U.S. BANKRUPTCY COURT
District of South Carolina

Case Number: **09-03719-hb**

ORDER ON APPLICATION FOR FINAL COMPENSATION

The relief set forth on the following pages, for a total of 20 pages including this page, is hereby ORDERED.

FILED BY THE COURT
05/10/2011

Entered: 05/10/2011

US Bankruptcy Judge
District of South Carolina

UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF SOUTH CAROLINA

IN RE:	C/A No. 09-03719-HB
	Chapter 7
Outdoor RV and Marine, LLC, a Limited Liability Co,	**ORDER**
Debtor(s).	

THIS MATTER came before the Court for hearing on March 31, 2011, pursuant to the Application for Final Compensation ("Application") (Doc. No. 285) for Levy Law Firm, LLC ("Levy"), Attorneys for the Debtor Outdoor RV and Marine, LLC ("Debtor"), for the period of May 15, 2009 through July 27, 2009. The Application requests fees of $60,781.50 and costs and expenses of $2,324.73. An Objection to the Application ("Objection") (Doc. No 289) was filed by creditor Thomas R. Mims. The Objection acknowledges that, after the filing of the Application, Levy reached an agreement with the Office of the United States Trustee ("UST") to limit fees and costs to $39,234.50, which is equal to the remaining amount deposited by the Debtor with Levy before the filing of this case, now held in his trust account. Mims objected to the Application and to the compromised amount, stating that the fees are excessive. In addition, Mims asserts that any fees approved should not be paid from the funds on deposit, but rather those fees should be allowed only as a Chapter 11 administrative expense, with any funds deposited returned to the Chapter 7 Trustee for disbursement in accordance with the provisions of the Bankruptcy Code.

The Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2)(A)

and (K). Venue of this proceeding is proper in this district pursuant to 28 U.S.C. §§ 1408 and 1409.

Facts

Debtor filed its voluntary petition for relief under Chapter 11 of the Bankruptcy Code on May 15, 2009. The Debtor's petition and accompanying public filings received by the Court to initiate the case included the following relevant documents: (1) a *Statement Regarding Authority to Sign and File Petition* ("*Statement to Sign and File Petition*"), signed by John Kent Lester as Manager and Sole Member of Outdoor RV and Marine, LLC on May 15, 2009, evidencing that organization's authority to file the bankruptcy petition and to employ Levy as counsel; and in the same docket event the Debtor filed (2) a *Statement Pursuant to Rule 2016(B)* ("*2016(b) Statement*") which indicates that Levy received the amount of $50,000.00 from the Debtor and agreed to provide legal services in connection with this case at the rate of $375.00 per hour (as approved by the Court). In addition, Debtor filed an *Application of Debtor-In-Possession for Authorization to Employ Bankruptcy Counsel* ("*Application to Employ*") (Doc. No. 12), signed by Lester on May 22, 2009, for Debtor, requesting the employment of Levy for the Chapter 11 case. The *Application to Employ* again recited the hourly rates of professionals, and stated that Levy "was paid by Outdoor RV and Marine, LLC an initial retainer for pre-petition and post-petition costs and services for the Debtor in the amount of $50,000.00." *Id.* at 3. This information was repeated in Levy's Affidavit in support of that employment and after due notice the employment of Levy was approved by Order entered on June 9, 2009.[1] (Doc. No. 25). The Debtor filed additional schedules and

[1] The terms of the Order merely approved the employment of Levy and stated that "compensation shall be set by the Court according to 11 U.S.C. § 330(a), and therefore, may be different from the terms of

statements on June 12, 2009. (Doc. No. 36). The *Statement of Financial Affairs*, signed by Benjamin Keith Simpson, Debtor's CFO, included a disclosure of payment of $50,000.00 to Levy on May 11, 2009, in response to question number 9 which asks the Debtor to "List all payments made or property transferred by or on behalf of the debtor to any person, including attorneys, for consultation concerning debt consolidation, relief under the bankruptcy law or preparation of a petition in bankruptcy within one year immediately preceding the commencement of this case." (Doc. No. 36-1 at 4).

