NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re:	BAP Nos. HI-04-1172-MoRB
	HI-04-1181-MoRB
WORLDPOINT INTERACTIVE, INC., a Delaware corporation,	(cross-appeals)
	Bk. No. 02-00867
Debtor.	
	Adv. No. 03-90015
WAGNER CHOI & EVERS,	
Appellant/Cross-Appellee,	
v.	**M E M O R A N D U M**[1]
MARY LOU WOO, Chapter 7 Trustee,	
Appellee/Cross-Appellant.	

Argued by Telephone Conference
and Submitted on May 12, 2005

Filed - June 28, 2005

Appeal from the United States Bankruptcy Court
for the District of Hawaii

Honorable Lloyd King, Bankruptcy Judge, Presiding.

Before: MONTALI, RIMEL[2] and BRANDT, Bankruptcy Judges.

[1]This disposition is not appropriate for publication and may not be cited except when relevant under the doctrines of law of the case, res judicata, or collateral estoppel. See 9th Cir. BAP Rule 8013-1.

[2]Hon. Whitney Rimel, Bankruptcy Judge for the Eastern District of California, sitting by designation.

The debtor's former law firm asserted a secured claim against assets of the debtor. The trustee objected to the claim on many grounds, asserting (inter alia) that the transaction by which the firm obtained its security interest violated the Hawaii Rules of Professional Conduct, particularly the rule requiring a lawyer to give his or her client a reasonable opportunity to seek the advice of independent counsel before entering a business transaction in which the lawyer acquires a security interest adverse to the client. The bankruptcy court eventually entered a judgment determining that the firm had violated the ethical rules and that its security interest in the assets of the debtor was therefore invalid and unenforceable. The bankruptcy court also held that the firm was not negligent in providing certain legal advice to debtor. The bankruptcy court reserved for later resolution other issues pertaining to the trustee's claim objection.

The firm appealed the bankruptcy's court invalidation of its lien, while the trustee cross-appealed the bankruptcy court's determination that the firm had not acted negligently with respect to a different matter. We AFFIRM in both appeals.

I.
FACTS

A. Facts Relating to the Main Appeal

WorldPoint Interactive, Inc. ("WorldPoint" or "Debtor"), formerly known as Universal Resource Locator, Inc. ("URL"), is a

debtor under chapter 7 of the United States Bankruptcy Code.[3] Appellee Mary Lou Woo ("Trustee") is the trustee of Debtor's bankruptcy estate. Appellant Wagner Choi & Evers, LLP ("WCE") is a law firm that formerly represented Debtor. Massimo Fuchs ("Fuchs") and Larry Cross ("Cross")[4] were the directors of Debtor.

In June 1995, the State of Hawaii ("Hawaii") made a loan to URL. URL signed a security agreement in favor of Hawaii, which recorded a financing statement on June 20, 1995. On January 13, 1997, URL changed its name to WorldPoint, but Hawaii did not record a new or amended financing statement under Debtor's new name.

On November 11, 1997, Debtor executed a loan and security agreement in favor of Fuchs, granting Fuchs a blanket lien on Debtor's assets. Fuchs perfected his lien by recording financing statements in Delaware on August 4, 2001.

On June 8, 2001, Hawaii filed a collection action against Debtor in Hawaii state court (the "Collection Action"). On or about July 9, 2001, Debtor consulted with WCE in connection with the Collection Action and other matters. On behalf of WCE, James A. Wagner ("Wagner") executed a retention letter agreement ("Retention Agreement"), which Fuchs signed. The first sentence of the Retention Agreement states that "[t]his letter will confirm <u>that we have been retained</u> to represent you in connection

---

[3]Unless otherwise indicated, all chapter, section and rule references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330 and the Federal Rules of Bankruptcy Procedure, Rules 1001-9036.

[4]Cross is now deceased.

with the above matter." (Emphasis added). The "above matter" is identified as a "creditor workout." The Retention Agreement incorporated WCE's standard fee and retainer policy, but did not provide anywhere that Debtor would provide a security interest or lien to WCE to secure payment of fees. The letter required Debtor to pay a $2000 retainer; that amount was never paid. The letter did not specifically mention the Collection Action.

On July 18, 2001, Wagner contacted counsel for Hawaii in the Collection Action; Wagner indicated that WCE represented Debtor in the action and requested an extension of time in which to file an answer. On July 19, 2001, another attorney at WCE, James F. Evers ("Evers"), signed and faxed a letter to counsel for Hawaii confirming that WCE "is serving as counsel for WorldPoint" and that Hawaii had granted an extension of time for filing an answer. In this letter, Evers indicated that Debtor was contemplating an auction of its assets.[5]

On the morning of July 24, 2001, Evers sent another letter to Hawaii's counsel. This letter was similar to the July 19 letter, except that, inter alia, it changed the extension of time for filing the answer from July 31 to August 31, 2001, and refined the terms for depositing the proceeds from any auction into an escrow account. The letter also noted that Debtor "is

[5]There are several instances where testimony of Evers is inconsistent with documented evidence. For example, notwithstanding the fact that Evers signed and faxed the letter, he contended at trial that the letter was a draft. He also contended at trial that WCE did not represent Debtor with respect to the Collection Action, despite his confirmation in the letter that Hawaii had "graciously given us" (emphasis added) an extension of time to file an answer.

not admitting that the State of Hawaii has a valid lien[.]"[6]

Debtor, with the assistance of WCE, proceeded with plans to liquidate its assets through an auction. Hawaii agreed to allow the auction to proceed as long as the net sale proceeds were placed in an escrow account.[7]

The time records for Evers for July 24, 2001, indicate that he conferred with Wagner regarding a UCC-1 to cover litigation expenses and that he drafted a security agreement and financing statement. Fuchs testified that prior to that date, Evers had not discussed drafting a security agreement in favor of WCE. Evers filed a declaration stating that he had previously discussed with Fuchs the possibility of WCE obtaining a security interest in Debtor's assets.

