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OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re: DEXTER DISTRIBUTING CORP., et al., Debtors. _______________________________ TAYLOR R. COLEMAN, Appellant, v. STINSON MORRISON HECKER, LLP, Appellee. _______________________________	BAP No. AZ-09-1386-MkKiJu Bk Nos. 03-03546; 03-03548; 03-04695 through 03-04710; 03-05427; 03-11513; 03-11515; 03–04238; 07-01017 through 07-01019; 08-05785 (Jointly Administered) **MEMORANDUM**[*]

Argued and Submitted on
June 18, 2010, at Phoenix, Arizona

Filed - October 21, 2010

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

Honorable Randolph J. Haines, Bankruptcy Judge, Presiding

Appearances: Richard M. Lorenzen, Perkins Coie Brown & Bain P.A. for Appellant Taylor R. Coleman
C. Taylor Ashworth, Stinson Morrison Hecker LLP for Appellee Stinson Morrison Hecker LLP

Before: MARKELL, KIRSCHER and JURY, Bankruptcy Judges.

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

INTRODUCTION

Taylor Coleman, a former equity owner of the debtors, appeals the bankruptcy court's award of $3 million in fees and expenses to the debtors' counsel. For the reasons explained below, we AFFIRM.

FACTS

On March 5, 2007, New Castle Megastore Corporation ("New Castle"), self-described as "America's Leading Adult Retailer," filed Chapter 11 bankruptcy[1] after defaulting on lease payments for some of its stores. New Castle was joined in its filing by its distributor, Dexter Distributing Corporation ("Dexter"), as well as 1113 Progress Drive, Medford, LLC ("Medford"), an entity which owned one Castle megastore store in Medford, Oregon (collectively, the "Debtors").

On March 13, 2007, the bankruptcy court entered an order for the Debtors' cases to be jointly administered with the prior bankruptcy cases involving these companies or their predecessors,[2] as well as the personal bankruptcy of Taylor

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[1]Unless specified otherwise, all code, chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and all "Rule" references are to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037.

[2]On March 7, 2003, Castle Megastore Corporation ("Castle"), Dexter and the limited liability companies which owned Castle's real estate filed for Chapter 11. Pursuant to a plan confirmed on February 4, 2004, Dexter was reorganized with less debt; New Castle was created with some assets and liabilities of Castle; and the real estate companies were reorganized as Medford and Castle Realty Corporation ("Castle Realty"). Castle Realty owned all of New Castle's megastores, apart from Medford. Coleman owned 100% of the equity in all the debtors prior to those cases,

(continued...)

Coleman ("Coleman"), who owned a 40% equity ownership stake[3] in New Castle.

Although Coleman owned this equity stake, as well 100% of Castle Realty, Castle's creditors had been concerned about Coleman's prior mismanagement of the business. To induce them to vote for the 2004 plan, Coleman had agreed to place his voting interests in New Castle and Castle Realty into a voting trust until all the plan payments were completed. Vernon Schweigert, then Chief Restructuring Officer of Castle, and later Chairman of the Board of New Castle("Schweigert"), served as the trustee of the voting trust.

Thus, Coleman owned a substantial stake in New Castle and all of Castle Realty, but had no say in management decisions. He opposed the bankruptcy filings in 2007. This opposition set the stage for Coleman's later vociferous opposition to the Debtors' reorganization efforts.

The Debtors were represented by Stinson Morrison Heckler, LLP ("Stinson"),[4] which on March 14, 2007 applied for employment as Debtors' counsel pursuant to section 327(a). Coleman objected to Stinson's application on the grounds that Stinson was not

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(...continued)
and after the plan was confirmed he owned 40% of New Castle and 100% of Castle Realty. It does not appear that Coleman owned any of Dexter or Medford.

[3]In some filings, Coleman stated that he owned 80% of New Castle. The record is not clear if he owned 40% or 80%, but the actual percentage does not affect the disposition of this appeal.

[4]Stinson served as debtors' counsel in the cases from 2003. It also represented Castle Realty, after it filed in 2008.

disinterested and that it had failed to provide adequate disclosure about its potential conflicts.

Coleman specifically identified four reasons why Stinson was not disinterested. Initially, he pointed out that Stinson had received a payment from New Castle on account of an antecedent debt within the 90 days prior to the petition date.[5] As such, Stinson was the beneficiary of a preference and, therefore, a creditor and not disinterested. Next, Coleman argued that Stinson had a web of professional ties to Schweigert, the Chairman of the Board of New Castle.[6] According to Coleman, these ties meant that Stinson was conflicted because it could not act as “an objective fiduciary for the estate” or for the other “interest holders.” Furthermore, Coleman alleged that Stinson failed to provide adequate disclosure about its ties to Schweigert. Additionally, Coleman alleged that Stinson either directly or indirectly, in a formal or informal capacity, represented Castle Realty,[7] which “appear[ed] to be a creditor of New Castle,” and that this also constituted a preclusive conflict.[8] Finally, Coleman alleged that Stinson could not represent multiple debtors in this proceeding, because they had overlapping creditors and possibly divergent interests.

