fees in his attempt to rescue the Debtor's business, but that he was not entitled to compensation once the reorganization was determined to be hopeless.

Debtor's attorney was ordered to turn over to the Trustee the amount of the retainer held in his trust account in excess of \$25,000.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

In re:) Bankruptcy Case
) No. 04-70024-fra7
GEORGE G. NELSON,)
) MEMORANDUM OPINION
)
Debtor.)

Debtor's attorney holds in his trust account a retainer of \$31,332.75. The trustee has filed a motion seeking an order requiring turnover of these funds. The attorney opposes the motion, and has renewed his motion for leave to apply these funds toward earned fees exceeding \$40,000.00. For the reasons that follow, the trustee's motion is denied, and the attorney's motion is allowed in part and denied in part.

I. BACKGROUND

The funds in question were delivered to the attorney by the debtor. The debtor received these funds as proceeds of loans from one or more affiliates. In August of 2005 the court denied, without prejudice, a motion seeking approval of the attorney's Chapter 11 fees and leave to apply the retainer because there was a dispute between the trustee and the debtor over the debtor's right to use the funds. The trustee at the

1 time argued that the funds were either not property of the estate at all,
2 and thus not available to the attorney, or that the transfer of the funds
3 to the debtor, and thereafter to his attorney, was avoidable. The court
4 held that "Whatever the merits of these assertions, they must be
5 determined in an adversary proceeding." In re Nelson, Case No.
6 04-70024-fra7 (Bankr. D.Or. 8/16/05).

7 The court's opinion notwithstanding, the parties again seek to
8 establish control over the funds through motion practice. It is sorely
9 tempting to say no once again, and deny all pending motions in favor of
10 the yet to be instituted adversary proceeding. However, the court
11 believes that it has sufficient information upon which to rule, that all
12 parties are subject to the court's *in personam* jurisdiction, and that the
13 interests of justice and judicial economy will be best served by dealing
14 with the matter directly, notwithstanding the case's procedural defects.

15 II. DISCUSSION

16 1. **The funds in the attorney's trust account are property of**
17 **the estate.** Property of the estate is defined by Code § 541, and
18 includes all property of any sort in which the debtor has an interest.
19 The funds delivered from Mr. Nelson to his attorney were proceeds of a
20 loan. That does not mean that the money was not the debtor's to deliver.
21 Once the money was lent to him, it was, at least as far as this record
22 reflects, his to do with as he saw fit. The fact that there is an offset
23 in debt does not alter the debtor's property rights in the case. The
24 transfer of the funds to the trust account subjected the funds to an
25 attorney's lien, as will be discussed below, but did not alter the
26 essential character of the cash as property of the debtor, and

1 subsequently property of the debtor's estate. It follows that the
2 property is subject to turnover pursuant to Code § 542, absent some
3 intervening right, such as a valid lien.

4 **2. Counsel's disclosure was not inadequate.** It is intimated
5 in the trustee's turnover demand that the attorney's application for
6 compensation is misleading insofar as it provides that no payments were
7 made to the applicant by any third party. While there may be some
8 ambiguity in this context, there is no reason to believe that counsel
9 intended to mislead. There is a distinction to be made between a payment
10 directly from a third party or affiliate, and the application by a debtor
11 of proceeds from a third party. In any event, the court is duly advised
12 in this situation, and finds that there is no occasion to penalize
13 counsel for a confusion.

14 **3. Debtor's attorney is entitled to a possessory lien under**
15 **Oregon law.** ORS 87.430 provides as follows:

16 An attorney has a lien for compensation whether
17 specially agreed upon or implied, upon all papers,
18 personal property and money of the client in the
19 possession of the attorney for services rendered to the
20 client. The attorney may retain the papers, personal
21 property *and money* until the lien created by this
22 section, and the claim based thereon, is satisfied, and
23 the attorney may apply the money retained to the
24 satisfaction of the lien and claim.

25 The court has previously indicated that the money held by the
26 attorney was the debtor's money. It is undisputed that it is in the
27 attorney's possession. It follows that the funds are subject to the
28 attorney's possessory lien created by state law. The Bankruptcy
29 Appellate Panel has held that the estate and administrative claimants
30 cannot look to encumbered property to satisfy their claims. In re Dick

1 Cepek, Inc., 339 B.R. 730, 737 (9th Cir. BAP 2006). In this case, unlike
2 Dick Cepek, Inc., there was adequate disclosure of the fact that debtor's
3 attorney held funds in his trust account intended to secure payment of
4 his fees. The resulting lien exists as a matter of law. While the court
5 may have the authority to reject the arrangement, *id.* at 741 (Pappas,
6 concurring), that authority should, as a rule, be exercised at the time
7 the attorney is employed, rather than after the work has been done and
8 the fees earned.

9 4. **Debtor's counsel is entitled to compensation.** Both the
10 trustee and the principal creditor in this case argue that the debtor's
11 attorney should somehow be penalized because, as the trustee puts it, the
12 case should have never been filed in the first place.

13 It is clear from the record before the court that this Chapter
14 11 case was commenced in an effort to bring Iskum, debtor's principal
15 creditor, to the bargaining table. At the time the case had been
16 commenced, debtor was subject to an eviction judgment of the state court.
17 There was no reasonable prospect of any relief from the bankruptcy court,
18 given the termination and forfeiture of the debtor's lease. Indeed, on
19 at least one occasion, debtor's counsel readily agreed with this
20 proposition. The case was a last ditch effort to rescue the debtor's
21 business, and the only prospect of reorganization depended on the
22 acquiescence of the landlord/creditor. When it became clear that this
23 cooperation would not be forthcoming, the attempt to reorganize
24 collapsed, and the case ultimately was converted to one under Chapter 7.

25 The trustee and creditor effectively seek to sanction debtor's
26 attorney for engaging in this sort of desperate tactic. The court has

1 previously declined to impose sanctions under Rule 9011, and declines to
2 do so now in the guise of an attack on the debtor's attorney's fees. It
3 is argued that the value of the services of the debtor's attorney must be
4 measured by the benefit of the services to the estate. This is a fine
5 concept in the abstract, but overlooks the fact that attorneys are hired
6 by debtors for the purpose of pursuing the debtor's interest in
7 preserving the debtor's financial position. Debtor's counsel is
8 obligated to render advice in accordance with the client's expressed
9 needs (within, of course, the boundaries of the law) and is obligated to
10 pursue the debtor's interest even where they may be inimical to those of
11 particular creditors, or of creditors generally.

12 This case is, it must be admitted, a close one. However, the
13 court does not accept the premise that, having elected to engage in--to
14 say the least--hardball tactics, debtor's counsel forfeits any right to
15 compensation. If that were the case, debtors' attorneys would be
16 deterred from taking aggressive positions on behalf of their clients for
17 fear of being penalized for failing to identify a particular creditor's
18 unwillingness to negotiate.

19 5. **\$25,000.00 is a reasonable fee under the circumstances of**
20 **the case.** The court has reviewed the fee application. There appears to
21 be no particular entry that is untoward, and there is no suggestion that
22 the time claimed was not spent, or that the rate charged is unreasonable.
23 However, Iskum opposed the bankruptcy proceeding at every turn, and made
24 it unmistakably clear to the debtor and his counsel that it would not
25 contemplate further business dealings with the debtor. While counsel
26 should not be penalized for electing the strategy he did, neither should

