

FEB 12 2008

HAROLD S. MARENUS, CLERK
U.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL
OF THE NINTH CIRCUIT

6	In re:)	BAP Nos.	CC-07-1137-DMoPa
)		CC-07-1160-DMoPa
7	WON HO SONG and EUN JA SONG,)		(Consolidated)
)		
8	Debtors.)	Bk. No.	LA 02-17320-ER
)		
9	_____)		
)		
10	WON HO SONG and EUN JA SONG,)		
)		
11	Appellants,)		
)		
12	v.)	MEMORANDUM ¹	
)		
13	HOWARD EHRENBERG, Chapter 7)		
	Trustee; SUNG BAE PARK;)		
14	SHAPERO, SHAPERO & HURST,)		
)		
15	Appellees.)		
)		

Argued and Submitted on January 25, 2008
at Orange, California

Filed - February 12, 2008

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

Honorable Ernest M. Robles, Bankruptcy Judge, Presiding

Before: DUNN, MONTALI and PAPPAS, Bankruptcy Judges.

¹ 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.

1 The debtors, Won Ho Song and Eun Ja Song ("debtors"), appeal
2 the bankruptcy court's order granting the interim fee application
3 of Sung Bae Park ("Park") and Shapero, Shapero & Hurst ("SS&H").
4 Over the debtors' objections, the bankruptcy court approved \$2.5
5 million in fees and \$71,003.66 in costs for services rendered by
6 Park and SS&H in behalf of the chapter 7 trustee ("Trustee") as
7 special counsel.²

8 For the reasons set forth below, we AFFIRM the bankruptcy
9 court's award of fees and REVERSE the bankruptcy court's award of
10 costs.

11 I. FACTS

12 A. The debtors' prepetition state court action

13 Prior to their bankruptcy filing, the debtors filed a claim
14 with Cigna Property & Casualty Insurance Company ("Cigna") for
15 losses sustained in a fire that substantially damaged the
16 debtors' shopping center.³ Cigna denied their claim, asserting
17 that the debtors started the fire.

18 On April 26, 1996, Won Ho Song ("Song") filed a state court
19 action against Cigna for denying the claim ("State Court
20
21
22

23 ² Unless otherwise indicated, all chapter, section and rule
24 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330, and
25 to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037, as
26 enacted and promulgated prior to the effective date (October 17,
27 2005) of the provisions of the Bankruptcy Abuse Prevention and
Consumer Protection Act of 2005, Pub. L. 109-8, April 20, 2005,
119 Stat. 23.

28 ³ The debtors later lost the shopping center to foreclosure.

1 Action").⁴

2 While the State Court Action was pending, a criminal
3 complaint was filed against the debtors for felony arson, grand
4 theft and insurance fraud ("Criminal Action"). Song pleaded no
5 contest to the charges of grand theft and insurance fraud.⁵ Song
6 later filed a motion to withdraw his pleas, which was denied. On
7 July 9, 1999, Song was sentenced to two years imprisonment and
8 was ordered to pay Cigna \$521,375 in restitution in the Criminal
9 Action.

10 One month later, Cigna moved for summary judgment in the
11 State Court Action on the ground that Song's plea to insurance
12 fraud in the Criminal Action voided the insurance policy. The
13 state trial court granted summary judgment in favor of Cigna.
14 Song appealed.

15 Park became Song's attorney when Song moved to withdraw his
16 pleas in the Criminal Action. He then represented Song in the
17 appeal of the summary judgment in the State Court Action.

18 Park also represented the debtors in a matter involving
19 Golden Eagle Insurance Company ("Golden Eagle Matter"). The
20 record is not clear, however, as to what the Golden Eagle Matter
21 entailed. According to Song, Park represented the debtors in
22 administrative hearings and appeals against Golden Eagle
23 Insurance Company for fire damages to the shopping center.
24 According to Park, he represented debtor Eun Ja Song in a
25 conservatorship hearing involving Golden Eagle Insurance Company.

26
27 ⁴ Joseph M. Fredrics ("Fredrics") and Mazursky, Schwartz &
28 Angelo ("MS&A") initially represented Song in the State Court
Action. MS&A eventually withdrew. Song later employed Park.

⁵ The charges against Eun Ja Song were dropped.

1 B. The debtors' bankruptcy case

2 While the appeal of the summary judgment was pending, the
3 debtors, acting pro se, filed their voluntary chapter 7 petition
4 on March 13, 2002. They did not include the State Court Action
5 as an asset in their schedules. The debtors received their
6 discharge on June 24, 2002. The case closed as a no asset case
7 on July 12, 2002.

8 One week later, the state appellate court reversed summary
9 judgment in favor of Cigna. On December 17, 2002, the debtors
10 moved to reopen their bankruptcy case to add the State Court
11 Action to their schedules. On the same day, Park substituted in
12 as bankruptcy counsel for the debtors. The bankruptcy court
13 entered an order reopening the case on April 4, 2003.

14
15 1. The chapter 7 trustee's application to employ Park &
16 SS&H as special counsel

17 On August 18, 2003, the Trustee filed an application to
18 employ ("Employment Application") Park and SS&H as his special
19 counsel (collectively, "Special Counsel") to prosecute the State
20 Court Action. The debtors were served with a copy of the
21 Employment Application.

22 The captions on both the notice of the Employment
23 Application ("Employment Application Notice") and the Employment
24 Application cited § 327(a), instead of § 327(e), as the statutory
25 basis for employment.⁶ However, both the Employment Application
26

27 ⁶ The Employment Application also stated that "[a]uthority
28 for this application comes from 11 U.S.C. § 327(a) and 11 U.S.C.
§ 328(a) which allows for the employment of professional persons
on any reasonable terms and conditions of employment."

1 Notice and the Employment Application explicitly stated that the
2 Trustee sought to employ Park and SS&H to act as his special
3 counsel, as of June 17, 2003, and that “[i]t [was] necessary for
4 [the Trustee] to employ [them] . . . to prosecute [the State
5 Court Action].”

6 The Employment Application Notice and the Employment
7 Application disclosed that Special Counsel was to be paid on a
8 contingent basis. Specifically, the Employment Application
9 disclosed that Special Counsel did not receive a retainer and
10 would not be paid at an hourly rate or recover costs. Instead,
11 Special Counsel would be paid, subject to court approval, a
12 contingent fee of 50% of any funds collected in behalf of the
13 bankruptcy estate. The Employment Application also disclosed
14 that Special Counsel would be compensated only as approved by the
15 bankruptcy court. The Employment Application Notice made no
16 mention as to recovery of costs.

17 The Employment Application included statements of
18 disinterestedness from E. Rich Hurst, a principal of SS&H (“Hurst
19 Statement”), and from Park (“Park Statement”). The Hurst
20 Statement and the Park Statement (collectively, “Statements”)
21 both disclosed that Special Counsel “[would] not be paid at an
22 hourly rate or recover costs[,]” but would be paid a contingency
23 fee of 50% of the funds recovered in the State Court Action.
24 (Emphasis added.)

25 Per the Statements, Park and Hurst asserted that they were
26 disinterested parties in the bankruptcy case with no existing
27 conflicts of interest, as they did not represent any persons or
28 interests, past or present, adverse to the interests of the

1 debtors or the bankruptcy estate.