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[5]Later quantified as around $252,000 over the eight days before the petition date.

[6]And, as mentioned, previously the Chief Restructuring Officer of Castle.

[7]Castle Realty at that point was a non-debtor. It did not file its chapter 11 bankruptcy until 2008, and it also was ordered jointly administered with the prior cases.

[8]Coleman did not pursue this argument.

The bankruptcy court held a hearing on Stinson's employment application on March 19, 2007. Before that hearing, Stinson provided additional disclosures. The bankruptcy court heard Coleman's objections and rejected them all.

Addressing the alleged preference issue, the bankruptcy court noted that all of the parties, including Coleman, agreed that the Debtors were solvent.[9] As the Debtors were solvent, one of the essential elements of a preferential transfer was missing. See 11 U.S.C. § 547(b)(3).

As for the other alleged conflicts, the bankruptcy court did not find them to be preclusive either. It ordered additional disclosures pursuant to FED. R. BANKR. P. 2016, entered an interim order authorizing employment of Stinson, and was satisfied with

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[9]Coleman's counsel was insistent at the employment hearing that the Debtors were solvent, and therefore, the board of directors of New Castle owed Coleman fiduciary duties as a shareholder. Coleman's counsel further declared that the payment default which formed the basis of the bankruptcy filing could lead a "cynical person" to say that "it almost appears to be a manufactured default, because we have a solvent company" with substantial assets and a "great deal of cash flow." March 19, 2007 hearing transcript at 51:9-14. Coleman's counsel also requested the appointment of an examiner or trustee to protect Coleman's equity interests, as Coleman viewed the entire bankruptcy as a plot to steal his equity in the Debtors and remove him entirely from New Castle.

As discussed below, it is axiomatic that, if Coleman's equity interests in the Debtors had any value, then there must have been enough value in the companies to pay all unsecured creditors in full. 11 U.S.C. § 1129(b)(2)(B)(ii) (the "Absolute Priority Rule"). And it follows that if there was enough value to pay all the creditors, then any pre-petition payment Stinson might have received would not be a preference, because Stinson was not receiving more on account of the payment than it otherwise would have received.

It was also noted at the hearing that the Debtors intended to file a plan that called for paying all creditors in full.

Stinson’s additional disclosures. Coleman, on the other hand, was not satisfied. He subsequently and unsuccessfully objected to Stinson’s interim fee application.

On May 13, 2007, the Debtors proposed a plan that would have paid their creditors in full but which would have diluted Coleman’s equity interest. Not surprisingly, Coleman opposed that plan. In his opposition, Coleman insisted, as he did at the first-day hearing, that the Debtors were solvent, that they did not even have cash-flow problems, that there was no need for this bankruptcy in the first instance, and that any lease defaults were part of a scheme manufactured to rob him of his valuable equity in New Castle and Castle Realty. After much wrangling, this plan was withdrawn.

Several other plans were subsequently proposed and withdrawn, including a plan by Coleman. Under Coleman’s plan, he would have maintained his entire equity stake, while also paying all allowed, non-disputed claims in full. Meanwhile, on three separate occasions Coleman requested the appointment of a trustee or, in the alternative, an examiner. Each time, Coleman argued that since his equity in the Debtors had value, the directors of New Castle and Castle Realty owed him fiduciary duties and that they were violating these duties. A trustee, Coleman argued, would protect his equity stake from the depredations of the directors, or, in the alternative, an examiner would clarify the

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value of his equity and the fiduciary duties that the directors owed him.[10]

Finally, after contentious litigation over various plans, on May 19, 2009, the bankruptcy court confirmed a plan of reorganization filed by the Debtors. As it turned out, at that time, the estate was not solvent, and the equity was worthless.[11] The plan wiped out Coleman's equity in the Debtors and imposed losses on the creditors. On May 21, 2009, Coleman appealed the order confirming the plan to the federal district court for the District of Arizona. On March 18, 2010, the district court affirmed the bankruptcy court's confirmation of the plan and dismissed Coleman's appeal as moot. On April 16, 2010, Coleman appealed the district court's ruling to the Ninth Circuit Court of Appeals. That appeal is pending.

On August 20, 2009, Stinson filed its final application for fees and expenses. Although Stinson had incurred over $5 million in fees and costs over the course of the case, they agreed to accept $3 million to cover all their fees and expenses. Since they had been paid about $1 million on an interim basis, the outstanding balance of about $2 million was to be paid through the plan. The hearing on the fee application was originally scheduled for September 22, 2009, but the court granted two one-

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[10] The court eventually granted Coleman's motion for the appointment of an examiner. After the examiner completed his work, there was extensive litigation about the proper amount of his compensation.

[11] Whether the estate was solvent at the time of filing is the crucial issue and is discussed below.

month continuances, and the hearing was finally held on November 19, 2009.

