NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re:	BAP No. NC-07-1240-KJuMk
3DFX INTERACTIVE, INC.,	Bk. No. 02-55795
Debtor.	
ADORNO & YOSS LLP,	
Appellant,	
v.	**MEMORANDUM**[*]
UNITED STATES TRUSTEE; OFFICIAL COMMITTEE OF EQUITY SECURITY HOLDERS; OFFICIAL COMMITTEE OF UNSECURED CREDITORS; WILLIAM A. BRANDT, JR., Trustee; NVIDIA CORP.; 3DFX INTERACTIVE, INC.,	
Appellees.	

Argued and Submitted on January 24, 2008
at San Francisco, California

Filed – February 6, 2008

Appeal from the United States Bankruptcy Court
for the Northern District of California

Honorable Roger L. Efremsky, Bankruptcy Judge, Presiding

Before: KLEIN, JURY and MARKELL, Bankruptcy Judges.

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[*]This disposition is not appropriate for publication. Although it may be cited for whatever persuasive value it may have (see Fed. R. App. P. 32.1), it has no precedential value. See 9th Cir. BAP Rule 8013-1.

This is an appeal from an order disqualifying appellant as special counsel to the chapter 11 Official Committee of Unsecured Creditors due to a conflict of interest arising out of appellant's representation of a creditor and named defendant in a fraudulent conveyance action brought by the trustee in the same bankruptcy case. Appellees, the Official Committee of Equity Security Holders and the United States Trustee, contend that appellant's concurrent representation violated 11 U.S.C. § 1103(b) and California State Bar Rule of Professional Conduct 3-310. We AFFIRM.

FACTS

On October 15, 2002, debtor 3dfx Interactive, Inc. filed for chapter 11 bankruptcy relief. Subsequently, the Office of the United States Trustee appointed the Official Committee of Unsecured Creditors ("Committee") and the bankruptcy court appointed a chapter 11 trustee.

A. Adorno's Employment

On January 9, 2004, the bankruptcy court approved employment of Sedgwick, Detert, Moran & Arnold LLP ("Sedgwick") as attorneys to the Committee.

Due to a potential conflict that existed between Sedgwick and the Committee in an upcoming mediation of litigation involving the debtor's trustee, nVidia Corporation, and others, Sedgwick asked appellant Adorno & Yoss LLP ("Adorno") to serve as special conflicts counsel for the Committee.

On February 1, 2005, the bankruptcy court granted Sedgwick's application for order approving employment of Adorno as special counsel to the Committee to participate in and advise the Committee on the mediation.[1] In support of the employment application, Charles M. Tatelbaum of Adorno filed a declaration disclosing that he represented Avnet, Inc., one of the debtor's creditors and the chair of the Committee, for many years.[2] Tatelbaum also declared that he would file supplemental declarations as needed to disclose any other relevant connections.

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[1]Specifically, the Committee requested an order under § 1103(a) authorizing the Committee to retain Adorno as special counsel to perform the following services, among others:

> (a) preparing for and attending the February 10 mediation on behalf of the Committee;
> (b) advising the Committee on the results of the mediation or any settlement that is obtained thereafter; and
> (c) attending to any necessary follow-up or other required action in response to the outcome of the mediation.

Application for Order Approving Employment of Adorno & Yoss as Special Counsel for the Official Committee of Unsecured Creditors at 4:26-5:5.

[2]In his declaration, Tatelbaum disclosed:

> For many years I represented Avnet, Inc. one of the creditors in this case, and whose representative serves as Chair of the Committee. The representation of Avnet has included general legal advise [sic], the defense and prosecution of contract claims and the defense of bankruptcy preference claims.

Decl. of Charles M. Tatelbaum in Support of Application for Order Approving Retention of Adorno & Yoss, LLP as Counsel for the Official Committee of Unsecured Creditors at 5:6-9.