2 Park and Hurst also set forth in their respective Statements
3 an account of all of their connections with the debtors, which
4 Park and Hurst asserted was a complete account. Hurst disclosed
5 that SS&H had no connections with the debtors. Park disclosed
6 that he was attorney of record for the debtors in the bankruptcy
7 case. Park also disclosed that he had "represented [Song] in the
8 State Court Action, on appeal, and . . . in related criminal
9 proceedings." Park did not mention the Golden Eagle Matter.

10 On August 29, 2003, the bankruptcy court entered the
11 Employment Application Order. The Employment Application Order
12 authorized the Trustee "to employ the law firm of Shapero,
13 Shapero & Hurst and Sung Bae Park to act as his special
14 bankruptcy counsel as of June 17, 2003, at the expense of the
15 Estate, under the contingency fee arrangement as described in the
16 Employment Application . . . with the amount of compensation to
17 be determined by [the bankruptcy court] upon proper
18 application(s) therefore."

19 The debtors did not contest either the Employment
20 Application or the Employment Application Order. No amendments
21 to the Employment Application or Employment Application Order
22 were ever proposed, noticed and/or adopted.

23 On September 12, 2006, the debtors filed a substitution of
24 attorney, replacing Park with another attorney.⁷ The
25 substitution of attorney reflected that Park consented to the
26 substitution on August 22, 2006.

27
28 ⁷ The debtors subsequently filed two more substitutions of
counsel. Jaenam Coe currently is attorney of record for the
debtors and is representing the debtors in the appeal before us.

1 2. The interim fee application of Park and SS&H

2 The State Court Action proceeded to a seven-week jury trial.
3 Although prior counsel had performed services with respect to
4 preparing the State Court Action for trial, Special Counsel
5 conducted further extensive discovery, retained and prepared
6 expert witnesses, and briefed and argued approximately 35 motions
7 *in limine* over a period in excess of two years prior to the
8 trial, at which the jury rendered a verdict in Song's favor. On
9 December 21, 2005, a judgment was entered against Cigna in the
10 amount of approximately \$6.2 million. Cigna appealed.

11 On July 13, 2006, the Trustee and Cigna entered into
12 mediation and settled the State Court Action. Under the terms of
13 the settlement, Cigna agreed to pay the Trustee \$5 million in
14 cash and to cancel as satisfied the restitution award it obtained
15 against Song in the Criminal Action. Song signed the settlement
16 agreement.

17 On September 19, 2006, the Trustee filed a motion for
18 approval of the settlement. The debtors opposed, arguing that, as
19 they obtained judgment against Cigna, they intended to move to
20 dismiss their bankruptcy case and to pay their creditors in full
21 with proceeds from the judgment.⁸ After notice and a hearing,
22 the bankruptcy court entered an order approving the settlement
23 ("Settlement Order") over the debtors' opposition. The debtors
24

25 ⁸ The debtors filed their opposition to the Trustee's motion
26 to approve the settlement and the motion to dismiss on the same
27 day. In the motion to dismiss, the debtors advanced the same
28 arguments as those given in their opposition to the Trustee's
motion to approve the settlement. After holding a separate
hearing on the motion to dismiss, the bankruptcy court denied the
motion to dismiss.

1 did not appeal the Settlement Order.

2 On December 19, 2006, Special Counsel filed their interim
3 fee application ("Fee Application"), requesting \$2,943,665 in
4 fees and \$71,003.66 in costs. Special Counsel calculated the
5 fees by including 50% of the restitution award obtained by Cigna
6 in the Criminal Action and waived by Cigna as part of the
7 settlement, with 50% of the \$5 million cash settlement proceeds.⁹

8 The Fee Application included, as an exhibit, a copy of the
9 legal services agreement between the Trustee and Special Counsel
10 ("Service Agreement"). The Service Agreement, dated and signed
11 by the Trustee on September 15, 2003, after the Employment
12 Application Order was entered, provided that the attorney's fees
13 would be 50% of the recovery - that is, the total amount
14 received, including attorney's fees, after reduction for costs.
15 It further provided that the Trustee was to pay all costs in
16 connection with Special Counsel's representation of the Trustee
17 in the State Court Action.¹⁰ The Fee Application also included,
18 as an exhibit, a breakdown of the costs incurred by Special
19 Counsel in prosecuting the State Court Action.

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25 ⁹ Although the original restitution obligation was \$521,375,
26 Special Counsel added interest, which increased the amount of the
restitution obligation to \$887,331.

27 ¹⁰ The Service Agreement described costs as court and
28 arbitration filing fees, deposition costs, expert fees and
expenses, investigation costs, computer legal research, and other
similar expenses.

1 The debtors opposed both the fees and costs requested by
2 Special Counsel in the Fee Application.¹¹

3 With respect to the issue of fees, the debtors advanced
4 several arguments. The debtors contested the inclusion of 50% of
5 the restitution obligation in the calculation of fees, arguing
6 that the restitution waiver was not a part of the recovery as
7 described in the Fee Application.

8 The debtors also argued that the bankruptcy court should
9 deny Special Counsel's fees on the basis that Special Counsel had
10 a conflict of interest which disqualified Special Counsel from
11 representing the Trustee. Specifically, the debtors averred that
12 Park was not disinterested and held interests adverse to the
13 debtors when he became employed as special counsel to the Trustee
14 while still employed as attorney for the debtors.

15 The debtors asserted that, under § 327(c), a bankruptcy
16 court may deny the fees of a professional if, during employment,
17 that professional was not a disinterested person, or held an
18 interest adverse to the interests of the estate. Park was no
19 longer a disinterested person once he began representing the
20 Trustee as special counsel. Specifically, because Park was to
21 receive a substantial contingent fee as the Trustee's special
22 counsel, he favored the Trustee's interests over the debtors'
23 interests. The debtors cited a number of examples of Park's lack

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25 ¹¹ The debtors filed an opposition ("Original Opposition"),
26 a supplemental opposition ("Supplemental Opposition") and a
27 second supplemental opposition ("Second Supplemental
28 Opposition") (collectively, "Oppositions") to the Fee Application.
Special counsel filed a reply to the debtors' opposition ("Reply
to Opposition") and a reply to the debtors' supplemental and
second supplemental oppositions ("Reply to Supplemental
Oppositions").

1 of disinterestedness. For instance, the debtors claimed, Park
2 pushed Song to sign on to the settlement and "agreed," along with
3 SS&H, to reduce the fees to \$2.25 million to induce Song to sign
4 on to the settlement.¹²

5 The debtors further contended that, because the Trustee held
6 an interest in conflict with the debtors, Special Counsel
7 represented an adverse interest in serving as attorneys for the
8 Trustee. The debtors asserted that the Trustee and the debtors
9 had conflicting interests in the State Court Action. According
10 to the debtors, the Trustee merely wanted sufficient funds to pay
11 creditors; he had no interest in obtaining any additional amounts
12 to provide the debtors with a surplus. The debtors, on the other
13 hand, wanted to obtain as large a recovery as possible.

14 The debtors also claimed that Rule 2014 required an attorney
15 to disclose fully all of his or her connections with the debtor
16 in an application for employment for purposes of determining
17 whether the attorney should be disqualified.¹³ Here, the debtors

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19 ¹² According to Song, Special Counsel agreed to reduce their
20 fees by \$250,000 to defray the fees and costs of Fredrics and
MS&A, as well as to induce Song to agree to the settlement.