Debtor and Levy also filed Applications to Employ Mary P. Ouzts, CPA, as accountant for the Debtor and Harry A. Swagart, III, PC, as special counsel for the Debtor. Employment of these professionals was approved on June 9, 2009. (Doc. Nos. 26, 27).

On June 15, 2009, KeyBank National Association filed a Motion to Convert Chapter 11 Case to Chapter 7. (Doc. No. 38). The case was ultimately converted to Chapter 7 on July 27, 2009. (Doc. No. 85). W. Ryan Hovis was appointed as Chapter 7 Trustee.

Before the May 15, 2009, bankruptcy filing and until the case was converted to Chapter 7, Debtor was in the business of selling recreational vehicles and boats at its dealerships located in South Carolina as well as servicing vehicles and selling parts. *See* Doc. No. 1 at 1; *see also* Doc. No. 47 at 6. Mims' Objection and the evidence indicate that prior to the bankruptcy filing, the Debtor obtained a 2005 Fleetwood motor home ("Motor Home") on consignment from its prior owners, Robert W. and Ann T. Taylor. Subsequently, on or about May 21, 2009 (after the bankruptcy was filed on May 15th),

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compensation discussed by the applicant and the attorney." (Doc. No. 25). Inclusion of this provision is standard practice in this District.

Debtor reached an agreement with the lien holder on the Motor Home, GEMB Lending, Inc., to satisfy the lien by payment of $100,000.00. On May 20, 2009, Mims purchased that Motor Home by trading-in a 2008 Ford F-250 pickup with clear title, and a 2007 Cardinal fifth wheel camper ("Camper") with a $42,703.00 lien held by Bank of America, per the Bill of Sale. In addition, Mims paid the Debtor $108,823.00, which included $42,703.00 to pay off the lien to Bank of America and other administrative fees. This amount was paid with a $67,823.00 loan proceeds check from BB & T Bank of Sumter and a $41,000.00 Visa credit card payment.

Apparently, Debtor never applied the $42,703.00 from the proceeds of the sale of the Motor Home to pay off the Bank of America lien on the Camper Mims traded-in. Further, the Debtor never advised Mims of the GEMB lien on the Motor Home and failed to pay off this lien prior to, or after delivering the Motor Home to Mims. As a result, Mims was unable to license or obtain title to the Motor Home, had to make payments to BB & T to protect his interest in the Motor Home, and had to make payments to Bank of America for the lien on the Camper to protect his credit.

Mims called the Court's attention to the Rule 2004 Examination of Lester conducted on March 31, 2010. Lester testified that he placed the funds received by Mims into his business' "regular checking account" and used them to allow the business to continue to operate, in spite of a cash collateral order in place in the case. He also testified that he could not account for the whereabouts of the truck Mims traded-in. Lester, apparently, sold the Camper and applied the sales proceeds to the operation of the business rather than payment of the Bank of America lien. Mims has filed a request for an administrative expense in this case, and with the consent of the Chapter 7 Trustee,

holds a Chapter 11 administrative expense in an amount to be determined at the appropriate time.[2]

In his Objection, Mims clarifies that he does not allege that Levy was in any way directly or indirectly knowingly involved in Debtor's improper conduct. Rather, Mims asserts that there was no benefit gained from the Chapter 11 filing, in which Levy served as counsel. In addition, Mims claims that, as attorney for the Debtor, Levy had the obligation to monitor the operation of the business and to assure that orders of the Court and proper business practices were being followed to prevent the harm Mims suffered during the time the Debtor was operating under Chapter 11. In support of his Objection, Mims also contends that there were inaccuracies in the schedules filed by the Debtor. Lester asserted in his 2004 exam that he never read the petition and schedules and that they were prepared by Levy.

Levy testified at the hearing. He stated that this case was presented to him by Lester as an emergency filing and that he counseled the Debtor's officers and advised them of their obligations. He testified that he recognized title problems and recommended hiring an additional attorney (Swagart) and an accountant to assist with any matters involving titles and alleged misappropriations of funds. Levy testified that he, with the assistance of other professionals, put controls in place to attempt to ensure that the Debtor's business operated in an appropriate manner. He testified that Simpson

[2] Pursuant to a Consent Order entered by the Chapter 7 Trustee and Mims on July 21, 2010, determining the amount of Mims' administrative claim :

> will require time for [Mims] to seek other sources of compensation, such as the existence of performance bonds, the possible recovery of some other physical assets, and, perhaps, other yet unknown sources. In addition, because the recovery under these motions is to be determined by the benefits bestowed upon the estate, not the losses incurred by [Mims], the parties will need to explore the process of determining the actual benefits to the estate.