On behalf of the Committee, Adorno attended the mediation session that sought a global settlement of the bankruptcy case on February 10, 2005. Adorno remained involved throughout that year in the mediation process, which culminated in a vote by the Committee on November 1, 2005, to approve a settlement. As the bankruptcy court noted, the docket indicates that until at least July 2006, Adorno continued to do work for the Committee which was not limited to the mediation.[3]

B. The Avnet Action

In October 2004, the trustee filed numerous fraudulent conveyance actions (collectively referred to as the "STB Actions" by the trustee), including one against the predecessor to Avnet, Inc.[4] Avnet, a member of the Committee, is represented by Adorno. A default judgment was entered against Avnet's predecessor in March 2005.

According to Tatelbaum, he first learned of the default judgment on March 31, 2005. Thereafter, on May 3, 2005, Tatelbaum, on Adorno's behalf, and the trustee's counsel stipulated to set aside the default judgment and allow the trustee to amend the complaint to name Avnet as a defendant.

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[3]In July 2006, Adorno represented the Committee in filing an opposition to the motion of Zoran Corporation to deem its claim timely filed. The court noted that this "belies Adorno's contention that it was retained only for the purpose of attending the mediation and then departed from the case." Mem. Decision at 9:5-7.

[4]Kent Electronics Corporation was predecessor to Avnet. Avnet had purchased the stock of Kent in 2002, and subsequently had merged Kent into Avnet.

Tatelbaum also declared that it was his understanding and belief based on email and facsimile correspondence in April 2005 that the trustee's adversary proceeding against Avnet was to be held in abeyance once the amended complaint was filed until the conclusion of the mediation.

On May 11, 2005, the trustee filed an amended complaint naming Avnet, which sought to avoid and recover for the benefit of the estate an alleged fraudulent conveyance of $902,619.74 ("Avnet Action").

Adorno's response to the amended complaint was due June 13, 2005, as required by the court's October 2004 scheduling order for the STB Actions. A series of emails between the trustee's counsel and Tatelbaum ensued over a period of several months revealing that an answer had to be filed on behalf of Avnet in the trustee's litigation in compliance with the Federal Rule of Civil Procedure 26 "meet and confer" and initial disclosure requirements, regardless of whether the STB Actions were to be held in abeyance pending the nVidia settlement discussions.

In summary, the bankruptcy court noted that the email correspondence provided by the Official Committee of Equity Security Holders ("Equity Committee") in its Reply Brief indicated the following:

> Adorno promised to respond by the end of the week of June 20, 2005 -- which it did not do. It also indicates that when no response had been filed by September 16, 2005 and Adorno had failed to serve its Rule 26 initial disclosures as it had agreed by August 31, the Trustee threatened to take Avnet's default.

Mem. Decision at 5:7-11.

After months of postponing, on September 21, 2005, Adorno defended Avnet by filing an answer, which denied all allegations of trustee's amended complaint and asserted twenty-three affirmative defenses.

C. Disqualification of Adorno

On December 20, 2005, Adorno was replaced by another law firm in the Avnet Action.

On November 22, 2006, the Equity Committee filed its motion to disqualify Adorno from its Committee representation. The United States Trustee ("UST") filed its motion to disqualify Adorno on January 12, 2007. Both appellees, the Equity Committee and the UST, contend that Adorno should be disqualified for violating § 1103(b) and Rule 3-310.

In opposition, Adorno argued that there was no conflict of interest in violation of § 1103(b) or violation of Rule 3-310 and that the Equity Committee and the UST lacked standing to seek disqualification of Adorno.

On June 1, 2007, the bankruptcy court granted appellees' motions disqualifying Adorno as special counsel to the Committee.[5] It concluded that once Adorno acted on behalf of Avnet in the Avnet Action, it had a disqualifying adverse interest under § 1103(b) and Rule 3-310. Adorno's defense of Avnet, if successful, would be detrimental to the interests of the Committee.

[5]The court noted that it would not then rule on the UST's request that fees paid to Adorno be disgorged, and that such a request would be considered if and when the UST (or other interested parties) filed a separate motion.