On the afternoon of July 24, 2001, Evers called Fuchs and stated that he had developed a means for defeating Hawaii's purported security interest in Debtor's assets. He requested Fuchs to meet him that evening on a street corner in downtown Honolulu to sign some documents. After business hours, Evers presented documents to Fuchs which created a blanket security interest in favor of WCE in Debtor's assets. Fuchs testified

---

[6]In litigation discussed later, WCE (seeking to establish priority of its lien over that of Hawaii) convinced a state court that Hawaii's failure to record amended UCC-1 financing statements under WorldPoint's name (after URL changed its name to WorldPoint) defeated the first priority of Hawaii's lien.

[7]On July 16, 2001, Cross sent an e-mail to Fuchs (copied to Wagner) suggesting that any sale proceeds be placed in WCE's retainer/escrow account and not in Debtor's checking account "due to possible/probably [sic] State intervention." He added a postscript indicating that "I'm willing to assign all such residual values to Lawyer Wagner ASAP."

that Evers told him only that the security interest was to protect the auction proceeds from the claims of Hawaii and that WCE would not record documents relating to WCE's security interest unless necessary to protect those proceeds.

Evers brought Fuchs to the offices of another attorney for execution and notarization of a security agreement in the amount of $250,000.00. Fuchs testified that Evers did not discuss the terms or ramifications of the agreement; moreover, Evers did not advise Fuchs or Debtor to seek independent counsel and did not give Fuchs an opportunity to consult such counsel before executing the agreements. Fuchs executed the documents on behalf of Debtor, but was not given copies.[8]

The next day, WCE attempted to record the UCC-1 financing statements with the Bureau of Conveyances, State of Hawaii, but the office rejected it. On July 26, 2001, WCE recorded the

---

[8]Evers disagrees with this recitation of facts. He insists that Fuchs knew that WCE would require a security interest and that he discussed with Fuchs the security agreement in detail (although the Retention Agreement did not contain any reference to liens or other security interests).

In its Findings of Fact and Conclusions of Law, the bankruptcy court acknowledged the inconsistencies and conflicts between the testimony of Fuchs and the testimony of Evers. The court notes however, that even if Evers had discussed the transaction in as much detail and for as long (allegedly thirty minutes) as he contended, he still did not advise Fuchs to seek independent legal counsel and did not give Fuchs sufficient opportunity to consult another attorney. WCE did not cite to anything in the excerpts (such as testimony by Evers) to support its contention that Evers advised Debtor that it could consult with independent counsel. Moreover, as discussed later, WCE simply did not give Debtor a reasonable opportunity for such a consultation, inasmuch as the documents were drafted and signed on July 24, and WCE attempted to record the financing statements the following day (with actual recordation occurring in Hawaii on July 26).

financing statements in Hawaii. On the same day, Fuchs sent an e-mail to Wagner complaining that Evers had forced him to sign the security documents without providing him an opportunity to review them, that Evers had not provided copies, and that Evers had recorded the financing statements despite assurances that financing statements securing the 1997 loan from Fuchs to Debtor would be recorded first. Evers testified that upon receiving this e-mail, he terminated WCE's representation of Debtor.[9] Fuchs testified that WCE did not deny the allegations of his e-mail.

On July 25, 2001, Debtor and 1726, Inc. d/b/a Mark Glen Auctions ("Glen") executed an auction agreement whereby Glen agreed to sell Debtor's assets. The auction occurred on July 28, 2001. After the auction, Glen filed an interpleader action ("Interpleader Action") naming as defendants all parties with possible interests in the proceeds of the sale.

On or about August 4, 2001, Fuchs discovered that UCC-1 financing statements must be recorded in the state of incorporation (which, in Debtor's case, was Delaware). On that date, Fuchs recorded a UCC-1 financing statement in Delaware reflecting his security interest (arising from the 1997 security agreement) in Debtor's assets. On August 6, 2001, after Fuchs informed WCE of the necessity of recording in Delaware, WCE recorded its UCC-1 financing statement in Delaware. By agreement

[9]Fuchs does not agree. In any event, WCE resumed its representation of WCE and Fuchs did eventually inform WCE how to record its financing statement in Delaware and did eventually agree to subordinate his lien to that of WCE.

dated August 9, 2001, Fuchs agreed to subordinate his security interest to that of WCE.

Although WCE contends that it was not representing Debtor in the Collection Action when the Debtor executed a lien in favor of WCE, it did eventually agree to represent Debtor in the Collection Action "[b]ecause WCE would have to defeat [Hawaii's] lien claim in the [Interpleader Action] if WCE was to prevail on its own lien claim." Appellant's Opening Brief at pages 9-10.

WCE moved for summary judgment in the Interpleader Action, arguing that its lien against the assets of Debtor primed any lien of Hawaii. Hawaii filed its own motion for summary judgment. Before the state court could enter its written findings and conclusions with respect to the competing motions for summary judgment, an involuntary bankruptcy petition was filed against Debtor.