On September 10, 2009, Coleman filed an objection to Stinson’s final fee application. Neither then or at any time afterwards, however, did he request an evidentiary hearing on the reasonableness of the fees and expenses in the manner required by Arizona Local Bankruptcy Rule 9014-2(b).

In his objection, Coleman reiterated his arguments that Stinson had received a preference, and that Stinson had conflicts arising from its representation of multiple debtors and from its prior professional relationships with Schweigert. Coleman added a new argument, that the $3 million in fees that Stinson requested were not reasonable in light of the recovery to the creditors from the bankruptcy proceeding. Coleman also asserted that the bankruptcy court needed to hold an evidentiary hearing on the reasonableness of Stinson’s fee request, although he did not follow the local rules in requesting such hearing. Coleman concluded by asking the bankruptcy court to deny the final fee application and to require Stinson to disgorge all fees it already had received.

At the November 19, 2009 hearing on the fee application, Coleman’s attorney repeated his four objections. The bankruptcy court first addressed the three “conflicts,” declaring:

> . . . it strikes me that most of these objections were previously raised and decided and I have no new evidence and no evidence that clear error was made at the time of that decision and that applies to the preference objection, the relationships with Schweigert and the conflicts between the Debtors.
>
> I do think that at least when the facts are available and known, it's appropriate that those objections be raised at the time of employment of counsel

> and they were and they were decided. . . . I don't think it's appropriate then after employment has been authorized for the Court to revisit those based upon the same facts and same arguments that were initially considered at the time of authorization of the employment.

November 19, 2009 hearing transcript at 34:3-18.

The bankruptcy court then discussed the reasonableness of the fees incurred by Stinson in connection with the various unconfirmed plans:

> . . . I really have a hard time going there [finding Stinson’s fees unreasonable for the first, unconfirmed plan] given the number of creditors that supported that plan, including . . . the Unsecured Creditors Committee. . . . it would be very hard to make a determination that was such an unreasonable plan, not [sic] fee should be awarded for pursuing it. In addition, I do think –- I don't think there's any debate about this, that if that plan were confirmed, the result would have been a lot better . . . for all of the other unsecured creditors than what ultimately was confirmed.
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> So on that basis, I think it would be hard to say that fees should not be awarded for pursuing a plan like that, especially in light of the Ninth Circuit standard. . . . We judge [the services provided] with foresight and that is when this work was being done was it reasonable to conclude it would have a benefit to the estate?

November 19, 2009 hearing transcript at 35:21-36:13.

As for the need for an evidentiary hearing (which Coleman never requested in the manner required by the bankruptcy court’s local rules), the bankruptcy court declared:

> I don’t . . . need to have an evidentiary hearing on that because . . . I can't believe by any stretch of the imagination it's [the amount of Stinson’s unreasonable fees] going to approach two million dollars out of the total five million that's at stake.
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> * * *
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> And short of saying that, you know, almost 40 percent of what went on in this case shouldn't have been done, at the end of the day, it doesn't really matter. We'd still be down to allowance of fees in the total amount of $3 million which is all that's going to

> be paid under the plan anyway. And for that reason, I don't see that there's any really fact dispute here that necessitates an evidentiary hearing.

November 19, 2009 hearing transcript at 36:14-37:6.

Based on those rulings, the bankruptcy court approved $3 million in fees to Stinson. Coleman has appealed this fee award, arguing that the bankruptcy court erred by finding that the conflicts Coleman alleged were not preclusive and by finding that Stinson made adequate disclosures. Coleman also argues that the bankruptcy court erred in not conducting an evidentiary hearing on the reasonableness of Stinson's fees, and instead relying on the pleadings and the submitted evidence of the parties.

JURISDICTION

The bankruptcy court had jurisdiction under 28 U.S.C. §§ 1334 and 157(b)(2)(A). We have jurisdiction under 28 U.S.C. § 158, subject to our resolution of the standing issue discussed immediately below.

All litigants must have the "irreducible constitutional minimum" of standing under Article III of the Constitution.[12] As a bankruptcy appellant, Coleman must also meet the requirements

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[12]To establish standing under Article III, a party must demonstrate that:

> (1) it has suffered an injury in fact that is (a) concrete and particularized and (b) actual or imminent, not conjectural or hypothetical; (2) the injury is fairly traceable to the challenged action of the defendant; and (3) it is likely, as opposed to merely speculative, that the injury will be redressed by a favorable decision.

City of Sausalito v. O'Neill, 386 F.3d 1186, 1197 (9th Cir. 2004)(quoting Friends of the Earth, Inc. v. Laidlaw Envtl. Servs. (TOC), Inc., 528 U.S. 167, 180-81 (2000)).

of the "prudential appellate standing doctrine." Shortly after Congress enacted the Bankruptcy Code in 1978, the Ninth Circuit applied the "person aggrieved" appellant standing test from the 1898 Bankruptcy Act[13] to the new Code and held that:

> Only those persons who are directly and adversely affected pecuniarily by an order of the bankruptcy court have been held to have standing to appeal that order. . . . Thus, a hopelessly insolvent debtor does not have standing to appeal orders affecting the size of the estate. . . . Such an order would not diminish the debtor's property, increase his burdens, or detrimentally affect his rights.[14]

Fondiller v. Robertson (In re Fondiller), 707 F.2d 441, 442 (9th Cir. 1983) (citations omitted).

