Attorney Conflicts Of Interest In Bankruptcy Proceedings

Recent Bankruptcy decisions reflect confusion in the standards to be applied in resolving conflicts of interest issues. The trend of these cases appears to be toward the development of standards distinct from those which have developed under the Model Code of Professional Responsibility [hereinafter Model Code] and the court decisions interpreting it outside of the bankruptcy context. It is too early to determine if these cases reflect a general revision of conflicts of interest standards or merely a development of special principles applicable only in bankruptcy. If the former is true, then an analysis of the issue in the limited context of bankruptcy will simplify understanding of the policies behind the changes. If the trend is confined to bankruptcy cases, a different problem is presented.

The Model Code was drafted with every element of the legal profession in mind. The very concept of a professional ethic precludes the varying of ethical principles when applied to different areas of the law.[1] "The Canons of this Association govern all its members, irrespective of the nature of their practice, and the application of the Canons is not affected by statutes or regulations governing certain activities of lawyers which may prescribe less stringent standards."[2] Clearly, there is no room under the Code for a separate standard for bankruptcy. Congress intended to avoid the formulation of a separate bankruptcy bar when it reformed the Bankruptcy Act.[3]

In any given bankruptcy case there is a plethora of potential conflicts. The attorneys present may include:

—the debtor's attorney

—an attorney trustee acting as his own counsel

—the trustee's attorney

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1. "Nothing in the Code of Professional Responsibility or in the teaching of prior cases warrants such ethical relativity, for the Code, like its predecessor the Canons of Professional Ethics, 'set[s] up a high moral standard, akin to that applicable to a fiduciary. . . . Without firm judicial support, the Canons of Ethics would be only reverberating generalities'." Emle Indus., Inc. v. Patentex, 478 F.2d 562, 575 (2d Cir. 1973) (citation omitted).

2. ABA Comm. on Professional Ethics and Professional Responsibility, Op. 203 (1940). *Cf.* ABA Comm. on Professional Ethics and Grievances, Op. 152 (1936).

3. H.R. REP. No. 595, 95th Cong., 2nd Sess. 95-96 (1972). [hereinafter cited as "House Report"].

—the trustee's attorney in an ancillary proceeding
—the creditors' attorneys.

This comment will explore the various standards applied to attorney conflict of interest cases in bankruptcy cases with emphasis on the substantive provisions of the Bankruptcy Code and will compare those standards to the standards applied outside of bankruptcy.[4] Discussion of conflicts of interest of the trustee as trustee and not as an attorney are beyond the scope of this article, although the issues are frequently litigated together.[5]

Ironically, the potential for attorney conflicts of interest and the extent to which such conflicts can affect the bankruptcy process were greatly increased by the efforts of the drafters of the Bankruptcy Reform Act[6] [hereinafter BRA] to reduce the appearance of conflict created by the bankruptcy judge's dual role as judicial and administrative officer.[7] The discontinuation of routine case administration by the

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4. A complete discussion of the general conflict of interest subject is quite impossible in a short article. For illustrative cases from the various circuits *see*:

Second Circuit. Armstrong v. McAlpin, 625 F.2d 433 (2d Cir. 1979) (en banc); Board of Educ. v. Nyquist, 590 F.2d 1241 (2d Cir. 1979); Emle Indus., Inc. v. Patentex, Inc. 478 F.2d 562 (2d Cir. 1973).

Third Circuit. Kramer v. Scientific Control Corp., 534 F.2d 1085 (3d Cir.), *cert. denied*, 429 U.S. 830 (1976).

Fourth Circuit. United States v. Eggleston, 495 F.2d 1370 (4th Cir. 1974).

Fifth Circuit. Brennan's, Inc. v. Brennan's Restaurants, Inc., 590 F.2d 168 (5th Cir. 1979); Woods v. Covington County Bank, 537 F.2d 804 (5th Cir. 1976).

Sixth Circuit. General Elec. Co. v. Valeron Corp., 608 F.2d 265 (6th Cir. 1979).