On March 15, 2002 (before the order for relief on the involuntary petition was entered on April 2, 2002), WCE filed a motion for relief from stay so that the state court could enter its findings of facts and conclusions of law in the Interpleader Action. In the memorandum in support of the motion for relief from stay, WCE states that the state court's ruling "will not necessarily be binding upon the bankruptcy [T]rustee" and that "WCE knows of no basis on which the [T]rustee could challenge [the Interpleader Action] ruling, but in any event if a basis exists the [T]rustee is not precluded from seeking appropriate relief." (Emphasis added.) In its reply in support of the motion for relief from stay, WCE states that the Interpleader Action "ruling is not binding on the bankruptcy [T]rustee; it is

binding as between the parties to the state court litigation" and that the "order on that point will not prejudice the bankruptcy [T]rustee." (Emphasis added.)

On April 16, 2002, the bankruptcy court granted relief from the stay so that the state court hearing the Interpleader Action could enter findings and an order "concerning the relative priorities of interests asserted by [WCE] and the State of Hawaii." (Emphasis added.) In the course of determining the relative priorities of liens, the state court held that WCE had a valid enforceable security interest.

On July 8, 2002, WCE filed a secured claim against Debtor in the amount of $114,364.59, which it amended on June 5, 2003. Trustee objected to the claim on many grounds, including allegations that WCE committed malpractice and violated various rules of professional conduct.[10]

The bankruptcy court treated the claims objection as an adversary proceeding and held a trial on October 27 and 28, 2003, and on January 20, 21 and 22, 2004. In its findings and conclusions issued after trial, the bankruptcy court held that because Debtor was not afforded a reasonable opportunity to consult independent counsel before granting a blanket lien in its assets to WCE, WCE had violated Hawaii's Rules of Professional

[10]Even though Federal Rule of Bankruptcy Procedure 8009(b) requires appellant to provide the panel with underlying papers pertaining to the order, neither WCE nor Trustee provided the objection to the claim in its excerpts of record. In addition, other pleadings and documents related to the objection and required by Rule 8009(b) are not included in the excerpts.

Conduct and its lien was thus invalid and unenforceable.[11] The bankruptcy court also indicated that unresolved issues remain pending with respect to Trustee's objection to WCE's claim.

On March 25, 2004, the bankruptcy court entered a judgment stating that WCE's security interest was invalid and unenforceable and treating WCE's amended proof of claim as a general unsecured claim.[12] WCE filed a timely notice of appeal on April 2, 2004.[13]

B. Facts Relevant to the Cross-Appeal

In 2001, Eicon, Inc. ("Eicon") filed an action against Debtor in California (the "Eicon Action"). On July 19, 2001, a messenger delivered an envelope containing a cross-complaint and other documents to Fuchs' home. Fuchs contends that he consulted with Evers about the service and that Evers indicated that service was improper because it should have been served by a sheriff (and not a messenger). According to Fuchs, Evers suggested that Fuchs e-mail opposing counsel in the California action and inform him about the improper service. Fuchs did send an e-mail to the opposing counsel objecting to the manner of service; that e-mail does not indicate that WCE had rendered any

---

[11]The bankruptcy court also ruled that WCE had not provided negligent legal services with respect to separate litigation initiated against Debtor in California. Trustee has cross-appealed this ruling, which is discussed in more detail in the next section.

[12]Neither WCE nor Trustee provided a copy of this judgment in their excerpts.

[13]WCE did not provide a copy of its notice of appeal in its excerpts.

advice in the matter. Fuchs acknowledged that WCE never agreed to represent Debtor in the Eicon Action.

Evers denied that WCE ever gave any advice to Fuchs regarding service of the cross-complaint in the Eicon Action. Evers further testified that he repeatedly informed Fuchs that WCE could not represent Debtor in the Eicon Action since it was pending in California where WCE's attorneys were not admitted to practice.

Opposing counsel in the Eicon Action communicated directly with Fuchs and informed him that service was proper. Nonetheless, Debtor never filed an answer and a default judgment was entered against Debtor in the Eicon Action in 2002.[14]

In her objection to WCE's claim, Trustee alleged that WCE provided negligent legal advice to Debtor with respect to service of the Eicon Action, thus leading to a default judgment against Debtor. The bankruptcy court disagreed, holding that "WCE was not negligent in providing legal service to [Debtor]."

The bankruptcy court did not enter an order or judgment with respect to the negligence count against WCE. The judgment entered on March 25 simply invalidated WCE's security interest and treated WCE's claim as an unsecured claim. Nonetheless, on April 6, 2004, Trustee filed a notice of appeal, cross-appealing "from the Findings of Fact and Conclusions of Law and Judgment."[15]

---

[14]The Eicon Action cross-complaint and default judgment are not in the excerpts.

[15]After the bankruptcy court issued its findings, Trustee was successful in setting aside the default and default judgment in the Eicon matter.

II.
ISSUES

1. Did the Rooker-Feldman doctrine preclude the bankruptcy court from entering an order invalidating WCE's security interests after a state court issued an order stating that WCE's security interest was valid?

2. Are the appeal and cross-appeal interlocutory and, if so, should this panel grant leave to appeal?

3. Did the bankruptcy court err in holding that WCE obtained its security interests in Debtor's assets in violation of the Hawaii Rules of Professional Conduct?

4. Did the bankruptcy court err in invalidating WCE's security interest because of WCE's violation of the Hawaii Rules of Professional Conduct?

