

UNITED STATES BANKRUPTCY COURT

DISTRICT OF SOUTH CAROLINA

In re:

PassAm, Inc.,

Debtor.

Case No. 99-03475-W
Chapter 7

JUDGMENT

FILED
2000 APR 19 PM 2:28
DISTRICT OF SOUTH CAROLINA

ENTERED

APR 20 2000

S. R. P.

Based upon the Findings of Fact and Conclusions of Law as recited in the attached Order, the Court approves the employment of Nelson Mullins Riley and Scarborough, LLP as special counsel for the Chapter 7 Trustee pursuant to 11 U.S.C. §327(c).


UNITED STATES BANKRUPTCY JUDGE

Columbia, South Carolina
April 19, 2000.

CERTIFICATE OF MAILING

The undersigned deputy clerk of the United States Bankruptcy Court for the District of South Carolina hereby certifies that a copy of the document on which this stamp appears was mailed on the date listed below to:

✓ **APR 20 2000**

✓ (RFA) ✓ (POM)
DEBTOR, DEBTOR'S ATTORNEY, TRUSTEE

SHEREE R. PHIPPS

Deputy Clerk

✓ (WST)

✓ (Cawthon)

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Chapter 7

ORDER

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APR 20 2000

S. R. P.

THIS MATTER comes before the Court upon the Application To Employ an Attorney as Special Counsel (the "Application") filed on January 6, 2000 by the Chapter 7 Trustee, Ralph C. McCullough, II (the "Trustee"). The Application requested the authorization to employ the law firm of Nelson Mullins Riley and Scarborough, LLP ("NMRS") as special counsel for the Trustee. On January 20, 2000, the Court entered an Order stating that the Application would be considered after notice of the Application was provided to creditors and upon further hearing on any objections or, in the alternative, upon submission by the Trustee of an order and certificate of no objection. On February 10, 2000, Steven Bleistein ("Bleistein") and William H. Pike, II ("Pike") jointly filed an Objection to Application to Employ Nelson Mullins Riley and Scarborough, LLP as Special Counsel to the Trustee (the "Objection"). The United States Trustee (the "UST") supported the Trustee's Application. After reviewing the pleadings in this matter and hearing the arguments of counsel, the Court makes the following Findings of Fact and Conclusions of Law pursuant to Rule 52 of the Federal Rules of Civil Procedure, made applicable by Rule 7052 of the Federal Rules of Bankruptcy Procedure.¹

¹ The Court notes that to the extent any of the following Findings of Fact constitute Conclusions of Law, they are adopted as such, and to the extent any Conclusions of Law constitute Findings of Fact, they are so adopted.

FINDINGS OF FACT

1. PassAm, Inc. ("Debtor") filed a voluntary petition for Chapter 7 relief on April 21, 1999. The petition was signed by Pike in the capacity of Debtor's President.
2. Debtor's Schedule F lists Bleistein as an unsecured creditor in the amount of \$3,852.32. The Schedules do not list Pike as a creditor.
3. As of the date of the hearing on the Application, neither Pike nor Bleistein had filed a Proof of Claim; and, pursuant to Fed. R. Bankr. P. 3002(c), the bar date for timely filing non-governmental claims had expired.
4. Pike and Bleistein each own 48.5% of Passport American Holdings, Inc., Debtor's parent corporation.
5. Debtor's Statement of Affairs shows that Bleistein and Pike both kept or supervised the keeping of Debtors' records prior to the filing of the Chapter 7 case.
6. Debtors' Schedules list Carolina First Bank ("Carolina First") as a secured creditor in the amount of approximately \$437,000.00. Carolina First's claim against Debtor is secured by a lien on Debtor's accounts receivable and inventory. Debtor's Schedules, however, do not reveal any receivables or assets other than two automobile leases.
7. NMRS represents Carolina First in this bankruptcy case and in state court litigation currently pending against Pike and Bleistein, as guarantors of Carolina First's debt.
8. The Trustee proposes to employ NMRS to assist him in recovering assets for the bankruptcy estate. More specifically, the Trustee seeks to employ NMRS as special counsel pursuant to 11 U.S.C. §327(c)² to investigate pre-petition transfers of Debtors' property, to

² Further references to the Bankruptcy Code shall be by section number only.

review Debtor's corporate books and records, to investigate potential assets for the estate, and to possibly institute litigation.