Thus, an equity owner "that has no hope of obtaining any return from its estate" would "lack standing to contest orders

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[13]Section 39c of the 1898 Bankruptcy Act permitted an appeal only by a "person aggrieved by an order of a referee." When Congress enacted the 1978 Bankruptcy Code, it did not include a similar provision. However, the Supreme Court has counseled bankruptcy courts to remember that, when Congress amends existing statutes, it "does not write on a clean slate." Dewsnup v. Timm, 502 U.S. 410, 417 (1992). Courts should thus not "'read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure.'" Travelers Cas. and Sur. Co. of America v. Pacific Gas and Elec. Co., 549 U.S. 443, 454 (2007) (quoting Cohen v. de la Cruz, 523 U.S. 213, 221 (1998)) (in turn quoting Pennsylvania Dept. of Public Welfare v. Davenport, 495 U.S. 552, 563 (1990)).

Thus, the Ninth Circuit found that the prudential appellate standing doctrine filled "the need for an explicit limitation on standing to appeal in bankruptcy proceedings" since "bankruptcy litigation . . . almost always involves the interests of persons who are not formally parties to the litigation." In re Fondiller, 707 F.2d at 443.

[14]"This 'person aggrieved' requirement is more exacting than the requirements for general Article III standing." In re Andreuccetti, 975 F.2d 413, 416 (7th Cir. 1992).

affecting the size of the estate," which would include his or her ability to challenge a fee award to the debtor's counsel. In re J. M. Wells, Inc., 575 F.2d 329, 331 (1st Cir. 1978)(finding in a case under Chapter XI of the Bankruptcy Act that the equity owner had no standing to appeal a fee award in a case in which he would have "no financial interest") partially superseded by statute on other grounds, see Boston & Maine Corp. v. Sheehan, Phinney, Bass & Green, P.A., 778 F.2d 890, 898 (1st Cir. 1985).

Here, even if we reversed the bankruptcy court's order awarding Stinson $3 million in fees, and those estate funds instead were available to pay allowed claims, the Debtors would still be "hopelessly insolvent," In re Fondiller, 707 F.2d at 441. Since all creditors must be paid in full before the equity owners receive any distributions from the estate, 11 U.S.C. § 1129(b)(2)(B), Coleman would have "no further interest" in the estate. Hartman Corp. of America v. United States, 304 F.2d 429, 430 (8th Cir. 1962)(noting that "practical common sense need not be entirely divorced from bankruptcy proceedings" and denying standing to the equity owner to challenge an allowed tax claim against his "hopelessly bankrupt corporation").

Thus, on the basis of his equity stake in the Debtors, Coleman is not "aggrieved in a legal sense and has no standing to appeal from th[e] order" awarding fees to Stinson. Castaner v. Mora, 216 F.2d 189 (1st Cir. 1954); see also Skelton v. Clements, 408 F.2d 353, 354 (9th Cir. 1969); United States v. Fingers (In re Fingers), 170 B.R. 419, 425 (S.D. Cal. 1994) ("Since the bankrupt is normally insolvent, he is considered to have no interest in how his assets are distributed among his creditors and is held not to be a party in interest.")

However, Coleman has also filed a proof of claim for "a minimum" of $37 million, alleging that the Debtors improperly destroyed their "going concern value" and that the Debtors failed to pay him wages and other compensation.[15] If we overturned the bankruptcy court's fee award to Stinson, and Debtor's estate was consequently increased by $3 million, as a creditor, Coleman would then be "affected pecuniarily" because it would increase his recovery from the estate. It is exclusively on the basis of this claim - which holds the sole possibility of a recovery for Coleman - and not on the basis of his equity holdings that Coleman has standing to contest Stinson's fee award.

ISSUES

1. Did the bankruptcy court err when it found that Stinson did not receive a facially plausible preference before the petition date?

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[15]As pointed out by the Debtors in their February 20, 2009 Supplemental Disclosure to Accompany Modification of First Amended Joint Plan of Reorganization ("Supplemental Disclosure"), they have objected to Coleman's $37 million proof of claim, or alternately will attempt to subordinate his claim to the other claims in his class. The Supplemental Disclosure also listed an estimated range of recoveries to Coleman's class of creditors based on the bankruptcy court hypothetically allowing Coleman's claim in different amounts.

However, even though Debtors have objected to Coleman's claim (see docket entry 2460, December 17, 2008), the bankruptcy case docket indicates that the bankruptcy court has not yet heard or determined Coleman's claim. Of course, if Coleman's claim were disallowed in its entirety, he would no longer be "affected pecuniarily" by the bankruptcy court's fee award to Stinson and thus would lack standing to appeal the fee award.