21 ¹³ Rule 2014(a) provides, in relevant part:

22 An order approving the employment of attorneys . . .
23 pursuant to § 327 . . . of the Code shall be made only
24 on application of the trustee The application
25 shall state the specific facts showing the necessity
26 for the employment, the name of the person to be
27 employed, the reasons for the selection, the
28 professional services to be rendered, any proposed
arrangement for compensation, and, to the best of the
applicant's knowledge, all of the person's connections
with the debtor, creditors, any other party in
interest, their respective attorneys and accountants,

(continued...)

1 pointed out, Park did not fully disclose all of his connections
2 with the debtors in the Employment Application by omitting his
3 prior representation of the debtors in the Golden Eagle Matter.
4 Park conceded this point, admitting in his declaration attached
5 to the Supplemental Reply that he did not disclose his
6 representation of debtor Eun Ja Song in the Golden Eagle Matter
7 in the Employment Application.

8 With respect to the issue of costs, the debtors essentially
9 argued that they were unaware that Special Counsel would recover
10 \$71,003.66 in costs, in addition to their contingent fee. The
11 debtors understood that the reduced fees agreed upon by Special
12 Counsel at mediation would be the total amount that Special
13 Counsel would receive for services in the State Court Action.
14 According to the debtors, Special Counsel never mentioned
15 recovery of costs at the mediation. The debtors further
16 contended in their Oppositions that Special Counsel neither
17 listed nor explained the costs incurred in the Fee Application.

18 The debtors further claimed that, when the Trustee moved to
19 employ Special Counsel, "in making the application, [they were]
20 deceived of the terms of the fee agreement by [their] bankruptcy
21 attorney, Mr. Park" and discovered the "actual terms of the
22

23 ¹³(...continued)

24 the United States trustee, or any person employed in
25 the office of the United States trustee. The
26 application shall be accompanied by a verified
27 statement of the person to be employed setting forth
28 the person's connections with the debtor, creditors, or
any other party in interest, their respective attorneys
and accountants, the United States trustee, or any
person employed in the office of the United States
trustee.

1 agreement much later.”¹⁴ The debtors asserted that “[t]he fee
2 application now [was] totally contrary to [the] agreed deal . . .
3 [and] the fee application ask[ed] for numbers [they had] never
4 seen or been told [about] before.”

5 At the January 10, 2007 hearing on the Oppositions to the
6 Fee Application, the bankruptcy court found that the restitution
7 waiver was not part of the monies collected, as described in the
8 Employment Application, and the cancellation of the restitution
9 obligation simply was “an attempt to avoid further complications
10 of having to administer a proof of claim in the bankruptcy
11 estate.” Tr. of January 10, 2007 Hr’g, 2:11-14. Accordingly,
12 the bankruptcy court did not award fees to Special Counsel based
13 on the restitution waiver.

14 The bankruptcy court rejected the debtors’ assertion that
15 Special Counsel had reduced their fees to induce Song to agree to
16 the settlement on the ground that the debtors should have raised
17 the issue at the hearing on the Trustee’s motion to approve the
18 settlement.

19 The bankruptcy court then addressed the issue of Park’s
20 concurrent representation of the Trustee and the debtors. The
21 bankruptcy court expressed concern that, in light of Tevis v.
22 Wilke, Fleury, Hoffelt, Gould & Birney, LLP (In re Tevis), 347

23
24 ¹⁴ The debtors made this argument in the Supplemental
25 Declaration of Won Ho Song attached to the Supplemental
26 Opposition. In explicitly referencing the declarations
27 (“Supplemental Declarations”) attached to the Supplemental
28 Opposition and the Second Supplemental Opposition, Song made them
a part of his Oppositions. Per the Supplemental Declarations,
Song filed them “to point out factual errors in the [Fee
Application] . . . and to further supplement” the Supplemental
Opposition and the Second Supplemental Opposition.

1 B.R. 679 (9th Cir. BAP 2006), which the bankruptcy court believed
2 was directly applicable, Park's concurrent representation of the
3 Trustee and the debtors may have created a conflict of interest.

4 According to the bankruptcy court, Tevis provided, in part,
5 that attorney's fees cannot be awarded where an attorney, who had
6 been employed as general counsel under § 327(a), concurrently
7 represents the trustee and the debtor. By representing both the
8 trustee and the debtor, the attorney had a conflict of interest
9 and was no longer a disinterested person as required under
10 § 327(a). The bankruptcy court asked for further briefing on the
11 issue.

12 In their brief, the debtors advanced an additional
13 argument.¹⁵ The debtors asserted that Rule 3-310 of the
14 California Rules of Professional Conduct ("California RPC")
15 requires that, before undertaking the representation of another
16 client with a possibly conflicting interest, the attorney must
17 obtain his or her client's informed written consent. Park
18 neither advised the debtors of the potential conflict of interest
19 nor obtained the debtors' written consent when he became special
20 counsel for the Trustee.

21 After the parties submitted their briefs, the bankruptcy
22 court took the matter under submission. On March 26, 2007, the
23 bankruptcy court issued its Memorandum of Decision ("Memorandum
24 Decision").

25 In its Memorandum Decision, the bankruptcy noted the
26 debtors' argument regarding Park's alleged violation of the

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28 ¹⁵ The debtors earlier touched on this argument in the
Oppositions and elaborated on it in the Debtors' Reply Brief.

1 California RPC in failing to inform them of the potential
2 conflict and to obtain the debtors' written waiver of the
3 potential conflict. The bankruptcy court then summarily
4 addressed the issue as to whether Tevis applied to the instant
5 case, given that it involved the employment of general bankruptcy
6 counsel under § 327(a). The bankruptcy court reasoned that, as
7 both § 327(a) and (e) included the requirement that an attorney
8 hold no adverse interest, Tevis applied to the instant case and
9 could "provide guidance herein whether [Special Counsel] was
10 retained pursuant to § 327(a) or § 327(e)." Memorandum Decision,
11 11:2-9.

12 The bankruptcy court then focused on the issue concerning
13 Park's concurrent representation of the Trustee and the debtors
14 in light of Tevis. The bankruptcy court found that Tevis, upon
15 closer reading, suggested that the concurrent representation of
16 the trustee and the debtor by an attorney "necessarily and
17 automatically result[s]" in conflict only where the attorney
18 "represents one client in litigation against another of his or
19 her clients, that he or she represents or represented in a
20 related or unrelated matter or matters." Memorandum Decision,
21 11:10-17, 12:1-2.

22 Applying this rationale, the bankruptcy court determined
23 that, under the circumstances of the instant case, "[this]
24 automatic disqualification rule for concurrent representation
25 [did] not readily apply." Memorandum Decision, 13:2-7. The
26 bankruptcy court found that Park did not represent any interest
27 adverse to either the Trustee or the debtors because neither the
28 Trustee nor the debtors had sued the other on any matter. Thus,

1 the bankruptcy court concluded, no conflict of interest arose
2 when Park concurrently represented the Trustee and the debtors.¹⁶

3 The bankruptcy court further reasoned that the Trustee and
4 the debtors were actually aligned in their interests as to the
5 State Court Action. Both the Trustee and the debtors "wanted to
6 maximize the settlement amount; the Trustee wanted to maximize
7 the return for the estate and the Debtors wanted a surplus for
8 themselves." Memorandum Decision, 13:21-24. The bankruptcy
9 court found that the debtors did not demonstrate that their
10 interest in the State Court Action was adverse to that of the
11 Trustee.