9. Pursuant to his agreement with NMRS, the Trustee indicated that NMRS will charge an hourly fee, plus costs. NMRS, however, would not be entitled to any compensation from the estate unless its efforts in litigation produce income for the bankruptcy estate. If the litigation only benefits Carolina First, then NMRS would not receive any compensation from the bankruptcy estate; rather, Carolina First would be fully responsible for NMRS's legal fees and expenses. If, on the other hand, the litigation produces some benefit for the bankruptcy estate, NMRS may seek payment from the estate as to be determined by the Court.

10. At the hearing on the Application, the Trustee represented that his own law firm would not undertake the litigation on behalf of the bankruptcy estate due to the speculative nature of the recovery. The Trustee further represented to the Court that NMRS's knowledge of Debtor and its principals, coupled with the fact that NMRS's attorneys are practiced in the area of corporate transfers and are familiar with the legal issues involved in this case, make NMRS the best law firm to pursue the litigation on behalf of the Trustee.

CONCLUSIONS OF LAW

The Trustee seeks to employ NMRS as special counsel pursuant to § 327(c). The Application indicates that the Trustee seeks to retain NMRS to investigate pre-petition transfers of assets and business opportunities, including transfers to insiders; to locate and review books and records; to investigate potential assets for the estate; and to examine Debtor's relationship to its insiders and affiliate companies. The Trustee noticed the Application proposing to employ NMRS to all creditors and parties in interest. Only Bleistein and Pike, who are potential targets

of the Trustee's litigation, objected to the employment of NMRS as special counsel. The Trustee and UST recommend that the employment of the law firm be approved.

The first issue to be determined by the Court is whether Pike or Bleistein have standing to object to the Application. The general rule consented to among courts is that an insolvent debtor lacks standing to object to the allowance of claims against the estate or, as in this situation, to object to the proposed employment of special counsel because the debtor "is not a party in interest and thus lacks standing because he has no pecuniary interest in the distribution of his assets among his creditors." Willemain v. Kivitz (In re Willemain), 764 F.2d 1019, 1022 (4th Cir. 1985) (citing 3 J. Moore & L. King, *Collier on Bankruptcy* ¶57.17[2.1] (14th ed. 1977)). In this case, the Schedules and Statements clearly evidence the insolvency of Debtor; thus, technically neither Pike nor Bleistein, as shareholders and representatives of Debtor, have standing to object to the proposed employment of NMRS. However, Debtor's Schedule F lists Bleistein as having an unsecured claim against Debtor in the approximate amount of \$3,852.32; therefore, the Court will proceed under the view that his status of unsecured creditor in the case grants him standing to object to the Application.

The Court is next faced with the issue of whether employment of NMRS is prohibited pursuant to §327(c). Section 327(c) provides:

In a case under chapter 7, 12 or 11 of this title, a person is not disqualified for employment under this section solely because of such persons' employment by or representation of a creditor, unless there is objection by another creditor or the United States trustee, in which case the court shall disapprove such employment if there is an *actual* conflict of interest.