2. Did the bankruptcy court err when it found that Stinson made adequate disclosures and that Stinson did not suffer from any preclusive conflicts?

3. Did the bankruptcy court err by not holding an evidentiary hearing, or when it found that Stinson's fees were reasonable?

STANDARDS OF REVIEW

We review findings of fact for clear error and issues of law de novo. United States v. Gould (In re Gould), 401 B.R. 415, 421 (9th Cir. BAP 2009). Construction of rules of procedure and the Bankruptcy Code present questions of law that we review de novo. Litton Loan Serv'g, LP v. Garvida (In re Garvida), 347 B.R. 697, 703 (9th Cir. BAP 2006); Ruvacalba v. Munoz (In re Munoz), 287 B.R. 546, 550 (9th Cir. BAP 2002).

A bankruptcy court's award of attorney fees will not be disturbed unless the bankruptcy court abused its discretion. Leichty v. Neary (In re Strand), 375 F.3d 854, 857 (9th Cir. 2004). The bankruptcy court's decision not to conduct an evidentiary hearing also is subject to review under the abuse of discretion standard. See Tyner v. Nicholson (In re Nicholson), 435 B.R. 622, 629 (9th Cir. BAP 2010). Under this standard, we apply a two-part test. First, we consider de novo whether the bankruptcy court identified the correct law to consider in light of the relief requested. United States v. Hinkson, 585 F.3d 1247, 1262 (9th Cir. 2009). Second, we review the bankruptcy court's factual findings, and its application of those findings to the relevant law, to determine whether they were either "(1) 'illogical,' (2) 'implausible,' or (3) without 'support in inferences that may be drawn from the facts in the record.'" Id. (quoting Anderson v. City of Bessemer City, N.C., 470 U.S. 564, 577 (1985)).

DISCUSSION

A. The bankruptcy court did not err when it found that Stinson did not receive a facially plausible preference.

The Debtors paid Stinson $252,000 on account of an antecedent debt eight days before the Debtors filed bankruptcy. A bankruptcy estate has broad powers to avoid payments made to creditors under certain circumstances. One of those powers is the ability to avoid a preferential payment to a creditor. Section 547 provides:

> (b) Except as provided in subsections (c) and (i) of this section, the trustee may avoid any transfer of an interest of the debtor in property—
> (1) to or for the benefit of a creditor;
> (2) for or on account of an antecedent debt owed by the debtor before such transfer was made;
> (3) made while the debtor was insolvent;
> (4) made—
> (A) on or within 90 days before the date of the filing of the petition; or
> (B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and
> (5) that enables such creditor to receive more than such creditor would receive if—
> (A) the case were a case under chapter 7 of this title;
> (B) the transfer had not been made; and
> (C) such creditor received payment of such debt to the extent provided by the provisions of this title.

11 U.S.C § 547.

A debtors' counsel - or any estate professional - who is the beneficiary of a preference is in a precarious position:

> First, if [the debtor's counsel] actually did receive an avoidable preference then he would be ineligible to be paid anything from the estate unless and until he returns that preference. Second, if [the debtors' counsel]

> actually did receive an avoidable preference then he would probably be ineligible for employment, no matter how completely he disclosed the relevant facts, at least until he returns the preference . . . As one court has put it, he would be unlikely to sue himself.

Movitz v. Baker (In re Triple Star Welding, Inc.), 324 B.R. 778, 793 (9th Cir. BAP 2005), partially abrogated on other grounds, Dye v. Brown (In re AFI Holdings, Inc.), 530 F.3d 832 (9th Cir. 2008)(citing Staiano v. Pillowtex (In re Pillowtex, Inc.) 304 F.3d 246, 254 (3d Cir. 2002)).

We have adopted the test set out in In re Pillowtex, declaring that “where there is a ‘facially plausible’ preference claim then the preference issues must be resolved before proposed counsel can be employed (or compensated).” In re Triple Star Welding, 324 B.R. at 794 (citing In re Pillowtex, 304 F.3d at 254)).

An essential element of a preference claim is that the payment at issue was “made while the debtor was insolvent.” 11 U.S.C. § 547(B)(3). Section 547(f) supplies a presumption that debtors are insolvent “on and during the 90 days immediately preceding the date of the filing of the petition.” 11 U.S.C. § 547(f).

Coleman claims that the $252,000 payment to Stinson was an avoidable preference. As the beneficiary of a preference, Stinson would be ineligible to be employed and paid.[16] Stinson counters that the Debtors were solvent pre-petition[17] when it

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[16]At least until Stinson repaid the preferential payment. In re Triple Star Welding, 324 B.R. at 793.

[17]And indeed continued to be solvent for long after that date as well.

received the $252,000. If the Debtors were solvent, then the essential element of section 547(b)(3) was not present. Further, the payment did not enable Stinson "to receive more than [Stinson] would receive if . . . the transfer had not been made," section 547(b)(5), because Stinson would have been entitled to a bankruptcy recovery in that same amount in any event. As such, Stinson did not receive an avoidable preference and so was eligible to be employed as debtor's counsel.