5. Did the bankruptcy court err in holding that WCE did not provide negligent legal advice to Debtor?

III.
STANDARD OF REVIEW

A bankruptcy court's findings of fact are reviewed for clear error, and conclusions of law are subject to de novo review. Devers v. Bank of Sheridan, Montana (In re Devers), 759 F.2d 751, 753 (9th Cir. 1985). Review under the clearly erroneous standard is "significantly deferential, requiring a 'definite and firm conviction that a mistake has been committed.'" Granite State Ins. Co. v. Smart Modular Technologies, Inc., 76 F.3d 1023, 1028 (9th Cir. 1996) (quoting Concrete Pipe & Products of Cal., Inc. v. Construction Laborers Pension Trust for Southern Cal., 508 U.S. 602, 623 (1993)).

A bankruptcy court's findings of credibility are entitled to deference, because it is in a superior position to evaluate and weigh the evidence. See Exxon Co. v. Sofec, Inc., 54 F.3d 570, 576 (9th Cir. 1995), aff'd, 517 U.S. 830 (1996).

IV.
JURISDICTION

On March 9, 2005, this panel issued an order requesting the parties to file supplemental briefs addressing two jurisdictional issues: (1) whether the Rooker-Feldman doctrine precluded the bankruptcy court from entering an order invalidating WCE's blanket lien on Debtor's assets and (2) whether the appeal and cross-appeal were interlocutory and, if so, whether this panel should grant leave to consider the interlocutory appeals. The parties have filed their supplemental briefs.

A. The Rooker-Feldman Issue

As noted previously, the bankruptcy court entered an order granting relief from the stay to permit WCE to obtain an order from the state court in the Interpleader Action with respect to the relative priority of its security interest in Debtor's assets as against the security interest of Hawaii. On May 2, 2002, the state court entered its findings and conclusions and an order stating that "WCE holds a perfected security interest in the assets of [Debtor]" and that "WCE's perfected security interest in the assets of [Debtor] is a first priority lien against the assets of [Debtor]." The bankruptcy court's subsequent order, however, invalidates WCE's security interest inasmuch as it was obtained in violation of the Hawaii Rules of Professional Conduct.

Because the bankruptcy court's judgment seemed inconsistent with the state court order, this panel queried whether the Rooker-Feldman doctrine precluded entry of the subsequent bankruptcy judgment. See D.C. Court of Appeals v. Feldman, 460 U.S. 462, 486 (1983); Rooker v. Fid. Trust Co., 263 U.S. 413, 415-16 (1923); Huse v. Huse-Sporsem, A.S. (In re Birting Fisheries, Inc.), 300 B.R. 489, 497-98 (9th Cir. BAP 2003). Notably, WCE had not raised this as a issue, either before the bankruptcy court or before this panel.

In response, Trustee pointed to the numerous examples where WCE represented to the bankruptcy court in the context of its motion for relief from stay that the ruling of the state court would not bind Trustee. Remarkably, WCE did not mention these statements in its supplemental brief. To the extent WCE agreed on the record that the state court order and findings would not be binding on Trustee, the Rooker-Feldman doctrine is inapplicable to Trustee's subsequent objection to WCE's secured claim and the bankruptcy court's resulting order. At WCE's insistence and agreement, the Interpleader Action did not include any defenses or claims that could have been raised by the Trustee. WCE cannot now utilize preclusive devices such as the Rooker-Feldman doctrine to prevent the assertion of such claims, objections and defenses by Trustee before the bankruptcy court. Cf. Craig v. County of Maui, 157 F. Supp. 2d 1137, 1141 (D. Haw. 2001) (under Hawaii law, the defense of res judicata or claim preclusion "is deemed to have been waived by the defendant [i.e., WCE] where the first suit [i.e., the Interpleader Action] did not include the subject matter of the second [i.e., the claims

objection] at the insistence of the defendant [i.e., WCE]").[16]

In any event, after the panel issued its order requesting supplemental briefing, the United States Supreme Court issued Exxon Mobil Corp. v. Saudi Basic Indus. Corp., 544 U.S. ___, 125 S. Ct. 1517 (2005), which limits the Rooker-Feldman doctrine to cases in which "the losing party in state court filed suit in federal court after the state proceedings ended, complaining of an injury caused by the state-court judgment and seeking review and rejection of that judgment." 125 S. Ct. at 1526. Here, Trustee was not the losing party in state court; WCE acknowledged repeatedly in its pleadings in support of relief from stay that Trustee was not bound by the state court decision. Moreover, Trustee is not seeking to revisit the grounds supporting the state court's determination that WCE's lien primes Hawaii's lien; therefore, its objection to claim does not seek "review and rejection" of that order. Id.

Even if Trustee had been a party to the Interpleader Action, the Exxon Mobil decision clarifies that the Rooker-Feldman doctrine is inapplicable here, inasmuch as the bankruptcy court held concurrent jurisdiction over matters pertaining to the validity of WCE's security interest and claim at the time the state court entered its judgment. Bankruptcy courts have core

---

[16]See also Norfolk Southern Corp. v. Chevron U.S.A., Inc., 371 F.3d 1285 (11th Cir. 2004) (when a defendant signs a settlement agreement stating that only some claims will be precluded in the future, the defendant has preemptively waived any potential res judicata defense in future action; a party can agree to waive the defense of issue or claim preclusion); Clark v. Yosemite Comm. College Dist., 785 F.2d 781, 788 (9th Cir. 1986) ("a party who successfully blocks litigation of a cause of action in one proceeding may not hide behind the defense of res judicata in the second proceeding . . .").