Adorno's timely appeal ensued.

According to the Panel's September 25, 2007, order granting the third motion for extension of time for Adorno to file its opening brief, the issue regarding finality of the order on appeal and leave to appeal, raised sua sponte by the Panel, remains unresolved.[6] Although Adorno responded to this issue in its memorandum of law on August 7, 2007, the Panel ordered that the parties address this issue further in their appellate briefs.

JURISDICTION

The bankruptcy court had jurisdiction via 28 U.S.C. § 1334. We have jurisdiction under 28 U.S.C. § 158(a)(1).

ISSUES

(1) Whether the appeal from an order disqualifying counsel is final or whether leave to appeal should be granted.

(2) Whether the court erred in holding that a conflict of interest existed under § 1103(b) and California Rule of Professional Conduct 3-310 requiring disqualification of Adorno.

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[6]On July 25, 2007, the Panel ordered the appellant Adorno to file a written response explaining how the order on appeal was final and immediately reviewable under § 158(a)(1) or file a motion for leave to appeal. Adorno filed its memorandum of law responding to the issue on August 7, 2007.

Thereafter, due to settlement negotiations underway, three stipulations to extend the time for Adorno to file its opening brief were granted on August 8, 2007, August 28, 2007, and September 25, 2007, ultimately allowing Adorno until October 9, 2007 to file its opening brief, including further discussion of the finality issue.

(3) Whether the court erred in holding that the Equity Committee and the UST had standing to seek disqualification of Adorno.

STANDARDS OF REVIEW

The trial court's decision ordering disqualification of counsel generally will not be reversed unless the court either misperceives the relevant rule of law or abuses its discretion. Paul E. Iacono Structural Eng'r, Inc. v. Humphrey, 722 F.2d 435, 438 (9th Cir. 1983). An order disqualifying an attorney will not be disturbed if the record reveals "any sound" basis for the court's action. Id.

We review issues of statutory construction, including interpretation of provisions of the Bankruptcy Code, de novo. Einstein/Noah Bagel Corp. v. Smith (In re BCE W., L.P.), 319 F.3d 1166, 1170 (9th Cir. 2003); Mendez v. Salven (In re Mendez), 367 B.R. 109, 113 (9th Cir. BAP 2007). The bankruptcy court's interpretation of state law is also reviewed de novo. Conestoga Servs. Corp. v. Exec. Risk Indem., Inc., 312 F.3d 976, 981 (9th Cir. 2002); State Bd. of Equalization v. Leal (In re Leal), 366 B.R. 77, 80 (9th Cir. BAP 2007).

The bankruptcy court's findings of fact are reviewed for clear error, and conclusions of law are reviewed de novo. Wechsler v. Macke Int'l Trade, Inc. (In re Macke Int'l Trade, Inc.), 370 B.R. 236, 245 (9th Cir. BAP 2007). We review mixed questions of law and fact de novo. Id.

DISCUSSION

Before turning to the merits of this appeal regarding Adorno's disqualification as special counsel to the Committee, we must first address the jurisdictional issue of the finality of the order on appeal or whether to grant leave to appeal.

I

Generally, an order disqualifying or refusing to disqualify counsel is considered interlocutory. Stanley v. S.S. Retail Stores Corp. (In re S.S. Retail Stores Corp.), 162 F.3d 1230, 1232 (9th Cir. 1998). See also In re Devlieg, 56 F.3d 32, 34 (7th Cir. 1995). Appeal of an interlocutory order requires leave of the Panel. 28 U.S.C. § 158.

The Ninth Circuit has adopted the pragmatic approach to finality in bankruptcy cases, according to which an order is final and thus appealable if it: (1) resolves and seriously affects substantive rights and (2) finally determines the discrete issue to which it is addressed. Schulman v. California (In re Lazar), 237 F.3d 967, 985 (9th Cir. 2001).