Belying Coleman's contrary assertions, the record is clear that at the time the Debtors filed for bankruptcy, both parties acted in ways and took positions predicated on the understanding that the Debtors were solvent. At the onset of the case, all of the parties unequivocally asserted that the Debtors were solvent. The Debtors quickly proposed a plan that preserved some value for equity; it is axiomatic that if the equity holders were to retain any of their equity on account of their prepetition interest that all creditors would be paid in full. 11 U.S.C. § 1129(b)(2)(B)(ii).[18]

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[18]That section provides in relevant part:

> (1)[T]he court, . . . shall confirm the plan notwithstanding . . . if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.
> (2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements: . . .
> (B) With respect to a class of unsecured claims—
> (ii) the holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property.

11 U.S.C. § 1129(b).

Moreover, throughout the case, Coleman himself repeatedly argued that the Debtors were solvent. His counsel stated that the Debtors were solvent at the interim employment hearing on March 19, 2007. Coleman's counsel declared that the Debtors were solvent in his three requests to appoint a trustee, the most recent of which he filed on May 16, 2008. And Coleman's counsel asserted that the Debtors were solvent in the plan he proposed on June 12, 2007, under which Coleman would have retained his entire equity stake in the Debtors.

These actions and positions taken by Coleman and the Debtors are understandable only if they all believed that the Debtors were solvent prepetition. It was against this background that the bankruptcy court accepted the parties' assertions and was able to determine that Stinson was not the beneficiary of a "facially plausible" preference. When the bankruptcy court made this finding, there was a crucial difference between this case and <u>Triple Star Welding</u> and <u>Pillowtex</u>: unlike the law firms in those cases, Stinson followed the Bankruptcy Code and the Rules of Bankruptcy Procedure and disclosed the pre-petition payments. As we have explained, disclosure "is critical because . . . until the bankruptcy court can determine whether [the attorney] was properly employed it is premature to award him fees." <u>In re Triple Star Welding</u>, 324 B.R. at 794.

There is no evidence in the record indicating that Debtors were insolvent prepetition, and we therefore hold that the bankruptcy court did not err in crediting the parties' assertions that the Debtors were solvent at the time of their bankruptcy filings. In light of the Debtors' solvency at that time, the bankruptcy court correctly and properly inferred that Stinson could not have been the beneficiary of a “facially plausible” preference.

Coleman could have requested an evidentiary hearing to determine the Debtors’ solvency. But - for over a year - Coleman was content to take the opposite position and argue that the Debtors were solvent and therefore his equity had value. It is too clever by half - if not outright disingenuous - for Coleman to take a litigation position for over a year post-petition that would retain value for his equity, and then take the opposite position in an attempt to disallow Stinson’s fees and expenses.

Coleman makes three additional arguments in attempting to demonstrate that the bankruptcy court erred in not finding that the Debtors were insolvent. He argues that: 1) the Debtors were insolvent when their plan was confirmed; 2) an ambiguous statement by the bankruptcy court in the confirmation order “proves” that the bankruptcy court found that the Debtors were insolvent on the petition date; and 3) the Debtors’ schedules appear to indicate that their liabilities exceeded their assets as of the petition date. None of these arguments are persuasive.

Initially, Coleman points out that the Debtors were insolvent when their plan was confirmed in 2009. So they were, but this does not show that Stinson received a facially plausible preference as of the petition date. It does no more than show that after two years of bitter litigation and reorganization efforts opposed at every turn by Coleman, as well as two years of upheaval and reverses in the adult entertainment market, the real estate market in the American Southwest, and in the American and global financial and credit markets, the Debtors were insolvent when their plan was confirmed. But subsequent dislocations and the resulting decline in the value of the Debtors' estates do not undermine the bankruptcy court's acceptance of the Debtors' and Coleman's claims that the Debtors were solvent on the petition date; nor should it obscure Coleman's own claims (as late as May 2008) that the Debtors were solvent.

Next, Coleman points to the following statement by the bankruptcy court in its confirmation order:

> Virtually since the inception of this bankruptcy case Coleman has maintained that the bankruptcy filing was unnecessary and the default under the 2004 Plan was manufactured as a litigation strategy to extinguish his stock interest. About the only evidence he ever cited, however, was an e-mail [sent from a board member to an investor] . . . concerned that distributions were not being made pursuant to the 2004 Plan. At trial, however, the uncontroveted evidence established that the Debtor was both seriously insolvent and unable to pay its obligations as they became due in the next year or two.

May 19, 2009 Findings of Fact and Conclusions of Law at 2:10-16. Coleman interprets this to mean that the bankruptcy court made an explicit finding the Debtors were insolvent on the petition date. However, when read in context, the quoted findings merely demonstrate that the bankruptcy court found that the Debtors were insolvent on the confirmation date.[19]

Finally, Coleman points out that, on their amended schedules, the Debtors listed around $6.3 million in assets and $33.1 million in liabilities.[20] This is facially correct; however, as Stinson explained at oral argument, the listed

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[19]Moreover, this finding by the bankruptcy court also demonstrates Coleman's insistent contention that the Debtors were solvent on the petition date and undermines Coleman's argument on insolvency.