12 The bankruptcy court did not address the issue of Park's
13 failure to disclose his representation of the debtors in the
14 Golden Eagle Matter.

15 On April 12, 2007, the bankruptcy court entered its order
16 approving the Fee Application ("Fee Application Order") to the
17 extent of 50% of the monies collected plus costs for the reasons
18 set forth in its Memorandum Decision. The bankruptcy court also
19 authorized the Trustee to make payment upon entry of the Fee
20 Application Order.

21 On April 4, 2007, the debtors filed a notice of appeal of
22 the Memorandum Decision.¹⁷ On April 23, 2007, the debtors filed

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24 ¹⁶ As additional support, the bankruptcy court pointed out
25 the fact that, upon filing for bankruptcy, the Trustee succeeded
the debtors as the plaintiff in the State Court Action.

26 ¹⁷ Our clerk issued an order, questioning the finality of
27 the Fee Application Order. The debtors filed a letter in
28 response, arguing that the Fee Application was for final fees,
not interim fees. Our clerk then issued another order, inviting
(continued...)

1 a notice of appeal of the Fee Application Order. We consolidated
2 the appeals¹⁸ and decided to review the consolidated appeal,
3 determining the Fee Application Order to be sufficiently final
4 and, to the extent that it was not final, granting leave to
5 appeal.

6 7 **II. JURISDICTION**

8 The bankruptcy court had jurisdiction pursuant to 28 U.S.C.
9 §§ 1334 and 157(b)(1) and (b)(2)(A) and (O). We have
10 jurisdiction pursuant to 28 U.S.C. § 158.

11 12 **III. ISSUES**

13 (1) Whether the bankruptcy court abused its discretion in
14 awarding \$2.5 million as compensation to Special Counsel.

15 (2) Whether the bankruptcy court abused its discretion in
16 awarding \$71,003.66 in costs to Special Counsel.

17 18 **IV. STANDARDS OF REVIEW**

19 We review orders on employment, disqualification, and
20 compensation of professionals for abuse of discretion. Movitz v.
21 Baker (In re Triple Star Welding, Inc.), 324 B.R. 778, 788 (9th
22 Cir. BAP 2005); COM-1 Info, Inc. v. Wolkowitz (In re Maximus

23
24 ¹⁷(...continued)
25 Special Counsel to file a response to the debtors' letter.
26 Special Counsel instead filed a motion to dismiss the appeal,
which we denied.

27 ¹⁸ We consolidated the appeal of the Memorandum Decision,
28 BAP No. CC-07-1137, and the appeal of the Fee Application Order,
CC-07-1160, under BAP No. CC-07-1137.

1 Computers, Inc.), 278 B.R. 189, 194 (9th Cir. BAP 2002). An
2 abuse of discretion occurs if the bankruptcy court bases its
3 ruling upon an erroneous view of the law or clearly erroneous
4 factual findings. Hansen v. Moore (In re Hansen), 368 B.R. 868,
5 875 (9th Cir. BAP 2007). To reverse for abuse of discretion, we
6 must have a definite and firm conviction that the bankruptcy
7 court committed a clear error of judgment in the conclusion it
8 reached. Id.

9 We review de novo the bankruptcy court's legal conclusions.
10 Triple Star Welding, 324 B.R. at 788. We review de novo the
11 bankruptcy court's statutory interpretations. Maximus Computers,
12 278 B.R. at 194.

14 V. DISCUSSION

15 A. The bankruptcy court did not abuse its discretion in 16 awarding fees to Special Counsel

17 The debtors argue that the bankruptcy court abused its
18 discretion in awarding fees to Special Counsel in light of the
19 conflict of interest between Special Counsel and the debtors. As
20 in their Oppositions before the bankruptcy court, the debtors
21 contend that there was a conflict of interest because: (1) Park
22 was not a disinterested party; and (2) Special Counsel held an
23 interest adverse to the debtors.

- 24
25 1. Park did not need to be a disinterested party
26 to qualify for employment as special counsel under
§ 327(e)

27 Section 327 governs the trustee's employment of attorneys
28 and other professionals to represent or aid the trustee in

1 carrying out his or her duties. 3 Collier on Bankruptcy ¶ 327.01
2 (Alan N. Resnick & Henry J. Sommer, eds., 15th ed. rev. 2007).
3 Section 327(a) authorizes the trustee to employ an attorney for
4 general purposes in administering the bankruptcy estate.¹⁹ 3
5 Collier on Bankruptcy ¶ 327.02. To qualify for employment under
6 § 327(a), the attorney must be a disinterested person and cannot
7 hold or represent an interest adverse to the estate.

8 Section 327(e), on the other hand, authorizes the trustee to
9 employ, for a specified purpose, other than to represent the
10 trustee generally in fulfilling his duties in the case, an
11 attorney who has represented the debtor.²⁰ 3 Collier on
12 Bankruptcy ¶ 327.04[9]. Unlike § 327(a), § 327(e) does not
13 require disinterestedness. Film Ventures Int'l, Inc. v. Asher
14 (In re Film Ventures Int'l, Inc.), 75 B.R. 250, 252 (9th Cir. BAP
15 1987). Rather, § 327(e) only requires that the employment of an

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17 ¹⁹ Section 327(a) provides:

18 Except as otherwise provided in this section, the
19 trustee, with the court's approval, may employ one or
20 more attorneys, accountants, appraisers, auctioneers,
21 or other professional persons, that do not hold or
22 represent an interest adverse to the estate, and that
are disinterested persons, to represent or assist the
trustee in carrying out the trustee's duties under this
title.

23 ²⁰ Section 327(e) provides:

24 The trustee, with the court's approval, may employ, for
25 a specified special purpose, other than to represent
the trustee in conducting the case, an attorney that
26 has represented the debtor, if in the best interest of
the estate, and if such attorney does not represent or
27 hold any interest adverse to the debtor or to the
estate with respect to the matter on which such
28 attorney is to be employed.

1 attorney be in the best interest of the estate and that the
2 attorney not represent or hold an interest adverse to the debtor
3 or the estate with respect to the matter on which the attorney is
4 to be employed.

5 The debtors assert that the disinterestedness standard under
6 § 327(a), which is not present under § 327(e), applies because
7 the Employment Application set forth § 327(a) as the statutory
8 basis for employment. Due to Park's concurrent representation of
9 the Trustee and the debtors, Park was not a disinterested person
10 for § 327(a) purposes. Because Park was not a disinterested
11 person, the debtors argue, the bankruptcy court should have
12 denied Special Counsel fees pursuant to § 328(c).²¹

13 We disagree. Although the Employment Application and the
14 Employment Application Notice cited § 327(a) as the statutory
15 basis for employment, both the Employment Application and the
16 Employment Application Notice expressly described the limited
17 nature and purpose of the retention of Park and SS&H - to serve
18 as special counsel to prosecute the State Court Action. Also,
19 the Employment Application Order confirmed the limited nature of
20 the retention; the Employment Application Order stated that "the

21
22 ²¹ Section 328(c) provides:

23 Except as provided in section 327(c), 327(e), or
24 1107(b) of this title, the court may deny allowance of
25 compensation for services and reimbursement of expenses
26 of a professional person employed under section 327 or
27 1103 of this title if, at any time during such
28 professional person's employment under section 327 or
1103 of this title, such professional person is not a
disinterested person, or represents or holds an
interest adverse to the interest of the estate with
respect to the matter on which such professional person
is employed.