Finality in the bankruptcy context does not require complete adjudication of the underlying bankruptcy case but rather only of the given issue. See e.g., Brown v. Wilshire Credit Corp. (In re Brown), 484 F.3d 1116, 1121 (9th Cir. 2007) ("a complete act of adjudication need not end the entire case, but need only end any of the interim disputes from which an appeal would lie"), quoting Slimick v. Silva (In re Slimick), 928 F.2d 304, 307 n.1 (9th Cir. 1990). Moreover, flexibility of the finality test in the bankruptcy context has allowed some courts to conclude that a

disqualification order is a final judgment. See e.g., In re Albright, 95 B.R. 560 (N.D. Ill. 1989).

Adorno argues that the bankruptcy court order should be deemed a final order because the order resolved the substantive issue under Lazar by stating that, "Adorno is therefore disqualified as special counsel for the Creditors' Committee." Mem. Decision at 13:28-14:1.

In addition, Adorno contends that finality is addressed because there is no risk of the issue coming up on appeal again. See e.g., Silver Sage Partners, Ltd. v. City of Desert Hot Springs (In re City of Desert Hot Springs), 339 F.3d 782, 788 (9th Cir. 2003) (traditional finality concerns dictate the avoidance of a case making two complete trips through the appellate process). Adorno asserts that its representation of Avnet in the fraudulent conveyance action and its representation of the Committee in the mediation have both concluded on their own right.

We agree that the order disqualifying Adorno as special counsel to the Committee was a final order. Accordingly, we have appellate jurisdiction to review the order under § 158(a)(1).

Alternatively, if the order is interlocutory, and no motion for leave to appeal has been filed, we can consider a timely notice of appeal to be a motion for leave, which we would grant. See Fed. R. Bankr. P. 8003(c); Pfeiffer v. Couch (In re Xebec), 147 B.R. 518, 522 (9th Cir. BAP 1992). Although Adorno did not file a motion for leave to appeal, it filed a timely notice of appeal. Thus, we nevertheless have appellate jurisdiction to review the order under § 158(a)(3).

II

The bankruptcy court concluded that Adorno's conduct on behalf of Avnet in the Avnet Action while still representing the Committee in the mediation constituted a disqualifying adverse interest under § 1103(b) and Rule 3-310 because Adorno's defense of Avnet, if successful, would be detrimental to the interests of the Committee.

We examine Adorno's conduct under applicable federal and state law in turn.

A

In pertinent part, § 1103(b) provides that an attorney employed to represent the Official Committee of Unsecured Creditors in the bankruptcy case may not, while employed by such committee, represent any other entity having an adverse interest in connection with the case. Congress qualified this with a 1984 amendment: "Representation of one or more creditors of the same class as represented by the committee shall not per se constitute the representation of an adverse interest." 11 U.S.C. § 1103(b).

The stakes in the "adverse interest" calculus are high because the representation of an "interest adverse to the interest of the estate" with respect to the matter on which the professional is employed that occurs "at any time during such professional person's employment under section 327 or 1103 of this title" may lead to denial of all compensation for services and reimbursement of expenses. 11 U.S.C. § 328(c).

Section 1103(b) prohibits dual representation if such representation would interfere with counsel's vigorous advocacy

for either client, jeopardize counsel's undivided loyalty to either client, or endanger the confidences and secrets of either client. In re Nat'l Liquidators, 182 B.R. 186, 192 (Bankr. S.D. Ohio 1995). It also prohibits concurrent representation where there exists even the appearance of impropriety. Id.

While the Bankruptcy Code does not define "adverse interest," the generally accepted definition is the (1) possession or assertion of an economic interest that would tend to lessen the value of the bankruptcy estate; or (2) possession or assertion of an economic interest that would create either an actual or potential dispute in which the estate is a rival claimant; or (3) possession of a predisposition under circumstances that create a bias against the estate. Dye v. Brown (In re AFI Holdings, Inc.), 355 B.R. 139, 148-49 (9th Cir. BAP 2006) (context of trustee's lack of disinterestedness in having adverse interest under § 101(14)).