[20]On the Debtors' initial schedules, they listed $0 of assets.

liabilities exceeded the listed assets because the Debtors listed the full face amounts of debts (including guaranties and debts for which they were co-obligors), even if they were not fully responsible for repayment, but did not list assets that they did not own in full.

Therefore, we conclude that the bankruptcy court did not err when it found that Stinson was not the recipient of a facially plausible preference as of the petition date.

B. The bankruptcy court did not err when it found that Stinson made adequate disclosures and that Stinson did not suffer from preclusive conflicts.

Sections 327 and 328 lay out the professional obligations for attorneys in representing debtors, and provide important limitations on their ability to receive compensation.

Section 327(a) states:

> The trustee,[21] with the court's approval, may employ one or more attorneys . . . or other professional persons, that do not hold or 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.

11 U.S.C. § 327(a). As we have explained:

> Section 327(a) requires the application of a two-pronged test for the employment of professional persons. A debtor in possession or trustee may employ attorneys with court approval only if (1) they do not hold or represent an interest adverse to the estate and (2) they are disinterested persons. . . . To represent an adverse interest means to serve as an attorney for an entity holding such an adverse interest. . . . For the purposes of disinterestedness, a lawyer has an interest materially adverse to the interest of the estate if the lawyer either holds or represents such an interest.

[21]As the debtor in possession, New Castle has the status of a trustee in this case.

Tevis v. Wilke, Fleury, Hoffelt, Gould & Birney, LLP (In re Tevis), 347 B.R. 687-88(9th Cir. BAP 2006).

Section 328 provides that the bankruptcy court:

> May deny allowance of compensation for services and reimbursement of expenses of a professional . . . if, at any time during such professional person's employment . . . 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.

11 U.S.C. § 328(c).[22]

The linchpin of bankruptcy-professional employment is disclosure. "Full disclosure is an essential prerequisite for both employment and compensation . . . [o]nce the true facts are known the bankruptcy court had considerable discretion in determining whether to disallow all, part or none of the fees and expenses of a properly employed professional." In re Triple Star Welding, 324 B.R. at 781.

Here, Stinson filed three disclosure statements before the bankruptcy court approved its employment application. The bankruptcy court was ultimately satisfied with the adequacy of those disclosures.[23] Once the bankruptcy court was in possession

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[22]Interestingly, notwithstanding these sweeping statements, in at least one instance, we have held that the bankruptcy court had discretion to award compensation for services preformed in reliance on an order authorizing employment, before that order was reversed on appeal. See First Interstate Bank of Nevada v. CIC Inv. Corp. (In re CIC Inv. Corp.) 192 B.R. 549, 553-54 (9th Cir. BAP 1996).

[23]To be sure, an attorney's compliance with the disinterestedness requirement under § 327(a) not only applies at

(continued...)

of what it found to be "the true facts," In re Triple Star Welding, 324 B.R. at 781, it was in the best position to evaluate the adequacy of that disclosure and any potential resulting conflicts.

At the initial hearing on Stinson's employment, the bankruptcy court found that Stinson was not conflicted from serving as Debtors' counsel. At the hearing on Stinson's final fee application it was ultimately satisfied that Coleman had adduced "no evidence" since the initial hearing "that clear error was made at the time of that decision." Coleman does not argue on appeal that Stinson failed to disclose "the true facts." Rather, Coleman argues that the bankruptcy court erred – after evaluating Stinson's exhaustive disclosure – in its conclusion that Stinson was disinterested. But there is nothing in the record to indicate that the bankruptcy court "abused its broad discretion to approve employment and award fees after the true facts are known." In re Triple Star Welding, 324 B.R. at 781. To the contrary, after it was in possession of the facts, the bankruptcy court found that there were no conflicts that prevented Stinson's employment.

In sum, Coleman has not established that the bankruptcy court erred when it found that Stinson did not suffer from any preclusive conflicts from its representation of multiple debtors

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(...continued)
the time of retention but also throughout the case. In re Plaza Hotel Corporation, 111 B.R. 882, 891 (Bankr. E.D. Cal. 1990) (the court has a continuing supervisory role during the case which includes the ability to revisit issues such as disinterestedness whenever appropriate).

or from its professional ties to Schweigert and when it found adequate Stinson's disclosures.

C. The bankruptcy court did not err by not holding an evidentiary hearing or by finding that Stinson's fees were reasonable.

Coleman never requested an evidentiary hearing on the reasonableness of Stinson's fees in the manner required by Arizona Local Bankruptcy Rule 9014-2.[24] Consequently, he waived any right to such a hearing. See In re Nicholson, 435 B.R. at 636-37.