1 Trustee is hereby authorized to employ the law firm of [SS&H] and
2 [Park] to act as his special bankruptcy counsel . . . at the
3 expense of the Estate, under a contingency fee arrangement as
4 described in the Application[.]" (Emphasis added.) Given the
5 explicit language of the Employment Application and the
6 Employment Application Order, there is no question that the
7 Trustee employed Park and SS&H as special counsel. The standard
8 of disinterestedness under § 327(a) does not apply.

9 By extension, we disagree with the bankruptcy court that
10 Tevis applies to the instant case. In Tevis, the chapter 7
11 trustee had employed appellant law firm as his general counsel
12 pursuant to § 327(a). Tevis, 347 B.R. at 685. In Tevis, we
13 stated, in dictum, that had the appellant law firm concurrently
14 represented the trustee as his general counsel and the debtors,
15 it would not have been a disinterested party under § 327(a).
16 Tevis, 347 B.R. at 691.²² However, Tevis is inapplicable to the
17 instant case because Park and SS&H were employed as special
18 counsel under § 327(e) and were not subject to the
19 disinterestedness standard under § 327(a).

20
21 2. Special Counsel did not have interests adverse to the
22 debtors

23 The phrase "adverse interest" is not defined in the
24 Bankruptcy Code, Tevis, 347 B.R. at 688, but

25 _____
26 ²² Specifically, we stated that "[i]f [the debtors] had been
27 current clients of Wilke Fleury at the same time that it was
28 counsel for the trustee, it clearly would have failed the 'hold
or represent' requirement of § 327(a)." (Emphasis added and in
original.)

1 [a] generally accepted definition of "adverse interest"
2 is the (1) possession or assertion of an economic
3 interest that would tend to lessen the value of the
4 bankruptcy estate; or (2) possession or assertion of an
5 economic interest that would create either an actual or
6 potential dispute in which the estate is a rival
7 claimant; or (3) possession of a predisposition under
8 circumstances that create a bias against the estate.

9 Dye v. Brown (In re AFI Holding, Inc.), 355 B.R. 139, 148-49 (9th
10 Cir. BAP 2006). To represent an adverse interest means to serve
11 as an attorney for a party who holds an adverse interest. Tevis,
12 347 B.R. at 688.

13 The debtors contend that the substantial surplus they might
14 receive from the State Court Action created a conflict of
15 interest between the debtors and the Trustee.²³ According to the
16 debtors, the debtors' interest in the State Court Action - to
17 obtain as large a recovery as possible - conflicted with the
18 Trustee's interest to obtain a sufficient recovery to pay the
19 allowed claims of creditors. Thus, in acting as attorneys for
20 the Trustee in the State Court Action, Special Counsel was
21 representing an adverse interest.²⁴

22 _____
23 ²³ Under § 726(a)(6), the debtors will receive those estate
24 assets remaining after payment of all allowed claims and
25 administrative fees and expenses.

26 ²⁴ The debtors rely on In re Mercury, 280 B.R. 35 (Bankr.
27 S.D.N.Y. 2002), aff'd, 122 Fed. Appx. 528 (2d Cir. 2004), in
28 support of their argument. The bankruptcy court in Mercury
denied fees and costs to a law firm that had represented the
debtors in a state court action and in their bankruptcy case, but
later withdrew as bankruptcy counsel for the debtors and became
special counsel to the chapter 7 trustee.

Mercury is distinguishable from the instant case. Unlike
the case before us, in Mercury, neither the employment
application nor the motion to withdraw was served on the debtors.
Further, the law firm serving as special counsel for the chapter

(continued...)

1 The debtors do not demonstrate, however, that either the
2 Trustee or Special Counsel had an adverse interest, as described
3 in Tevis. Nothing in the record indicates that Special Counsel
4 or the Trustee has an economic interest that would lessen the
5 value of the estate or create a dispute in which the estate is a
6 rival claimant to the debtors, or that either Special Counsel or
7 the Trustee has a predisposition under the circumstances for a
8 bias against the debtors. Indeed, under § 704(1),²⁵ the trustee
9 has a duty to "collect and reduce to money the property of the
10 estate . . . , and close such estate as expeditiously as is
11 compatible with the best interests of parties in interest,"
12 including the debtors. See Pereira v. Centel Corp. (In re Argo
13 Commc'ns Corp.), 134 B.R. 776, 783 (Bankr. S.D.N.Y. 1991) ("It is
14 a fundamental concept within the Bankruptcy Code that the trustee
15 is empowered to 'collect and reduce to money the property of the
16 estate . . . [in] the best interest of parties in interest.'
17 These words constitute the trustee's main duty to both the debtor
18 and the creditors to realize from the estate all that is possible
19 for distribution among the creditors.") (citations omitted);

20
21 ²⁴ (...continued)

22 7 trustee in Mercury was employed to seek approval of a
23 settlement that the debtors always opposed.

24 Here, the bankruptcy court specifically found that the
25 debtors were served with the Employment Application. The debtors
26 themselves filed the substitution of attorney, replacing Park
27 with another attorney. In addition, up until the settlement
28 negotiations, which took place after the jury trial in the State
Court Action, there was no conflict, actual or potential, in
Special Counsel's representation of the debtors and the Trustee,
and Song signed the settlement agreement with Cigna.

²⁵ Under BACPA, § 704(1) has been redesignated as
§ 704(a)(1).

1 Obuchowski v. State of Vermont (In re Henry), 135 B.R. 6, 11
2 (Bankr. D. Vt. 1991) (citing 4 Collier on Bankruptcy § 704(1)
3 (15th ed. 1987)). See also 6 Collier on Bankruptcy ¶ 704.04[3]
4 at 704-17 (“[T]he trustee has a duty to distribute any surplus to
5 the debtor under section 726, and a failure to perform this duty
6 is treated similarly to a failure to make proper distributions to
7 creditors.”).

8 As the bankruptcy court noted, there was no conflict between
9 the debtors and the Trustee with respect to the State Court
10 Action. Both the debtors and the Trustee wanted the same outcome
11 - to obtain as substantial a recovery as possible. Simply
12 because the debtors and the Trustee have different motives in
13 wanting the same outcome does not signify that they have adverse
14 interests. Thus, as there was no conflict of interest between
15 the debtors and the Trustee with respect to prosecution of the
16 State Court Action, Special Counsel was not representing an
17 adverse interest.

- 18
19 3. The bankruptcy court granted Special Counsel fees in
20 full though it had the discretion to deny the fees for
21 Park’s failure to disclose all of his connections with
22 the debtors

23 The debtors contend that Park’s failure to disclose his
24 representation of the debtors in the Golden Eagle Matter
25 constitutes grounds for denial of fees under Rule 2014(a). The
26 debtors assert that failure to comply with Rule 2014(a) is a
27 sanctionable violation, regardless of the harm to the estate and
28 even if the omission was inadvertent. Thus, contrary to Park’s
assertion, even if his representation of the debtors in the

1 Golden Eagle Matter was irrelevant or trivial, he nonetheless was
2 required to disclose it.

3 Rule 2014(a) requires a professional to state in the
4 application for employment, to the best of his or her knowledge,
5 "all of [his or her] connections with the debtor." Fed. R.
6 Bankr. P. 2014(a) (West 2002) (emphasis added). The verified
7 statement accompanying the employment application also must set
8 forth the professional's connections with the debtor. Id.