jurisdiction over allowance and disallowance of claims and over determinations of the validity, extent or priority of liens against estate property. See 28 U.S.C. § 157 (b)(2)(B) and (K). WCE moved the bankruptcy court for relief from the stay so that the state court could enter a judgment, and acknowledged that Trustee could litigate similar issues in bankruptcy court. Because the bankruptcy case existed before the Interpleader Action judgment was entered (and where the bankruptcy court had to grant relief from the stay in order for the state court to even have jurisdiction to enter the judgment), the bankruptcy court held concurrent jurisdiction with the state court. Consequently, as noted by the Supreme Court in Exxon Mobil, the Rooker-Feldman doctrine is inapplicable:

> When there is parallel state and federal litigation, Rooker-Feldman is not triggered simply by the entry of judgment in state court. This Court has repeatedly held that 'the pendency of an action in the state court is no bar to proceedings concerning the same matter in the Federal court having jurisdiction.' [Citations omitted]. Comity or abstention doctrines may, in various circumstances, permit or require the federal court to stay or dismiss the federal action in favor of state-court litigation. [Citations omitted]. But neither Rooker nor Feldman supports the notion that properly invoked concurrent jurisdiction vanishes if a state court reaches judgment on the same or related question while the case remains *sub judice* in a federal court.

Exxon-Mobil, 125 S. Ct. at 1526-27 (emphasis added).

The Supreme Court in Exxon-Mobil states that in circumstances where the federal and state court have concurrent jurisdiction, disposition of the federal action would be governed by preclusion law. Id. at 1527. Therefore, at oral argument, counsel for WCE urged this panel to apply the principles of claim or issue preclusion. Claim and issue preclusion are not,

however, jurisdictional matters but are affirmative defenses. Id. at 1527; Contractors' State License Board of Calif. v. Dunbar (In re Dunbar), 245 F.3d 1058, 1063 n.5 (9th Cir. 2001) ("Rooker-Feldman is a jurisdiction-stripping doctrine while collateral estoppel and res judicata are affirmative defenses that have nothing to do with a federal court's jurisdiction."). Because issue and claim preclusion are affirmative defenses, they must be raised by a party before the trial court or they are waived. Horwitz v. State Bd. of Med. Examiners, 822 F.2d 1508, 1512 (10th Cir. 1987) ("Res judicata rules and principles . . . are waived if not raised as affirmative defenses in the trial court and cannot be raised for the first time on appeal . . . ."); American Capital Corp. v. U.S., 65 Fed. Cl. 241, 2005 WL 1023517 (Fed. Cl. 2005) (government waived defense of collateral estoppel by not asserting it in answer or raising issue in any motion before trial court before seeking reconsideration of order granting partial summary judgment). Because WCE did not raise the affirmative defenses of issue or claim preclusion before the trial court, and in fact did not raise these defenses in its opening appellate brief, we will not consider them on appeal. Smith v. Marsh, 194 F.3d 1045, 1052 (9th Cir. 1999) ("[A]n appellate court will not consider issues not properly raised before the [trial] court. Furthermore, on appeal, arguments not raised by a party in its opening brief are deemed waived.").

B. Interlocutory Jurisdiction

The bankruptcy court indicated in its findings of fact and conclusions of law that unresolved issues remain pending with respect to Trustee's objection to WCE's claim. As such, the

order is interlocutory. See Belli v. Temkin (In re Belli), 268 B.R. 851, 855 (9th Cir. BAP 2001) (an order that disposes of fewer than all the claims for relief is not final as to any of the claims for relief, unless the court directs the entry of a final judgment (under Federal Rule of Civil Procedure 54(b) and Rule 7054)) upon an express determination that there is no just reason for delay and upon an express direction for the entry of judgment); Slimick v. Silva (In re Slimick), 928 F.2d 304, 307 (9th Cir. 1990), citing United States v. F. & M. Schaefer Brewing Co., 356 U.S. 227, 234 (1958) (disposition is final if it contains a complete act of adjudication, fully adjudicates the issues at bar, and clearly evidences the judge's intention that it be the court's final act in the matter).[17]

Both WCE and Trustee request the panel to grant leave to hear this interlocutory appeal, since the issues have been fully briefed. Because both parties have requested leave, and because judicial economy and efficiency are served by having the appeals considered on their merits after full briefing, we will grant leave to hear both interlocutory appeals (the main appeal and the cross appeal). We do this reluctantly as to the cross appeal because there is no order expressly disposing of the Trustee's negligence claim against WCE, but it is clear that the bankruptcy court intended to dispose of that claim entirely.

---

[17]WCE argues in its supplemental brief that the decision is final. Not only does this contradict the bankruptcy court's own statement that other issues pertaining to the objection remain open, but it also ignores the possibility that even if this panel reversed the bankruptcy court's invalidation of the security agreement, the bankruptcy court could eventually disallow the claim in its entirety on other grounds.

V.
DISCUSSION

A. The Main Appeal

The bankruptcy court invalidated WCE's security interest because it concluded that WCE had violated Rule 1.8(a) ("Rule 1.8") of the Hawaii Rules of Professional Conduct in acquiring that interest. Rule 1.8(a) provides that

> (a) A lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless:
>
> (1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing to the client in a manner which can be reasonably understood by the client;
>
> (2) the client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; and
>
> (3) the client consents in writing thereto.

Hawaii Rules of Prof. Conduct, Rule 1.8 (emphasis added).