Seventh Circuit. Westinghouse Elec. Corp. v. Kerr-McGee Corp., 580 F.2d 1311 (7th Cir.) *cert. denied*, 439 U.S. 95 (1978); Westinghouse Elec. v. Gulf Oil Corp., 588 F.2d 221 (7th Cir. 1978).

Eighth Circuit. Arkansas v. Dean Foods Prods. Co., 605 F.2d 380 (8th Cir. 1979); Fred Weber, Inc. v. Shell Oil Co., 566 F.2d 602 (8th Cir. 1977), *cert. denied*, 436 U.S. 905 (1978).

Ninth Circuit. Gas-a-tron v. Union Oil Co., 534 F.2d 1322 (9th Cir.), *cert. denied*, 429 U.S. 861 (1976).

Tenth Circuit. Waters v. Western Co., 436 F.2d 1072 (10th Cir. 1971).

5. *See* REA Holding Corp., 2 Bankr. 733 (Bankr. S.D.N.Y. 1980); W.T. Grant, 4 Bankr. 53 (Bankr. S.D.N.Y. 1980).

6. Title I Section 101 of the Bankruptcy Reform Act of 1978, Pub. L. 95-598, 92 Stat. 2549, enacted and codified the substantive bankruptcy law as Title 11 of the United States Code.

7. House Report, *supra* note 3, at 88-116.

bankruptcy judge shifted the responsibility for administration of the debtor's estate[8] to the creditors' committee in Chapter 11 reorganization cases and to the trustee in Chapter 7 liquidation cases. The increased importance of the role that attorneys representing these parties fulfill makes a coherent and comprehensive approach to conflicts of interest more important than ever.

In a Chapter 11 case, the creditors' committee is appointed by the court.[9] Ordinarily, the creditors' committee will consist of those persons holding the seven largest claims against the debtor. If the creditors have formed a committee prior to the order for relief, the court may continue that committee.[10] The creditors' committee represents the creditors in the formulation and negotiations of a reorganization plan[11] and is empowered to engage an attorney to represent it in investigating the acts, conduct, assets, liabilities, and financial condition of the debtor.[12] Under certain circumstances, a trustee may also be appointed in a Chapter 11 case.[13] If a trustee is not appointed, the debtor in possession[14] will have most of the rights and duties of a trustee.[15]

The primary restriction upon the committee's selection of an attorney is 11 U.S.C. § 1103(b)[16] which prohibits the creditors' committee attorney from simultaneously representing any other entity in connection with the case.[17] This section was enacted for the explicit purpose of reducing the potential for conflicts of interest.[18] Critics of this revision argue that there is no conflict of interest in the representation of one or more creditors concurrently with the creditors' committee and that disqualification works a hardship upon creditors, par-

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8. Defined at 11 U.S.C. § 541 (1982).
9. 11 U.S.C. § 1102 (1982).
10. 11 U.S.C. § 1102(b)(1) (1982).
11. 11 U.S.C. § 1103(c) (1982).
12. 11 U.S.C. § 1103 (1982).
13. 11 U.S.C. § 702(d) (1982).
14. 11 U.S.C. § 1101(1) (1982). This section defines debtor in possession as "debtor except when a person that has qualified . . . is serving as a trustee in the case." *Id.*
15. 11 U.S.C. § 1107 (1982); *see* House Report, *supra* note 3, at 404.
16. 11 U.S.C. § 1103(b) (1982): "A person employed to represent a committee . . . may not, while employed by such committee, represent any other entity in connection with the case."
17. 11 U.S.C. § 1103(a) (1982).
18. House Report, *supra* note 3, at 402.

ticularly in small communities, by reducing the availability of experienced bankruptcy attorneys.[19]

Changes in the substantive provisions of the B.R.A. make great protection against conflicts of interest necessary. The Bankruptcy Code makes all payments to a creditor during the ninety days preceding the petition subject to avoidance as a preference.[20] Even payments made in the ordinary course of business are avoidable if they are made more than forty-five days after the debt is incurred.[21] Prevailing commercial practices find even the most solvent companies paying their trade debts after forty-five days. Where an attorney represents a creditor who has received a preference the conflict which exists between the creditor and the committee is a clear violation of DR 5-105.[22]