(Doc. No. 278 at 3).

(Debtor's CFO) was involved in the day to day operations and controls to assist Lester and the Debtor, and that Simpson was later hired and approved to assist the Chapter 7 Trustee in this matter.

Levy pointed out that his reduction in fees negotiated with the UST represents a 38% reduction in fees requested thus far, and that he continues to voluntarily cooperate with the Chapter 7 Trustee, likely without compensation. He referred the Court to his detailed hourly time records and summaries filed in support of his Application as evidence of his efforts and to support his compensation request.

Discussion and Conclusions of Law

Mims presents two challenges to the Application. First, Mims argues that Levy has failed to establish that the compensation is warranted pursuant to 11 U.S.C. § 330.[3] Specifically, Mims argues that Levy has not shown that its services were beneficial at the time they were rendered, as required by § 330(a)(3)(C), and questions the rates charged by Levy's paralegals under § 330(a)(3)(F). Secondly, Mims contends that payment of any approved fees from funds held by Levy should not be allowed. Rather, those funds should be returned to the Chapter 7 Trustee and Levy's fees should at best be a Chapter 11 administrative expense pursuant to § 726(b), with Levy sharing equally with similarly situated administrative claimants.

Reasonableness of Fees

This Court has the duty and authority to review the reasonableness of attorney's fees sought and obtained by the Debtor's attorney. *See In re Henderson,* No. 05-14925-JW, slip op. at 3 (Bankr. D.S.C. Sept. 5, 2006); *see also In re Larson*, 346 B.R. 693, 699 (Bankr. E.D. Va. 2006) (discussing duty to review supplemental fee applications in

[3] Further reference to the Bankruptcy Code, 11 U.S.C. § 101 *et. seq.*, will be by section number only.

Chapter 13 cases). The Court is guided by the Code and law adopted by the Fourth Circuit in determining whether counsel is entitled to the requested fees. The criteria for awarding attorney's fees is set forth in § 330:

> 3) In determining the amount of reasonable compensation to be awarded to an examiner, trustee under chapter 11, or 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 toward the completion of, a case under this title . . .
>
> . . . .
>
> (F) whether the compensation is reasonable based on the customary compensation charged by comparably skilled practitioners in cases other than cases under this title.

11 U.S.C. § 330(a)(3). In addition to the factors set forth by the Code, the Fourth Circuit utilizes the lodestar method to evaluate the reasonableness of attorney's fees. This "method entails the application of various factors to calculate a reasonable rate and reasonable number of hours in order to produce a lodestar figure." *In re J.T. Custom Coatings, Inc.*, No. 04-01671-W, slip op. at 3 (Bankr. D.S.C. Dec. 19, 2005). The factors to be considered by the Court are:

> (1) the time and labor expended;
> (2) the novelty and difficulty of the questions raised;
> (3) the skill required to properly perform the legal services rendered;
> (4) the attorney's opportunity costs in pressing the instant litigation;
> (5) the customary fee for like work;
> (6) the attorney's expectations at the outset of the litigation;
> (7) the time limitations imposed by the client or circumstances;
> (8) the amount in controversy and the results obtained;
> (9) the experience, reputation and ability of the attorney;
> (10) the undesirability of the case within the legal community in which the suit arose;
> (11) the nature and length of the professional relationship between attorney and client; and
> (12) attorneys' fees awards in similar cases.

Harman v. Levin, 772 F.2d, 1150, 1152 n.1 (4th Cir. 1985) (citing *Barber v. Kimbrell's Inc.*, 577 F.2d 216, 226 n.28 (4th Cir.), *cert denied*, 439 U.S. 934, 99 S.Ct. 329 (1978)).