WCE contends that the bankruptcy court erred as a matter of fact (alleging that the court erred in concluding that Debtor was not given a sufficient opportunity to consult independent counsel) and as a matter of law (alleging that Rule 1.8(a) was inapplicable to its transactions with Debtor and further alleging that invalidation of the security interest was an improper remedy for a violation of Rule 1.8(a)). We disagree.

1. Factual Finding

The bankruptcy court found that WCE did not provide Debtor with a reasonable opportunity to seek the advice of independent counsel. On appeal, WCE argues that the bankruptcy court erred in making this factual finding. Among other things, WCE states

on page 23 of its opening brief (without citation to the excerpts of record) that "Fuchs was informed of [the right to have independent counsel review the security documents] and elected not to seek an independent review."

The record contains sufficient evidence to support the bankruptcy court's finding, including Fuchs' testimony and the fact that WCE's own time records indicate that the security documents were drafted on July 24, that the documents were presented to Fuchs and signed on the evening of July 24, and that WCE attempted record the financing statements on July 25 and then did record the financing statements in Hawaii on July 26. That time period simply did not give Debtor a reasonable opportunity to seek independent counsel.[18] Nothing in the record leaves this panel with a definite and firm conviction that the bankruptcy court's factual finding is incorrect. The bankruptcy court did not err.

2. Application of Rule 1.8(a) v. Rule 1.8(j)

WCE also argues that the bankruptcy court erred as a matter of law by applying Rule 1.8(a) instead of Rule 1.8(j) to the transactions between Debtor and WCE. As noted previously, Rule

---

[18]WCE argues that its security interest did not become perfected until it recorded its financing statements in Delaware on August 6 and that Debtor had an opportunity to consult independent counsel before that date. This argument is disingenuous, inasmuch as Evers admitted that he believed that the recording in Hawaii on July 26 was sufficient to perfect WCE's interests until informed otherwise by Fuchs. Evers intended for WCE's security interests to become perfected on July 25 (when he initially attempted to record the financing statements in Hawaii) and WCE's post hoc argument that another counsel could have been consulted prior to perfection is rejected.

1.8(a) requires that a lawyer give his or her client a reasonable opportunity to obtain the advice of disinterested counsel before the lawyer obtains a security interest adverse to a client.

WCE argues that subsection (a) of Rule 1.8 is inapplicable, because its transactions with Debtor are covered by subsection (j)[19] of Rule 1.8, which does not require that a client be provided with a reasonable opportunity to confer with independent counsel.

Subsection (j) of Rule 1.8 states that a lawyer "shall not acquire a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client, except that the lawyer may (1) acquire a lien granted[20] by law to secure the lawyer's fee or expenses; and (2) contract with a client for a reasonable contingent fee in a civil case." WCE contends that Rule 1.8(j)(1) is applicable because WCE was acquiring a lien on the subject matter of the Interpleader Action and the Collection Action. As discussed below, if WCE's lien did

---

[19]Subsection (j) has been moved to subsection (i) of Rule 1.8 of the Model Rules of Professional Conduct, upon which the Hawaii Rules of Professional Conduct are based. The Hawaii rules, however, have not adopted that particular change.

[20]Model Rule of Professional Conduct 1.8(i) (formerly 1.8(j)) states that the lawyer may acquire a lien "authorized" by law to secure the lawyer's fees or expenses, but Hawaii's Rule 1.8 states that the lien must be "granted" by law. This is a significant difference, as discussed later.

On February 7, 2005, WCE filed a Notice of Amendment of HRPC 1.8(j). According to WCE, the Hawaii Supreme Court (on February 1, 2005) entered an order amending Rule 1.8(j) to change "granted" to "authorized." According to the Supreme Court's order, however, the change does not become effective until July 1, 2005. Therefore, Rule 1.8(j) as currently drafted governs this appeal.

indeed fall within the scope of subsection (j)(1), subsection (a) is inapplicable.

On May 31, 2002, the American Bar Association issued ABA Formal Opinion 02-427 entitled "Contractual Security Interest Obtained By a Lawyer To Secure Payment of a Fee" (the "Opinion"). The Opinion indicates that a lawyer does not have to comply with the requisites of Model Rule 1.8(a) (i.e., allowing the client a reasonable opportunity to consult independent counsel) if the lawyer's security interest falls within the parameters of Model Rule 1.8(i) (formerly Rule 1.8(j)). Model Rule 1.8(i) permits a lawyer to acquire a lien in the "cause of action or subject matter of litigation" if the lien is "authorized" by law to secure the lawyer's fees or expenses. The Opinion notes that the term "authorized" was substituted in lieu of "granted" so that any legally recognized lien, such as consensual liens, would be included.[21]

Here, the Hawaii statute currently in effect does not use the more inclusive term "authorized." Rather, Rule 1.8(j) applies to liens "granted" by law. The lien acquired by WCE was not "granted" by law; it was "granted" by contractual agreement.

---

[21]WCE cites to several cases from other states (including Skarecky & Horenstein, P.A. v. 3605 North 36th St. Co., 170 Ariz. 424, 825 P.2d 949 (Ariz. 1992)) in which the court held that a lien "granted" by law encompasses consensual liens. No Hawaii case is cited. To the extent that the comments to Model Rule 1.8 indicate that the language was changed because courts construed "liens granted by law" to exclude consensual liens, WCE's cited cases are not persuasive. In any event, as noted below, even if the Rule 1.8(j)(1) refers to consensual liens, that subsection is still inapplicable because the assets upon which WCE acquired the lien existed before the security documents were executed. WCE's efforts in the Collection Action and the Interpleader Action did not involve the recovery of such assets for Debtor.