9 Essentially, Rule 2014(a) imposes on the professional
10 seeking employment "an affirmative duty to disclose all of his
11 [or her] connections with the [d]ebtor." Film Ventures Int'l
12 Inc., 75 B.R. at 252 (emphasis added). See also Mehdi pour v.
13 Marcus & Millichap (In re Mehdi pour), 202 B.R. 474, 480 (9th Cir.
14 BAP 1996) ("Pursuant to § 327, a professional has a duty to make
15 full, candid and complete disclosure of all facts concerning his
16 transactions with the debtor."); Triple Star Welding, 324 B.R. at
17 788-89 ("Full disclosure is an essential prerequisite for both
18 employment and compensation.").

19 "Complete disclosure is for the court's benefit so that it
20 can scrutinize any adverse interests of the attorney." First
21 Interstate Bank, NA v. CIC Inv. Corp. (In re CIC Inv. Corp.), 175
22 B.R. 52, 54 (9th Cir. BAP 1994). Thus, professionals must
23 disclose all connections with the debtor, no matter how
24 irrelevant or trivial those connections seem. Mehdi pour, 202
25 B.R. at 480.

26 However, the bankruptcy court has discretion to excuse a
27 failure to disclose. CIC Inv. Corp., 175 B.R. at 54. Once the
28 bankruptcy court acquaints itself with the true facts, it "has

1 considerable discretion in determining to allow all, part or none
2 of the fees and expenses of a properly employed professional.”
3 Triple Star Welding, 324 B.R. at 789. See also Film Ventures
4 Int’l Inc., 75 B.R. at 253 (“[T]he trial court is in the best
5 position to resolve disputes over legal fees.”). If the
6 bankruptcy court finds no need to take remedial measures, it
7 appropriately can do so in the exercise of its discretion. CIC
8 Inv. Corp., 175 B.R. at 54 (citing Film Ventures Int’l, Inc., 75
9 B.R. at 253).

10 Here, Park admitted that he did not disclose his
11 representation of the debtors in the Golden Eagle Matter. Thus,
12 at the time of hearing on the debtors’ Oppositions to the Fee
13 Application, the bankruptcy court was aware from the record of
14 Park’s failure to disclose this connection. Though the
15 bankruptcy court had the discretion to deny all or a portion of
16 the fees for Park’s failure to disclose, it nonetheless awarded
17 nearly all of the fees requested by Special Counsel, disallowing
18 only that portion of the fee that included 50% of the restitution
19 obligation, as it was not part of the funds actually collected.

20 Because the bankruptcy court awarded Special Counsel a
21 substantial contingent fee in spite of Park’s failure to comply
22 fully with Rule 2014(a), we assume that the bankruptcy court
23 found no need to take remedial measures against Special Counsel,
24 and we will not second guess the bankruptcy court’s decision on
25 that basis. See, e.g., Film Ventures Int’l, Inc., 75 B.R. at
26 253.

1 4. Rule 3-310 of the California Rules of Professional
2 Conduct²⁶

3 ²⁶ Rule 3-310 provides:

4 (A) For purposes of this rule:

- 5 (1) "Disclosure" means informing the client or
6 former client of the relevant circumstances and of
7 the actual and reasonably foreseeable adverse
8 consequences to the client or former client;
9 (2) "Informed written consent" means the client's
10 or former client's written agreement to the
 representation following written disclosure;
 (3) "Written" means any writing as defined in
 Evidence Code section 250.

11 (B) A member shall not accept or continue
12 representation of a client without providing written
13 disclosure to the client where:

- 14 (1) The member has a legal, business, financial,
15 professional, or personal relationship with a
16 party or witness in the same matter; or
17 (2) The member knows or reasonably should know
18 that:
19 (a) the member previously had a legal,
20 business, financial, professional, or
21 personal relationship with a party or witness
22 in the same matter; and
23 (b) the previous relationship would
24 substantially affect the member's
 representation; or
 (3) The member has or had a legal, business,
 financial, professional, or personal relationship
 with another person or entity the member knows or
 reasonably should know would be affected
 substantially by resolution of the matter; or
 (4) The member has or had a legal, business,
 financial, or professional interest in the subject
 matter of the representation.

25 (C) A member shall not, without the informed written
26 consent of each client:

- 27 (1) Accept representation of more than one client
28 in a matter in which the interests of the clients
 potentially conflict; or
 (2) Accept or continue representation of more than

(continued...)

1 As an additional ground for denying the award of fees to
2 Special Counsel, the debtors argue that California RPC 3-310(C)
3 required Park to obtain an informed written consent from the
4 debtors before accepting employment for the Trustee.

5
6 ²⁶(...continued)

7 one client in a matter in which the interests of
8 the clients actually conflict; or
9 (3) Represent a client in a matter and at the same
10 time in a separate matter accept as a client a
11 person or entity whose interest in the first
12 matter is adverse to the client in the first
13 matter.

14 (D) A member who represents two or more clients shall
15 not enter into an aggregate settlement of the claims of
16 or against the clients without the informed written
17 consent of each client.

18 (E) A member shall not, without the informed written
19 consent of the client or former client, accept
20 employment adverse to the client or former client
21 where, by reason of the representation of the client or
22 former client, the member has obtained confidential
23 information material to the employment.

24 (F) A member shall not accept compensation for
25 representing a client from one other than the client
26 unless:

27 (1) There is no interference with the member's
28 independence of professional judgment or with the
client-lawyer relationship; and

(2) Information relating to representation of the
client is protected as required by Business and
Professions Code section 6068, subdivision (e);
and

(3) The member obtains the client's informed
written consent, provided that no disclosure or
consent is required if:

(a) such nondisclosure is otherwise
authorized by law; or

(b) the member is rendering legal services on
behalf of any public agency which provides
legal services to other public agencies or
the public.

1 State rules of professional responsibility apply, as long as
2 they do not conflict with the Bankruptcy Code and/or the
3 Bankruptcy Rules.²⁷ See generally AFI Holding, 355 B.R. at 153
4 n.15.

5 Rule 3-310(C)(1) of the California RPC provides that an
6 attorney shall not, without the informed written consent of each
7 client, accept representation of more than one client in a matter
8 in which the interests of the clients potentially conflict.

9 Zador Corp. v. Kwan, 31 Cal. App. 4th 1285, 1295 (Cal. Ct. App.
10 1995). Rule 3-310(C)(2) provides that an attorney shall not,
11 without the informed written consent of each client, accept
12 representation of more than one client in a matter in which the
13 interests of the clients actually conflict. Id. If a conflict
14 of interest exists, the attorney must disclose the conflict to
15 each client and either obtain written waivers or withdraw. See
16 Gulf Ins. Co. v. Berger, 79 Cal. App. 4th 114, 132 (Cal. Ct. App.
17 2000).