(Emphasis added).³ While some courts have adopted a *per se* rule prohibiting the employment of a professional who currently represents a creditor, this Court favors a case-by-case analysis. In the case presently before the Court, there clearly exists a “potential” conflict of interest between Carolina First and the estate. In fact, Carolina First is a secured creditor in the approximate amount of \$437,000.00 with a lien on Debtor’s accounts receivable and inventory. Such claim was guaranteed by Bleistein and Pike, who are also potential targets of estate claims. At some point, Carolina First may be in clear competition with the bankruptcy estate for recovery of assets. However, at this stage of the case, no assets have been identified for recovery by either the estate, Carolina First, or any other secured creditors; the explanation implied is that a fraudulent transfer might have occurred or Debtor may have failed to fully disclose its assets. At the hearing on the Application, the Trustee testified that he has reviewed Carolina First’s position and is unaware of any cause of action that the bankruptcy estate presently has against the bank. Furthermore, the Trustee has employed his own law firm to independently evaluate Carolina First’s position and to handle all matter associated with it. Finally, the Trustee indicated that the estate lacks the ability and has not otherwise located another professional willing to undertake this investigation and representation.

³ Prior to its amendment in 1984, §327(c) provided:

In a case under chapter 7 or 11 of this title, a person is not disqualified for employment under this section solely because of such persons’s employment by or representation of a creditor, but may not, while employed by the trustee, represent, in connection with the case, a creditor.

Whereas prior to the 1984 amendments, dual representation of the trustee and a creditor was prohibited, §327(c) presently does not include a *per se* rule of disqualification but rather sets forth a heightened requirement to disqualify a person from potential employment.

The Court finds that at the present time, no “actual” conflict exists which would *per se* prohibit the employment of NMRS; however a “potential” conflict is clearly present. The Court recognizes that employment of professionals with such a “potential” conflict of interest should be disfavored. As the Court in *In re BH&P, Inc.*, 103 B.R. 556 (Bankr. N.J. 1989) stated, “the terms ‘actual’ and ‘potential’ conflict merely describe different stages in the same relationship.” *Id.* at 563 (“As previously noted, an actual conflict can be defined as an active competition between two interests, in which one interest can only be served at the expense of the other. A potential conflict can then be defined as one in which the competition is presently dormant, but may become active if certain contingencies occur.”). However, the Court believes that the decision of whether to approve the employment of a person who has a “potential” as opposed to an “actual” conflict is solely within the Court’s discretion.

The Court finds that the Application to employ NMRS pursuant to §327(c) should be approved. When contemplating the services to be provided by NMRS, it is clear that the primary goals of Carolina First and the bankruptcy estate are presently harmonious and there is no active competition of interests between the two. However, the Court notes that the “potential” conflict of interest requires constant and heightened monitoring by NMRS, the Trustee, and the UST. NMRS bears the ultimate responsibility to report its actions and any potential divergence of interests between Carolina First and the bankruptcy estate. Likewise, the Trustee and the UST, who support the Application, bear a continuing responsibility to diligently inquire and review the possibility that an actual conflict may develop.

In making its decision of whether to approve the employment in this case, the Court has taken into consideration the lack of a present “actual” conflict of interest, the lack of other available counsel suited for the representation of the estate, the foreign location of Debtor’s

principal, and the common interest of all parties as well as the estate in investigating and locating assets of the estate. Keeping in mind the admonitions set forth above, the Court concludes that compelling reasons exist to authorize the employment of NMRS. It is therefore,

ORDERED that the Application to Employ an Attorney as Special Counsel filed by the Trustee is approved. In the case of the development of an actual conflict of interest during the course of NMRS's representation, and upon a report of such conflict to the Court, the Court will take such action as is appropriate to address the situation. NMRS shall keep the Court, the Trustee, and the UST informed of any change of interest in this matter during the course of representation through continuous disclosure as required by Fed. R. Bankr. P. 2014(a) and 2016(b).

AND IT IS SO ORDERED.


UNITED STATES BANKRUPTCY JUDGE

Columbia, South Carolina
April 19, 2000.

CERTIFICATE OF MAILING

The undersigned deputy clerk of the United States Bankruptcy Court for the District of South Carolina hereby certifies that a copy of the document on which this certificate appears was mailed on the date listed below to:

APR 20 2000

DEBTOR, DEBTOR'S ATTORNEY, TRUSTEE

SHEREE R. PHIBBS

Deputy Clerk

✓ (WST)

✓ (Cuthen)