Rule 1.8(j) is thus inapplicable and the bankruptcy court did not err in applying Rule 1.8(a). In any event, the lien in question was not in "the subject matter of litigation." Even though the Interpleader Action involved a dispute as to whom held a secured interest in the funds, WCE's stance in that litigation was to protect its own security interest. In essence, the subject matter of the litigation was the lien itself. Moreover, WCE repeatedly contended that -- despite its communications with Hawaii's counsel and its Retention Agreement with Debtor -- that it did not represent Debtor in the Collection Action. According to its own admission in its Opening Brief, it commenced representation of Debtor in the Collection Action in order to protect its lien and interests in the Interpleader Action. WCE's contention now that it was taking a security interest in the subject matter of that litigation is unfounded, particularly when the subject matter of the Collection Action was Hawaii's efforts to collect on Debtor's obligations to it.

Even if the broader "authorized" language were contained in current Rule 1.8(j), WCE would not be sheltered from complying with Rule 1.8(a). As noted by the ABA in its Opinion (quoting the comments to the Model Rules): "When a lawyer acquires by contract a security interest in property other than that recovered by the lawyer's efforts in the litigation, such an acquisition is a business or financial transaction with a client and is governed by the requirements of paragraph (a)." (Emphasis added). Here, the Debtor had the assets before the security agreements with WCE were executed. WCE's efforts did not result in a recovery of those assets for Debtor, and its lien thus falls

outside the scope of subsection (j). The requirements of Rule 1.8(a) therefore apply.

For the foregoing reasons, we hold that the bankruptcy court did not err as a matter of law in applying the requirements of Rule 1.8(a) to WCE's security transactions with Debtor.

3. Proper Remedy for Violating Rule 1.8(a)

Citing only two Connecticut cases, WCE also argues that the bankruptcy court erred in invalidating WCE's lien as a punishment or remedy for WCE's violation of Rule 1.8. See Ankerman v. Mancuso, 830 A.2d 388, 393 (Conn. App. Ct. 2003), aff'd, 860 A.2d 244 (Conn. 2004) ("We conclude that under the facts, a violation of rule 1.8(j) of the Rules of Professional Conduct cannot be the sole basis to bar the enforcement of an otherwise valid promissory note and mortgage"), citing Noble v. Marshall, 579 A.2d 594 (Conn. App. Ct. 1990) ("[T]he Rules of Professional Conduct do not of themselves give rise to a cause of action, even to an attorney's client.").

Both of these cases are inconsistent with pertinent restatements, commentary and case law from jurisdictions other than Connecticut. For example, section 6 of the Restatement (Third) of Law Governing Lawyering entitled "Judicial Remedies Available To a Client or Nonclient for Lawyer Wrongs" provides that for "a lawyer's breach of a duty owed to the lawyer's client or to a nonclient, judicial remedies may be available through judgment or order . . . . Judicial remedies include . . . ordering cancellation or reformation of a contract, deed, or similar instrument[.]" Restatement (Third) of Law Governing Lawyering § 6 (2000) (emphasis added). Comment e to this

Restatement section provides:

> Cancellation of an instrument with otherwise legal effect would be appropriate when, for example, a lawyer obtains a deed to a client's property through undue influence in violation of limitations on business dealings with a client (see § 126) or on client gifts to lawyers (see § 127) or when the instrument was prepared by a lawyer representing clients with substantial conflicts of interests (see § 130). The remedy implements substantive standards applicable to lawyers as an expression of the strong public policy of the jurisdiction.

The Reporter's Note to Comment (e) further states:

> Cases setting aside such a contract or gift to a lawyer-recipient include Hicks v. Clayton, 136 Cal. Rptr. 512 (Cal. App. 1977) (lawyer's purchase of client's property with $14,000 in equity for $33 worth of stock was inequitable and subject to imposition of constructive trust, rescission, restitution, and incidental damages); Succession of Cloud, 530 So. 2d 1146 (La. 1988) (lawyer's violation of lawyer-code prohibition against acquisition of interest in client's mineral holdings as basis for nullifying transfer); Cuthbert v. Heidsieck, 364 S.W.2d 583 (Mo. 1963) (setting aside client gift of $20,000 in stock to lawyer) . . . .

Succession of Cloud, 530 So. 2d at 1150-51, is particularly instructive. In Cloud, an attorney acquired a proprietary interest in his client's mineral interest in violation of the Louisiana Code of Professional Responsibility. The Louisiana Supreme Court held that annulment of the contract transferring the proprietary interest to the attorney was the appropriate judicial remedy. Id. The court noted that the standards of the Code of Professional Responsibility have the force and effect of substantive law. "The disciplinary rules are mandatory rules that provide the minimum level of conduct to which an attorney must conform without being subject to disciplinary action. When an attorney enters into a contract with his client in direct and flagrant violation of a disciplinary rule and a subsequent civil

action raises the issue of enforcement (or annulment) of the contract, this court, in order to preserve the integrity of its inherent judicial power, should prohibit enforcement of the contract which directly contravenes the [Code of Professional Conduct]." Id. at 1150 (emphasis added).

Leading treatises on legal professional responsibility echo the sentiment of the Cloud court. For example, section 12.4 of The Law of Lawyering specifically provides that a violation of Model Rule 1.8(a) (which is identical to Hawaii's Rule 1.8(a) and which WCE violated) may result in a rescission of the offensive transaction or contract. See Geoffrey C. Hazard, The Law of Lawyering, 3d Ed. § 12.4 (2004 Supp.) ("Courts scrutinize lawyer-client transactions with special care, and may rescind the transaction or award damages for violating the principles underlying Rule 1.8(a).").[22]

The foregoing authorities are more persuasive than Ankerman and demonstrate that the bankruptcy court did not err as a matter of law in rescinding or voiding a transaction that violated Rule 1.8(a).[23] We therefore affirm.