18 In addition, Rule 3-310(B)(3) provides that, where the

19
20 ²⁷ We first look to the local rules of the United States
21 Bankruptcy Court, Central District of California, as a source of
22 ethical standards for attorneys. See Paul E. Iacono Structural
23 Engineer, Inc. v. Humphrey, 722 F.2d 435, 439-40 (9th Cir. 1983).
24 Local Rule 2090-1(e) of the Local Rules for the United States
25 Bankruptcy Court, Central District of California, provides that
26 any attorney who appears before the bankruptcy court shall be
27 subject to the standards of professional conduct as set forth in
28 Local Rule 83-3.1.2 of the District Court Rules.

25 Local Rule 83-3.1.2 of the District Court Rules for the
26 United States District Court, Central District of California,
27 provides that "each attorney shall be familiar with and comply
28 with the standards of professional conduct required of members of
the State Bar of California and contained in the State Bar Act,
the Rules of Professional Conduct of the State Bar of California
and the decisions of any court applicable thereto."

1 attorney has a legal or professional relationship with another
2 person that the attorney knows or reasonably should know would be
3 affected substantially by resolution of the subject matter, the
4 attorney must provide the client with written disclosures before
5 the attorney accepts representation of the client.

6 A violation of Rule 3-310 does not automatically preclude an
7 attorney from obtaining his or her fees, as there is nothing in
8 Rule 3-310 that mandates a denial of fees. Pringle v. La
9 Chappelle, 73 Cal. App. 4th 1000, 1006 (Cal. Ct. App. 1999).

10 However, the court may refuse to grant an attorney fees for
11 services rendered if his or her relations with the client are
12 tainted with fraud or unfairness, or if the attorney commits acts
13 of impropriety inconsistent with the character of the legal
14 profession and incompatible with the faithful discharge of his or
15 her duties. Clark v. Millsap, 197 Cal. 765, 785 (Cal. 1926);
16 Mardirossian & Assocs., Inc. v. Ersoff, 153 Cal. App. 4th 257,
17 278 (Cal. Ct. App. 2007) ("In certain circumstances, a violation
18 of the Rules of Professional Conduct may result in a forfeiture
19 of an attorney's right to fees."); Cal Pak Delivery, Inc. v.
20 United Parcel Serv., Inc., 52 Cal. App. 4th 1, 14 (Cal. Ct. App.
21 1997) ("It is the general rule in conflict of interest cases that
22 where an attorney violates his or her ethical duties to the
23 client, the attorney is not entitled to a fee for his or her
24 services.").²⁸ See also Huskinson & Brown, LLP v. Wolf, 32 Cal.

25
26 ²⁸ At least three California appellate courts read Clark to
27 suggest that, before a court can require an attorney to forfeit
28 his or her fees, it should determine whether the violation of the
rules was sufficiently serious to warrant such a forfeiture. See
(continued...)

1 4th 453, 463 (Cal. 2004) (noting that courts have, on occasion,
2 disallowed quantum meruit recoveries to attorneys who violated
3 the California Rules of Professional Conduct) (citing Jeffry v.
4 Pounds, 67 Cal. App. 3d 6 (Cal. Ct. App. 1977); Goldstein v.
5 Lees, 46 Cal. App. 3d 614 (Cal. Ct. App. 1975)). In the exercise
6 of such discretion, some courts have allowed partial recoveries
7 of attorney's fees where there was no objection by the client,
8 where the client's recovery was a direct result of the attorney's
9 services, or for services rendered prior to the violation of the
10 rule. Cal Pak Delivery, Inc., 52 Cal. App. 4th at 16 (citations
11 omitted).

12 In this case, Park ideally would have obtained the debtors'
13 written consent at the outset of his representation of the
14 Trustee as special counsel. At the latest, following the trial
15 in the State Court Action, during the mediation and the
16 settlement negotiations encompassed thereby, Park would have
17 advised the debtors of the potential for conflict with the
18 Trustee and the bankruptcy estate in terms of the timing and
19 amount of a negotiated settlement and secured their informed
20 written consent to his continued representation. There is
21 nothing in the record before us showing that Park obtained the
22 debtors' written consent.

23 It was within the bankruptcy court's discretion to determine
24 whether a potential conflict existed and whether a violation by
25

26 ²⁸ (...continued)
27 Pringle, 73 Cal. App. 4th at 1006; Mardirossian, 153 Cal. App.
28 4th at 278; Sullivan v. Dorsa, 128 Cal. App. 4th 947, 965 (Cal.
Ct. App. 2005).

1 Park of Rule 3-310 constituted an act contrary to his ethical and
2 moral responsibilities as an attorney. In considering the
3 Employment Application, the bankruptcy court chose not to
4 disqualify Park, even though Park expressly disclosed that he was
5 bankruptcy counsel for the debtors at the time. The bankruptcy
6 court allowed the Trustee to employ Park because, as set forth in
7 the Employment Application, Park was employed for a limited,
8 specific purpose - to prosecute the State Court Action. Park was
9 not helping the Trustee in administering the bankruptcy estate.
10 The work that Park was performing as special counsel for the
11 Trustee in the State Court Action and the work that he was
12 performing for the debtors as their bankruptcy attorney were two
13 discrete matters. The bankruptcy court, aware of Park's
14 representation of the debtors at that time, still approved his
15 employment as special counsel pursuant to § 327(e).²⁹

16 When considering the Fee Application, the bankruptcy court
17 had the discretion to deny Special Counsel their fees in full or
18 in part, if it determined that Park had violated his ethical
19 duties. Although the bankruptcy court denied recovery of 50% of
20 the restitution waiver as part of Special Counsel's fees, it
21 awarded fees of 50% of the \$5 million cash recovered in the
22 settlement, even though the bankruptcy court was aware, as
23

24 ²⁹ Arguably, the debtors no longer had any interest in the
25 State Court Action. Upon filing for bankruptcy, all of the
26 debtors' legal and equitable interests became property of the
27 estate. See 11 U.S.C. § 541(a)(1). "Once the estate is created,
28 no interests in property of the estate remain in the debtor." 5
Collier on Bankruptcy ¶ 541.04. Only after all claims have been
paid and if funds remain do the debtors receive the surplus. See
11 U.S.C. § 726(a)(6).

1 demonstrated in its Memorandum Decision, of Park's failure to
2 obtain the debtors' written consent after disclosure, pursuant to
3 Rule 3-310.

4 Rule 3-310, in effect, encourages attorneys to make full
5 written disclosures of any conflicts, actual or potential, and to
6 obtain their clients' written consent prior to, or during the
7 course of continuing, representation. Park did not obtain such
8 written consent from the debtors.

9 However, when they took on the role as special counsel for
10 the Trustee, Park and SS&H took on a very difficult case in the
11 State Court Action for a contingent fee and litigated the State
12 Court Action through trial to a highly favorable result. That
13 result ultimately made the settlement, that will allow for
14 payment in full of all administrative expenses and allowed
15 creditor claims in the debtors' bankruptcy with a substantial
16 surplus to the debtors, possible. In these circumstances, even
17 though Park may not have complied strictly with the California
18 Rules of Professional Conduct, we nevertheless do not have a
19 "definite and firm conviction" that the bankruptcy court
20 committed a clear error of judgment in approving compensation to
21 Special Counsel. We conclude that the bankruptcy court did not
22 abuse its discretion in awarding the contingent fee of 50% of
23 monies collected to Special Counsel.