Adherence to or violation of § 1103(b) is determined on a case-by-case basis. In re Oliver's Stores, Inc., 79 B.R. 588, 595 (Bankr. D.N.J. 1987).

In the instant case, appellees argue that disqualification under § 1103(b) is necessitated by Adorno's concurrent representation of two parties with adverse interests: (1) the Committee, whose goal it was to maximize the assets available for distribution to unsecured creditors and (2) the creditor, Avnet, in the same bankruptcy case, whose goal it was to defeat an action brought by the trustee on behalf of the debtor's estate, thereby diminishing the assets available to unsecured creditors.

Appellees contend that Adorno's disqualifying simultaneous representation occurred during the course of its representation of the Committee, but no later than when it filed an answer to the complaint brought by the trustee against Avnet. The answer sought to deny the debtor's bankruptcy estate the right to recover from Avnet the approximate $902,000 alleged fraudulent transfer.

On the other hand, Adorno contends that only a theoretical conflict existed, in which the bankruptcy court's interpretation of the Code would read an absolute ban against concurrent representation. Adorno also argues that its representation to each client was limited in scope and that it was under the impression that the STB Actions would be put on hold until the conclusion of the mediation. Thus, Adorno's filing the answer on behalf of Avnet would only be a "stop-gap measure" to keep Avnet from forfeiting any rights it might have in the Avnet Action until the mediation was concluded.

The bankruptcy court concluded that Adorno violated § 1103(b) by representing another entity with an adverse interest in early 2005 because Adorno was resisting the recovery of the approximate $900,000 that the trustee sought to recover, which would benefit the Committee's constituents. Accordingly, the bankruptcy court determined that Adorno's continued representation of the Committee on these facts was improper and the court exercised its discretion to disqualify Adorno. The court ruled that Adorno's dual role raised serious concerns about the vigor and loyalty with which the firm could pursue the interests of the Committee.

Furthermore, in response to Adorno's contention that there was an agreement to hold the Avnet Action in abeyance until the mediation was concluded, the court determined that no such agreement was clear from the parties' correspondence, and nevertheless, the conflict had already been created even if such an agreement existed.

We do not find the court erred. Courts have the power to disqualify an attorney based on their inherent authority to supervise the attorneys before it. In re Muma Svcs, Inc., 286 B.R. 583, 587 (Bankr. D. Del. 2002). That authority is especially strong when § 1103(b) has been violated.

Although the facts may represent a close call, the court was not operating under an incorrect view of the law and did not abuse its discretion in disqualifying Adorno as special counsel to the Committee. Thus, we will not disturb the court's determination to disqualify Adorno.

B

The court also ruled as an alternative basis for disqualification that Adorno's concurrent representation of adverse interests was prohibited under California law.

Civil Local Rule 11-4(a)(1) for the Northern District of California provides that, "Every member of the bar of this Court and any attorney permitted to practice in this Court under Civil L.R. 11 must . . . [b]e familiar and comply with the standards and professional conduct required of members of the State Bar of California." The Commentary section of N.D. Cal. Civ. R. 11-4 notes that, "The California Standards of Professional Conduct are

contained in the State Bar Act, the Rules of Professional Conduct of the State Bar of California, and decisions of any court applicable thereto."

Rule 3-310(C) of the California State Bar Rules of Professional Conduct provides that a member shall not, without the informed written consent of each client, accept representation of more than one client in a matter in which the interests of the clients potentially or actually conflict, or represent a client in a matter and simultaneously accept representation of another entity whose interest is adverse to the client in the first matter.

Rule 3-310(E) further states that a member shall not, without the informed written consent of the client, accept employment adverse to the client, where the member has obtained confidential information material to the employment during representation of the client.