---

[22]Trustee cites Lee v. Aiu, 936 P.2d 655 (Haw. 1997) in support of her argument that the bankruptcy court appropriately voided the transaction because it violated Rule 1.8(a). The court in Lee did refer the attorney to the Office of Disciplinary Counsel for violating Rule 1.8(a) (id. at 671) and did affirm a jury's determination that the attorney tortiously interfered with a contractual relationship, among other things. Lee, however, does not support Trustee's conclusion that the court rescinded a mortgage because of a violation of Rule 1.8(a).

[23]Interestingly, WCE did not cite a comment to the preamble to Hawaii's Rules of Professional Comment in its appellate briefs or to the bankruptcy court. In particular, comment [6] to the preamble (which does not have the force of a rule itself) states:

(continued...)

B. The Cross-Appeal

Trustee has appealed the bankruptcy court's finding that WCE was not negligent in providing legal service to Debtor with

---

[23](...continued)
Violation of a rule should not give rise to a cause of action nor should it create any presumption that a legal duty has been breached. The rules are designed to provide guidance to lawyers and to provide a structure for regulating conduct through disciplinary agencies. They are not designed to be a basis for civil liability. Furthermore, the purpose of the rules can be subverted when they are invoked by opposing parties as procedural weapons. The fact that a rule is a just basis for a lawyer's self-assessment, or for sanctioning a lawyer under the administration of a disciplinary authority, does not imply that an antagonist in a collateral proceeding or transaction has standing to seek enforcement of the rule. Accordingly, nothing in the rules should be deemed to augment any substantive legal duty of lawyers or the extra-disciplinary consequences of violating such a duty.

See Comment [6] to the Preamble [entitled "Scope"] of the Hawaii Rules of Prof. Conduct.

Notwithstanding the disclaimer that the professional rules are not designed to be the basis of civil liability, the rules do establish standards of conduct for attorneys. See Munneke & Davis, The Standard of Care in Legal Malpractice: Do the Model Rules of Professional Conduct Define It?, 22 J. Legal Prof. 33 (1998) ("The Preamble language [admonishing against using Rules as basis for civil liability] has been criticized as self-serving economic protectionism, drafted by the organized bar and the courts. In fact, . . . courts consistently cite ethical rules to support decisions that modify the standards of civil liability."). While perhaps an attorney may not be sued for affirmative damages because of his or her violation of the rules, he or she should not be able to retain property that was acquired unethically. We do not believe the preamble contemplates allowing an attorney to keep property or interests acquired in violation of the rules; like the Cloud court and Professor Hazard and the drafters of the Restatement (Third) of Law Governing Lawyering, we believe that when an attorney fails to comply with the requisites of Rule 1.8, the attorney's self-interested and unethical transaction should be voidable. Rescission of the offensive transaction is permissible.

respect to the Eicon Action. Under Hawaii law, there are four primary elements to a negligence claim:

> (1) A duty or obligation, recognized by the law, requiring the defendant to conform to a certain standard of conduct, for the protection of others against unreasonable risks;
>
> (2) A failure on the defendant's part to conform to the standard required: a breach of duty;
>
> (3) A reasonably close causal connection between the conduct and the resulting injury; and
>
> (4) Actual loss or damage resulting to the interests of another.

Doe Parents No. 1 v. State of Hawaii, 58 P.3d 545, 579 (Haw. 2002). "In order to prevail on a claim of professional negligence, a plaintiff must establish that defendant's negligence was the proximate cause of plaintiff's loss. Defendant's negligent conduct is the proximate cause of harm to plaintiff if the conduct is a 'substantial factor' in bringing about the harm." Goss v. Crossley (In re The Hawaii Corp.), 567 F. Supp. 609, 630-31 (D. Haw. 1983) (internal citations omitted) (emphasis added); see also Dunbar v. Thompson, 901 P.2d 1285, 1293 (Haw. Ct. App. 1995) ("[I]n Hawai`i, an actor's negligence can be a legal cause of harm to another only if such negligence is causative, i.e., a 'substantial factor in bringing about the harm.'") (internal quotations and citations omitted).

Here, Trustee bore the burden of proving the requisite elements of negligence, including causation. Miyamoto v. Lum, 84 P.3d 509, 523 (Haw. 2004). Trustee, however, did not demonstrate that any negligence by WCE was a "substantial factor" in bringing about harm to Debtor (i.e., the entry of the default judgment in the Eicon Action). The bankruptcy court found that WCE advised

Fuchs that the attempted service in the Eicon Action was invalid and "that Fuchs should tell plaintiff's counsel in the Eicon litigation to start over." Fuchs did so, and plaintiff's counsel disagreed in his response to Fuchs. Rather than file an answer upon receiving the response from plaintiff's counsel, Fuchs and Worldpoint simply chose to do nothing. (In fact, the record does not reflect that Fuchs even called WCE to advise it of the plaintiff's position). This decision, not WCE's advice, caused entry of the default judgment. Because WCE actions were not a "substantial factor" in any harm to Debtor, the bankruptcy court did not err in concluding that WCE was not negligent.

VI.
CONCLUSION

For the foregoing reasons, we AFFIRM in both the main appeal and the cross-appeal.