Mims objects to Levy's fees under § 330(a)(3)(C), claiming that Levy's services were not beneficial because Mims was harmed by the Debtor during the Chapter 11 case. When questioned by the Court at the hearing, counsel argued that in this matter, the term "beneficial" would mean that Levy should have established sufficient safeguards or structure to prevent the harm Mims suffered and as a result of his failure to prevent the harm, his services were not beneficial. In addition, Mims asserts that the fees charged by Levy's paralegals are unreasonable under § 330(a)(3)(F).

The language of § 330(a)(3)(C), "unambiguously requires consideration of whether, at the time at which the services were rendered, a reasonable attorney would have believed that they would benefit the estate, rather than a subsequent consideration of the practical effects actually achieved by the attorney's services." *In re Cloverleaf Enter., Inc.*, 436 B.R. 339, 342-43 (Bankr. D. Md. 2010).[4] The debtor's attorney is not a guarantor that the work performed will actually be beneficial. As long as the services are reasonably likely to benefit the debtor, the attorney is entitled to compensation. *In re United Refuse LLC*, No. 04-11503-RGM, 2007 WL 1695337, slip op. at *45 (Bankr. E.D. Va. June 7, 2007). Therefore, analysis under § 330(a)(3)(C) to determine "whether a service was beneficial is prospective not retrospective." *In re Marshall*, No. 02-80496-

[4] Although a construction of § 330(a)(3)(C) has not been adopted by the Fourth Circuit, this court discussed the various interpretations utilized by other circuits and applied the Ninth Circuit Bankruptcy Appellate Panel's approach in *In re Mednet, MPC*, 251 B.R. 103 (B.A.P. 9th Cir. 2000). *See In re Cloverleaf Enter., Inc.*, 436 B.R. 339, 341-43 (Bankr. D. Md. 2010). The *Mednet* court held that "the applicant must demonstrate only that the services were 'reasonably likely' to benefit the estate at the time the services were rendered." 251 B.R. at 108.

RGM, 2010 WL 3959612, slip op. at *38 (Bankr. E.D. Va. Oct. 11, 2010) (citing 11 U.S.C. § 330(a)(3)(C)).

The only evidence before the Court indicates that prior to filing the chapter 11 petition, Levy explained to Lester and Simpson the Chapter 11 process as well as the Debtor-In-Possession's responsibilities and fiduciary obligations. Upon filing the petition, Levy recommended the retention of services from Ouzts, a CPA, for advice on issues relating to allegations of misappropriations of funds. He also recommended retaining Swagart as special counsel, who had previously been involved in litigation and disputes regarding titles to the recreational vehicles. At the time these services were rendered, it was reasonable for Levy to believe that they would benefit the estate because there was no indication that Lester would not follow the advice and instructions given by Levy or other professionals retained by the Debtor. There is no indication that Levy caused the harm or took any action or failed to take any action that directly resulted in Mims' harm. In addition, Levy's actions were reasonably likely to benefit the Debtor and the estate. To find otherwise would be to retrospectively determine whether Levy's services were beneficial to the estate, which is contrary to the statute's interpretation. *See Marshall*, 2010 WL 3959612, slip op. at *38. Therefore, any objection to Levy's fees under § 330(a)(3)(C) is overruled.

Regarding the rates charged by Levy's paralegals, the Application indicates that Levy charged for 70.6 hours of paralegal work at a rate of $100.00 - $120.00 per hour for a total of $8,094.00.[5] (Doc. No. 285 at 7). Levy has already agreed to reduce his fee and expense request by approximately 38% or $23,871.73. Therefore, addressing this

[5] The Application states that paralegal Robin C. Osborne worked a total of 51.7 hours and charged $120.00 per hour and paralegal Brien P. Levy worked a total of 18.9 hours and charged $100.00 per hour.

challenge is not necessary, as the fees and expenses have already been reduced by more than the total of all paralegal charges. Any objection to the rates charged for paralegal services is, therefore, overruled.

Source of Payment of Approved Fees and Expenses

Pursuant to § 726(b), distribution of property of the estate shall be conducted according to the following:

> Payment on claims of a kind specified in paragraph . . . (2) . . . of section 507(a) of this title . . . shall be made pro rata among claims of the kind specified in each such particular paragraph, except that in a case that has been converted to this chapter under section 1112, 1208, or 1307 of this title, a claim allowed under section 503(b) of this title incurred under this chapter after such conversion has priority over a claim allowed under section 503(b) of this title incurred under any other chapter of this title or under this chapter before such conversion . . .