24
25 B. The bankruptcy court abused its discretion in awarding costs
26 to Special Counsel

27 The debtors contend that the bankruptcy court abused its
28 discretion in awarding costs to Special Counsel when Special

1 Counsel expressly stated in the Employment Application and in the
2 Statements that they would not recover costs.

3 Special Counsel claims that the debtors never once opposed
4 the request for costs on such grounds before the bankruptcy
5 court. Rather, the debtors opposed the request for costs on the
6 grounds that Special Counsel neither listed nor explained the
7 costs incurred in the Fee Application. Therefore, Special
8 Counsel argues, because the debtors never raised the issue before
9 the bankruptcy court, the debtors cannot raise it now on appeal.

10 We disagree. The debtors made various arguments against
11 Special Counsel's recovery of costs before the bankruptcy court –
12 that Special Counsel's \$2.5 million fee included costs, that
13 Special Counsel never mentioned recovery of costs at mediation,
14 that the debtors were deceived as to the terms of the fee
15 arrangement at the time of the Employment Application, that the
16 fee application set forth amounts unknown or unreviewed by the
17 debtors. Although the debtors articulated different reasons for
18 denying Special Counsel's costs, by simply disputing the costs,
19 the debtors called the bankruptcy court's attention to the issue.
20 See, e.g., United States v. One Urban Lot Located at 1 Street A-1
21 Valparaiso, Bayamon, Puerto Rico, 885 F.2d 994, 1001 (1st Cir.
22 1989).

23 As the debtors point out, the Employment Application and the
24 Statements expressly stated that Special Counsel would not
25 recover costs.³⁰ Also, the Employment Application Order made no

26
27 ³⁰ Indeed, in the Employment Application, Special Counsel's
28 representation that they would "not be paid at an hourly rate or
recover costs" could be interpreted as justifications for their

(continued...)

1 mention that Special Counsel would recover costs; rather, it
2 authorized the Trustee to employ Park and SS&H to act as special
3 counsel under the contingency fee arrangement as described in the
4 Employment Application. The bankruptcy court cannot award costs
5 where none were authorized in the Employment Application Order.
6 We conclude that the bankruptcy court abused its discretion in
7 awarding costs when Special Counsel failed to request them in the
8 Employment Application.

9 We note that the recovery of costs is a fairly standard form
10 of compensation for contingent fee attorneys. The Service
11 Agreement between the Trustee and Special Counsel typifies such
12 an arrangement; the Service Agreement explicitly provides for the
13 recovery of costs by Special Counsel, but also provides for their
14 deduction from the overall recovery prior to the calculation of
15 Special Counsel's contingent fee. Since the Trustee and Special
16 Counsel formalized the terms of compensation after the bankruptcy
17 court entered the Employment Application Order, Special Counsel
18 could have amended the Employment Application and requested
19 amendment of the Employment Application Order to provide for the
20 recovery of costs pursuant to the Service Agreement, after
21 providing notice and opportunity for objection to interested
22 parties, including the debtors. Special Counsel did not amend
23 the Employment Application or seek such an amendment to the
24 Employment Application Order.

27 ³⁰ (...continued)
28 request for a super priority lien on any recovery from the State
Court Action.

1 **VI. CONCLUSION**

2 Contrary to the debtors' assertions, Special Counsel did not
3 have a conflict of interest that would warrant the denial of
4 fees. Nor did the debtors demonstrate that Park's failure to
5 comply with Rule 3-310 of the California RPC requires denial of
6 Special Counsel's fees. Therefore, we conclude that the
7 bankruptcy court did not abuse its discretion in awarding fees to
8 Special Counsel and AFFIRM.

9 We determine, however, that the bankruptcy court abused its
10 discretion in awarding costs to Special Counsel. The Employment
11 Application and the Statements indicated that Special Counsel
12 would not recover costs. The Employment Application Order, which
13 was based on the Employment Application, did not authorize
14 Special Counsel to recover costs. Therefore, we REVERSE the
15 bankruptcy court's award of costs to Special Counsel.

16
17
18 PAPPAS, Bankruptcy Judge, concurring:

19
20 I disagree with the majority's conclusion that Park's
21 conduct in this case did not run afoul of the Bankruptcy Code.

22 Park served as the debtors' bankruptcy attorney from
23 December 17, 2002 until September 16, 2006, just a few days
24 before Trustee filed his motion to approve the Cigna settlement.
25 When Park undertook to serve as Special Counsel for Trustee in
26 August 2003, while simultaneously representing the debtors in the
27 bankruptcy case, he held at least a potential adverse interest as
28 to debtors. Park disclosed his "connection" with debtors and

1 they did not challenge his employment. Of course, since Park was
2 also advising the debtors at the time, their lack of objection to
3 his dual role is hardly surprising. While later problems could
4 have been avoided by prohibiting Park from also representing
5 Trustee, in an apparent exercise of discretion, the bankruptcy
6 court signed onto the arrangement.

7 Park's potential adverse interest blossomed into a full-
8 blown, actual conflict of interest when, in July 2006, Cigna laid
9 a \$5 million settlement offer on the negotiating table to avoid
10 possible liability for an even larger verdict. A settlement at
11 that amount was more than sufficient to pay all claims in the
12 bankruptcy case in full, so it is understandable that Trustee
13 would instruct "his" attorneys, including Park, to accept the
14 deal. On the other hand, whether the proposed compromise was
15 sufficient to compensate Song for the injuries he had suffered
16 over the years was a different, more difficult, question.

17 According to the record, Song acquiesced to the deal, but he
18 apparently did so based upon the advice of "his" attorney, Park.

19 To me, it is clear that, from the time the settlement offer
20 was made, Park's ability to give objective, reliable advice, and
21 his loyalty to Song, could be questioned. Park's continued
22 participation in this process violated § 327(e)'s prescription
23 that special counsel for a trustee "not hold any interest adverse
24 to the debtor or to the estate" Since he was
25 simultaneously representing both Song and Trustee, and because
26 their respective interests as to Cigna's settlement offer
27 potentially conflicted, Park should have played no further role
28 as either Special Counsel or as the debtors' attorney. Instead,

1 as it turns out, Park aligned with Trustee and against Song.³¹

2 Given this record, were I to substitute my judgment for that
3 of the bankruptcy court, perhaps a reduction in the amount of
4 Park's fees may have been in order to address his failure to
5 abide by the Code and ethical rules. But while Park's approach
6 was problematic, I do not have the firm conviction that it was an
7 abuse of discretion for the bankruptcy court to approve full fees
8 for Special Counsel in this case. Special Counsel obtained a
9 significant verdict for the bankruptcy estate and the debtors
10 against Cigna, which obviously motivated it to settle their claim
11 for a significant sum. As a result, under our deferential
12 standard of review, I concur in the majority's decision to affirm
13 the bankruptcy court's award of compensation.

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24 ³¹ I agree with the majority that, in advising Trustee and
25 Song about whether to settle, Park also violated California's
26 Rule 3-310. Subsection (C) of that rule prohibited Park from
27 continuing to represent more than one client in a matter in which
28 the interests of the clients actually conflicted, and subsection
of the Cigna claim without the "informed written consent of each
client."