At oral argument, Coleman's counsel argued that, even though Coleman did not properly request an evidentiary hearing, the

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[24]That rule states in full:

RULE 9014-2. HEARINGS ON CONTESTED MATTERS

(a) Initial Hearing without Live Testimony. Pursuant to Bankruptcy Rule 9014(e), all hearings scheduled on contested matters will be conducted without live testimony except as otherwise ordered by the court. If, at such hearing, the court determines that there is a material factual dispute, the court will schedule a continued hearing at which live testimony will be admitted.

(b) Request for Live Testimony.

(1) Any party filing a motion, application, or objection who reasonably anticipates that its resolution will require live testimony may file an accompanying motion for an evidentiary hearing, stating:

(A) The estimated time required for receipt of all evidence, including live testimony;

(B) When the parties will be ready to present such evidence;

(C) The estimated time required to complete all formal and informal discovery;

(D) Whether a Bankruptcy Rule 7016 Scheduling Conference should be held; and,

(E) Whether any party who may participate at the evidentiary hearing is appearing pro se.

(2) The party requesting an evidentiary hearing shall accompany the motion with a form of order.

understanding in the District of Arizona is that failure to request such a hearing does not constitute a waiver. But even if Coleman did not waive the evidentiary hearing, no such hearing was necessary here because Coleman failed to establish the existence of a disputed material factual issue regarding the reasonableness of Stinson's fees.

Section 330 governs the award of fees by a bankruptcy court to estate professionals. That section states:

> (a)(1) After notice . . . and a hearing . . . the court may award to . . . a professional person employed under section 327 . . . —
>
> (A) reasonable compensation for actual, necessary services rendered by . . . professional person, or attorney . . . and
>
> (B) reimbursement for actual, necessary expenses. . . .
>
> (3) In determining the amount of reasonable compensation to be awarded to a[] . . . professional person, the court shall consider the nature, the extent, and the value of such services, taking into account all relevant factors, including — . . .
>
> (C) whether the services were necessary to the administration of, or beneficial at the time at which the service was rendered . . . .

11 U.S.C. § 330 (emphasis supplied).

Accordingly, under section 330, it is "clear and unambiguous" that "the question governing attorney compensation should be whether services were necessary or beneficial at the time at which the service was rendered." In re Roberts, Sheridan & Kotel, P.C. v. Bergen Brunswig Drug Co. (In re Mednet), 251 B.R. 103, 107 (9th Cir. BAP 2000). In practice, this means that "[t]he statute does not require that the services result in a material benefit to the estate in order for the professional to be compensated; the applicant must demonstrate only that the services were reasonably likely to benefit the estate at the time the services were rendered.” Id; see also In re Grosswiler Dairy, Inc., 257 B.R. 523, 528 (Bankr. D. Mont. 2000).

Coleman argued that the fees and expenses Stinson incurred attempting to confirm the Debtors’ first plan were unreasonable in light of the negligible recovery to creditors, and because Debtors eventually withdrew their heavily-litigated first plan of reorganization.[25] Addressing this argument at the hearing on the final fee application, the bankruptcy court explicitly found that the actions Stinson took regarding the first plan were reasonable at the time they took them. Applying the standard we articulated in In re Mednet, the bankruptcy court found that “it would be very hard to make a determination that was such an unreasonable plan, not [sic] fee should be awarded for pursuing it.” November 19, 2009 hearing transcript at 35:25-36:2.

More importantly, in concluding that an evidentiary hearing was unnecessary, the bankruptcy court relied on the undisputed fact that Stinson had voluntarily agreed to a 40% reduction of their fees. Thus, “short of saying that . . . almost 40 percent of what went on in this case shouldn't have been done . . . it doesn't really matter. We'd still be down to allowance of fees in the total amount of $3 million. . . . I don't see that there's

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[25]Those fees were about $2 million dollars. In his objection filed before the final fee hearing, Coleman not only complained about the first plan but also argued that Stinson incurred an unreasonable amount of fees fighting creditors’ moves to lift the automatic stay protecting Medford and contesting the fee award to the bankruptcy examiner.

any really fact dispute here that necessitates an evidentiary hearing." November 19, 2009 hearing transcript at 36:25-37:6. In other words, Stinson's voluntary write-down of its own fees by $2 million effectively removed any disputed material question of fact regarding the reasonableness of its fees.

Simply put, Coleman has not pointed us to any error of law or any clearly erroneous finding of fact concerning the court's rulings that Stinson's fees were reasonable and that no evidentiary hearing was necessary. Nor is any such error evident from our review of the record. At most, Coleman has shown that, after a vertiginous downturn in the economy and a severe real estate crash in the American Southwest, Stinson's restructuring efforts - expensively opposed at every step by Coleman himself - resulted in less recovery to the unsecured creditors than the total bill for Stinson's services.

Accordingly, we hold that the bankruptcy court did not err by not holding an evidentiary hearing or by finding that Stinson's fees were reasonable.

CONCLUSION

For all of the reasons set forth above, we AFFIRM the bankruptcy court's award of $3 million in fees and expenses to Stinson.