11 U.S.C. § 726(b). Attorney's fees are classified as administrative expenses under § 503(b)(2) for "compensation and reimbursement awarded under section 330(a) of this title." 11 U.S.C. § 503(b)(2). Pursuant to § 507, this type of administrative expense is given second priority among unsecured claims. 11 U.S.C. § 507(a)(2). According to § 726(b), attorney's fees are to be paid pro rata with other similarly situated claims enumerated in § 507(a). Section 726(b) further states that if a reorganization case has been converted to Chapter 7, the Chapter 7 administrative expenses under § 503(b), such as Mims' claim, have priority over the § 503(b) administrative expenses incurred during the reorganization case.

Levy asserts that his claim for attorney's fees is secured by the funds he obtained from the Debtor pre-petition; therefore, his claim is not subject to the priorities of § 726(b). Mims, however, asks the Court to classify Levy's claim as an unsecured Chapter 11 administrative claim that, pursuant to § 726(b), is subordinate to the Chapter 7

administrative claims because Levy has not established that he has a lien on the Debtor's fund held in his trust account.

"In general, Chapter 11 retainers are not flat fees for all services to be performed in a specific case. Instead, Chapter 11 retainers are usually held by an attorney as security for payment of fees for professional services to be rendered when requested by a client." *In re Burnside Steel Foundary Co.*, 90 B.R. 942, 945 (Bankr. N.D. Ill. 1988).

> A "security retainer" is defined as one held by attorneys to "secure payment of fees for future services that the attorneys are expected to render." The funds do not constitute a present payment for future services but, rather, remain the property of the estate until the attorney applies charges for services rendered against the retainer. The unearned portion of the retainer must be returned by the attorneys. Such a retainer constitutes a possessory security interest in the funds under the Uniform Commercial Code.

3 *Collier on Bankruptcy* ¶ 328.02[1][c] (15th ed. rev. 2005).

Attorneys obtain security retainers because, "if the case is converted from Chapter 11 to Chapter 7, the security interest in the retainer allows the lawyer to avoid the subordination provisions of Section 726(b) to the extent that services were provided and approved by the bankruptcy court." *In re Zukoski*, 237 B.R. 194, 198 (Bankr. M.D. Fla. 1998) (citing *Burnside Steel*, 90 B.R. at 944). A security retainer is not subject to § 726(b) because:

> The debtor's attorney who receives a prepetition retainer to insure payment of fees to be earned in the Chapter 11 case . . . becomes a secured creditor, secured by a possessory security interest in cash . . . The reason that the retainer succeeds in avoiding the subordination requirements of § 726(b) is that § 726 only affects distribution priorities among holders of unsecured claims, and an attorney with a retainer is, to the extent of the retainer, the holder of a secured claim.

Burnside Steel, 90 B.R. at 944 (citations omitted); *see also In re Dick Cepek, Inc.*, 339 B.R. 730, 737 (B.A.P. 9th Cir. 2006) (stating that "before section 726(b) is even

implicated, all amounts secured by a lien created by the security retainer must be paid"); *In re Printing Dimensions, Inc.*, 153 B.R. 715, 719 (Bankr. D. Md. 1993) ("Counsel, however will not be required to share a prepetition retainer pro rata with other administrative claimants where either the retainer is treated as security or the retainer is held in trust.").

"The prevailing view among bankruptcy courts is that security retainers are allowed and recognized in the context of bankruptcy proceedings." *In re Advanced Imaging Technologies, Inc.*, 306 B.R. 677, 680 (Bankr. W.D. Wash. 2003) (citing *In re Printcrafters, Inc.*, 233 B.R. 113, 118 (D. Colo. 1999); *Zukoski*, 237 B.R. at 198; *In re Insilco Technologies, Inc., et al.*, 291 B.R. 628, 636 (Bankr. D. Del. 2003)). In the instant case, pursuant to the Application to Employ, Levy held a retainer of funds by agreement with the Debtor to cover pre- and post-petition costs and services. (Doc. No. 12 at 3). Therefore, Levy holds a security retainer as defined by *Collier on Bankruptcy*. *See supra* p. 11 (defining "security retainer"); *see also Advanced Imaging Technologies*, 306 B.R. at 680 (finding that the attorney's employment agreement with the debtor to hold the retainer to secure future fees was sufficient to establish attorney's security retainer as defined in *Collier*).