Moreover, California law generally requires automatic disqualification where an attorney simultaneously represents clients with adverse interests. See People v. Speedee Oil Change Sys, Inc., 980 P.2d 371, 379 (Cal. 1999) (attorney's actual intention and motives are immaterial, and the rule of automatic disqualification applies); Cal West Nurseries, Inc. v. Super. Ct. of Sonoma County, 129 Cal. App. 4th 1170, 1175 (Ct. App. 2005); Flatt v. Super. Ct. of Sonoma County, 9 Cal. 4th 275, 284 (Ct. App. 1994) (with few exceptions, disqualification follows automatically, even though the simultaneous representations have nothing in common and there is no risk of disclosure of confidential information).

Among other reasons, Adorno contends that it disclosed its simultaneous representation of Avnet to the Committee by Tatelbaum's statement in his declaration, filed in support of Adorno's employment as special counsel to the Committee, that he represented Avnet for many years.

Appellees argue, however, that Tatelbaum did not disclose to the Committee that Adorno would be defending Avnet against the trustee's fraudulent conveyance action in the same case. Furthermore, appellees contend that Tatelbaum never filed any supplemental declarations disclosing Adorno's involvement in the Avnet Action.

The court determined that Adorno had not obtained the informed written consent of the Committee in advance of Adorno's representation of Avnet, even if Adorno claims the Committee and other interested parties were "aware" of its representation of Avnet. It concluded that this awareness, if it existed, was insufficient, where informed written consent of Rule 3-310 requires the client's written agreement to the representation following written disclosure. Rule 3-310(A)(1) & (2).

The court's findings of fact were not clearly erroneous, and we agree with its conclusions of law. We will not substitute our judgment for that of the trial court, which followed from factual findings that were based on substantial evidence. Speedee Oil Change Sys, Inc., 980 P.2d at 377. Thus, the court did not err in disqualifying Adorno as special counsel to the Committee because no informed written consent was obtained as required by Rule 3-310.

III

Adorno further contends that the Equity Committee and UST lacked standing to contest its representations under the general rule that only former or current clients have standing to seek disqualification based on a conflict of interest, and that the appellees did not suffer an injury in fact.

As the court determined, Adorno's argument is not persuasive because § 1109 provides that any party in interest may raise, and be heard, on any issue in a bankruptcy case.[7]

Furthermore, the court may raise the issue sua sponte and take any action necessary to prevent an abuse of process. Interwest Bus. Equip., Inc. v. United States Tr. (In re Interwest Bus. Equip., Inc.) 23 F.3d 311, 317 (10th Cir. 1994). The court has an independent duty to disqualify an attorney to preserve public trust in the administration of justice and the integrity of the legal system. City & County of San Francisco v. Cobra Solutions, Inc., 135 P.3d 20, 25 (Cal. 2006).

Courts have also recognized an exception to the general rule limiting standing to clients or former clients in cases where the ethical breach so infects the litigation that it impacts the moving party's interest in a just and lawful determination of the

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[7]Section 1109(b) of the Code provides:

> A party in interest, including the debtor, the trustee, a creditors' committee, an equity security holders' committee, a creditor, an 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).

claims. Colyer v. Smith, 50 F. Supp. 2d 966, 971-72 (C.D. Cal. 1999).

Here, the court determined that the facts of this case bring the Equity Committee and UST within this exception to have constitutional standing in bringing their motions to disqualify. The court did not abuse its discretion in this regard.

Regardless of whether the appellees are qualified under § 1109(b) to be heard, the court raises the conflict of interest issue on its own accord, or the appellees fall within the exception to the general rule, the court did not err in hearing and granting appellees' motions to disqualify.

CONCLUSION

Upon determination that this appeal from the order disqualifying Adorno is final, or alternatively granting leave to appeal, that the Equity Committee and UST had standing to seek disqualification of Adorno, and agreeing with the analysis of the bankruptcy court regarding conflict of interest under § 1103(b) and Rule 3-310 requiring disqualification of Adorno as special counsel for the Committee, we AFFIRM the court's order.