Although *Collier* recognizes this security retainer, state law determines the validity and extent of any lien in bankruptcy. *Advanced Imaging Technologies*, 306 B.R. at 680; *see also Printcrafters Inc.*, 233 B.R. at 117 ("Congress has generally left the determination of property rights in the assets of a bankrupt's estate to state law. Property interests are created and defined by state law. Accordingly, state law determines the

validity and extent of an attorney's lien in bankruptcy." (internal quotation marks and citations omitted)).

Many courts have held that an attorney's security interest in the retainer arises from perfection by possession of the retainer under Article 9 of the Uniform Commercial Code ("UCC"). *See e.g. In re On-Line Serv.*, 324 B.R. 342, 346-47 (B.A.P. 8th Cir. 2005) (holding that the debtor's attorney had a lien over a portion of the retainer used for pre-petition services that had not been drawn on because, "[a] security retainer involves the attorney holding the client's money as a pledge—a possessory security interest—and the Uniform Commercial Code expressly allows for a possessory security interest in money." (citations omitted)). "The law of secured transactions in South Carolina is governed by the Uniform Commercial Code—Secured Transactions as adopted in § 36-1-101 *et. seq.*" *In re Lewis*, 363 B.R. 477, 482 (Bankr. D.S.C. 2007). South Carolina's perfection by possession statute states that, "a secured party may perfect a security interest in . . . money . . . by taking possession of the collateral." S.C. CODE ANN. § 36-9-313(a) (2010).

However, the Rules of this Court require retainers held by professionals in a Chapter 11 case to "be maintained in a trust account and not be drawn against post-petition unless the Court orders otherwise," SC LBR 2016-1. In addition, the South Carolina Rules of Professional Conduct provide that "[a] lawyer shall deposit into a client trust account unearned legal fees and expenses that have been paid in advance, to be withdrawn by the lawyer only as fees are earned or expenses incurred." Rule 407, SCACR: Rule 1.15(c).

"Possession" is not defined by the UCC, nor is there any South Carolina case law lending any guidance as to the courts' interpretation of "possession." Therefore, the

Court must look to law outside South Carolina to determine whether holding a retainer in a *trust account* constitutes "possession" of that amount. "Possession" is defined as:

> 1. The fact of having or holding property in one's power; the exercise of dominion over property . . . 2. The right under which one may exercise control over something to the exclusion of all others; the continuing exercise of a claim to the exclusive use of a material object."

BLACK'S LAW DICTIONARY (9th ed. 2009). "Possession" has been interpreted as being "intended, and must be measured in part by its ability, to provide notice to other parties that the property in question is encumbered; thus the requisite possession must be actual and exclusive, or unequivocal, absolute, and notorious." 79 C.J.S. *Secured Transactions* § 65 (2011) (footnotes and citations omitted).

Courts with perfection by possession statutes similar to South Carolina's have held that, in bankruptcy, when an attorney receives a pre-petition retainer for services to be rendered during the Chapter 11 case, the attorney has a possessory security interest perfected by the attorney's possession of the retainer in his trust account. *See e.g.*, *Burnside*, 90 B.R. at 944 (holding that, pursuant to the UCC and Illinois' applicable perfection statute, *see* U.C.C. § 9-305 (1978); ch. 26 ILL. COMP. STAT. ANN. ¶ 9-305 (1987), "[t]he debtor's attorney who receives a prepetition retainer to insure payment of fees to be earned in the Chapter 11 case . . . becomes a secured creditor, secured by a possessory security interest in cash"). In *Advanced Imaging Technologies*, 306 B.R. 677, the court found that under Washington's Uniform Commercial Code, the Chapter 11 debtor's attorney held a perfected security interest in the retainer funds. *Id.* at 681. The Chapter 11 debtor and attorney entered a pre-petition engagement agreement that gave the attorney a $75,000.00 retainer. The agreement stated that "the retainer was 'to secure payment of fees and costs' incurred by the firm as bankruptcy counsel to the Debtor." *Id.*

at 679. In holding that the attorney held a perfected security interest over the retainer, the court first found that the conditions of attachment[6] were satisfied by the following: 1) the attorney gave value by agreeing to be counsel for the debtor; 2) the debtor owned the funds at the time the retainer was paid to the attorney and all times thereafter; 3) and although only one of the following conditions must be met, the court found that the engagement agreement described the retainer and the attorney *took possession* of the retainer funds (by placing them in a trust account) prior to bankruptcy. *See id.* at 681. Therefore, under Washington's perfection by possession statute[7], the attorney's "security interest in the retainer funds is perfected by possession." *Id.*

In the instant case, the Court finds that Levy's holding of the retainer in his trust account constitutes "possession" under § 36-9-313(a) because, although Debtor owned the funds and the bankruptcy estate held an interest in those funds, Levy had and has a right to exercise control over those funds to the exclusion of all others. *See* BLACK'S LAW DICTIONARY (9th ed. 2009). That is, only those authorized to make withdrawals and transfers of the money in his trust account could exercise physical control over those funds. Others may have an "interest" in those funds, but Levy's possession of the funds

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[6] The requirements for attachment under Washington's UCC are identical to those required under South Carolina's UCC. The relevant statute provides:

> Except as otherwise provided in subsections (c) through (i), a security interest is enforceable against the debtor and third parties with respect to the collateral only if :
> (1) value has been given;
> (2) the debtor has rights in the collateral . . . and
> (3) one of the following conditions is met:
> (A) the debtor has authenticated a security agreement that provides a description of the collateral . . . ; or
> (B) the collateral is not a certificated security and is in the possession of the secured party under RCW 62A.9A-313 [in Washington; Section 36-9-313 in South Carolina] pursuant to the debtor's security agreement . . .

WASH. REV. CODE ANN. § 62A.9A-203(b) (West 2005); S.C. CODE ANN. § 36-9-203(b) (2010).

[7] The perfection by possession statutes for Washington and South Carolina contain identical language: "a secured party may perfect a security interest in negotiable documents, goods, instruments, money, or tangible chattel paper by taking possession of the collateral." WASH. REV. CODE ANN. § 62A.9A-313(a); S.C. CODE ANN. § 36-9-313(a).

in his trust account with the understanding that the funds are for the purpose of paying his legal fees gives him initial control that is exclusive of and superior to the interests of all others. In addition, the holding of the funds in a trust account, along with all the required disclosures in bankruptcy disclosing and declaring the attorney's holding of the retainer to secure payment of his fees, provide notice to other parties that the funds are, or may be, owed to the attorney through the course of his representation. *See* 79 C.J.S. *Secured Transactions* § 65. Furthermore, placing the funds in a trust account constitutes possession that is "actual and exclusive, or unequivocal, absolute, and notorious," *id.*, because no other party is able to access those funds and the bankruptcy filings make clear where the funds are located and that Levy is making a claim on those funds. The Court also finds its decision to be aligned with a majority of those courts addressing this issue. *See Zukoski*, 237 B.R. at 198 ("The most persuasive view is that a debtor's attorney, by taking a security retainer, holds a possessory perfected security interest in a prepetition retainer to the extent of services provided and approved by the court." (citing *In re Dees Logging, Inc.*, 158 B.R. 302, 307 (Bankr. S.D. Ga. 1993))).

It would be an anomaly to require debtors' attorneys to place retainers in their trust accounts and to later hold that, as a result of this requirement, they do not adequately *possess* those funds placed there for the sole purpose of securing payment of fees and costs.[8] A finding of this sort would also prevent other attorneys from agreeing to represent debtors in Chapter 11 cases. *See Dick Cepek*, 339 B.R. at 738 (finding the attorney to have a security interest, preventing subordination under § 726(b), because to hold otherwise "would undermine the purpose of retainers and chill the willingness of

[8] In bankruptcy this may only be done post-petition upon the approval of the Court. 11. U.S.C § 330.

many professionals to undertake representation of chapter 11 debtors." (internal quotation marks and citations omitted)).

The majority of courts agree that a lien on the retainer prevents the attorney's fees from being subordinated by § 726(b). *See On-Line Serv.*, 324 B.R. at 347 (determining that "by taking a retainer—even though it is considered a security retainer—a professional becomes a secured creditor, and hence has a claim on the retained funds prior to any other administrative claimant." (internal quotation marks and citations omitted)); *see also In re Appalachian Star Ventures*, 341 B.R. 222, 228 (Bankr. E.D. Tenn. 2006) (holding that because the attorney with a lien on the retainer is a secured creditor, he "is not 'equally situated' with other administrative claimants that advance services or credit to the debtor on an unsecured basis. As such, § 726(b) is inapplicable . . ."); *Printcrafters*, 233 B.R. at 117-20 (finding that the debtor's attorney, under Colorado law, held a "possessory lien" on the "security retainer" and because the attorney complied with the fee application process, the attorney's fees were not required to be shared with other administrative claims); *Burnside Steel*, 90 B.R. at 944 (stating that a retainer paid to a debtor's attorney in a Chapter 11 case that is subsequently converted to Chapter 7 is not subject to § 726(b) because the attorney becomes "a secured creditor, secured by a possessory security interest in cash").

As Mims argued, it is true that in this case there was no separate document labeled "retainer agreement" executed between Debtor and Levy setting forth all of the terms of employment and compensation. The Court's decision would have come easier in this matter if Levy had presented such a document. However, after considering the documents filed on the public docket in this case, the Court finds that the retainer

agreement and terms of employment are adequately documented and disclosed. The Rules of Professional Conduct require:

> The scope of the representation and the basis or rate of the fee and expenses for which the client will be responsible [to be] communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation . . . Any changes in the basis or rate of the fee or expenses shall be communicated to the client, preferably in writing.

Rule 407, SCACR: Rule 1.15(b). In addition to the requirements set forth by the Rules of Professional Conduct, in bankruptcy, "[p]rudence, ethical considerations and general proof requirements all suggest that an arrangement whereby a professional is granted a security interest in a debtor's funds be adequately documented." *Dick Cepek*, 339 B.R. at 741; *see also*, *Advanced Imaging Technologies*, 306 B.R. at 681 n.3 (finding that, pursuant to Local Rule 2014-1, the engagement agreement adequately described the retainer).

The Court finds that the contents of the *Statement to Sign and File Petition* signed by Lester pre-petition (Doc. No. 1 at 4), which was filed together with the *2016(b) Statement*, disclosing and evidencing that Debtor paid Levy $50,000.00 as a retainer pre-petition and setting forth his hourly rate of compensation, are sufficient to document the arrangement and security retainer agreement between the parties. *Id.* at 5. In addition, the *Application to Employ*, signed by Lester on May 22, 2009, for Debtor, further evidences the pre-petition arrangement, clearly disclosing the terms of compensation and security retainer paid.[9] *See* Doc. No. 12. Levy again publically disclosed this information in his Affidavit in support of that employment, *see* Doc. No. 25, and Debtor's schedules stated that there was an agreement for a security retainer in the *Statement of Financial Affairs*,

[9] The *Application to Employ* states that Levy "was paid by Outdoor RV and Marine, LLC an initial retainer for pre-petition and post-petition costs and services for the Debtor in the amount of $50,000.00." (Doc. No. 12 at 3).

signed by Simpson, Debtor's CFO. (Doc. No. 36-1 at 4). Therefore, there is sufficient documentation and evidence of the agreement in the miscellaneous public filings, and the terms of the contract that was formed between the Debtor and Levy are clear and have been disclosed in this case repeatedly.

Because Levy possesses a retainer that is equal to the fees and costs approved herein, and as there is a pre-petition agreement that the retainer shall be used for payment of his attorney's fees and expenses, his attorney's fees are not subject to subordination or pro rata distribution under § 726(b) and, therefore, he may pay the approved amounts from the retainer.

IT IS THEREFORE, ORDERED:

1. That Levy's request for $39,234.50 in attorney's fees and expenses is approved and any objections pursuant to § 330(a)(3)(C) or (F) are overruled; and
2. That as a result of the retainer and § 36-9-313(a), Levy holds a perfected possessory security interest in the funds held in his trust account; therefore, his fees and expenses may be paid from that account and are not subject to subordination under § 726(b).