Critics of the restriction also urge that the creditors share a common interest in maximizing the dividend payable from the estate. While essentially correct, this argument fails to take into account the potential conflict among the creditors concerning how to achieve their common goal. Creditors who expect to receive a greater return and perhaps future business from a going concern, will much prefer reorganization. Other creditors will be unwilling to speculate on a dividend payable over time and will seek a liquidation dividend. An attorney concurrently representing an individual creditor and the creditors' committee could not pursue both objectives with equal vigor.[23]

Section 1103 has also been interpreted to preclude a law firm from representation of creditors' committees in other bankruptcy cases where there is a possibility of outstanding obligations from the debtors in one case to the other.[24] Representation of any individual committee member will also disqualify the attorney selected by the creditors'

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19. *See President Ungerman Represents League on H.R. 3949*, 86 COMM. L. J. 367-369 (Oct. 1981).

20. *See* B.R.A. § 547. A preference is a transfer by an insolvent to a creditor which will enable the creditor to receive a greater percentage of his debt than other creditors of the same class. *Id.*

21. 11 U.S.C. § 547 (1982).

22. MODEL CODE OF PROFESSIONAL RESPONSIBILITY, DR 5-105 (1980) (An attorney must refuse to accept or continue employment if the interests of another client may impair the independent professional judgment of the lawyer).

23. "An attorney who has been closely related by professional, business and personal ties to those whose conduct may now be suspect is evidently in no position to make any objective appraisal of the nature and extent of their involvement." *In re* Bohack Corporation, 607 F.2d 258, 264 (2d Cir. 1979). *But see* Matter of Allied Artists Pictures Corp. 17 Bankr. 288 (Bankr. S.D.N.Y. 1982).

24. *In re* Proof of the Pudding, Inc., 3 Bankr. 645, 648, (Bankr. S.D.N.Y. 1980).

committee.[25] This line of cases reflects the prophylactic standard generally applied outside of bankruptcy. Judge Friendly admonished, "[t]he conduct of bankruptcy proceedings not only should be right but must seem right."[26] On the whole, conflict of interest issues at the creditors' committee level are governed by standards designed to prevent any potential manifestation of conflict.

The Bankruptcy Code reinforces the spirit of the Model Code[27] by denying compensation for services and reimbursement of expenses of a professional person employed under 1103(a) if at any time during such employment, the person is not disinterested or holds or represents an interest adverse to the estate's interest with respect to the matter for which the person is employed.[28] The object of the B.R.A. is to ensure that an attorney employed by the creditors' committee does not have any interest which might impair his professional judgment in the case. In *In re Combustion Equipment Associates*,[29] the court established that even the appearance of conflict was to be avoided; thus the provisions of 11 U.S.C. § 1103(b) cannot be waived by the parties in interest.[30] If the court determines that there has been representation of an adverse interest it will deny compensation and reimbursement pursuant to section 328(c). The fee penalty is a prophylactic measure to prevent not only actual conflicts but also the mere possibility of divided loyalty.[31] Although these provisions do not extend so widely as Canons 4, 5 and 9, courts have generally found them sufficient to indicate that a stringent standard should be applied to conflict of interest questions for creditors' committee attorneys.

The less restrictive text of Model Rules 1.6, 1.7 and 1.9 are more closely aligned with the B.R.A. provision but are unlikely to work any substantial change upon courts' construction of the Act.

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25. *In re* Cumbustion Equip. Assoc., Inc., 8 Bankr. 566, (Bankr. Ct. S.D.N.Y. 1981). *See also* S. REP. 863, 97th Cong., 1st Sess. 94 (1981); S. REP. No. 150, 97th Cong., 1st Sess. 18-19 (1981).

26. *In re* Ira Haupt & Co., 361 F.2d 164, 168 (2d Cir. 1966). *See also* House Report, *supra* note 3, at 407.

27. *In re* Paine, 14 Bankr. 272, 274 (Bankr. W.D. Mich. 1981) ("The cancellation of the [attorney] fees was nothing more than a penalty for violation of the Code of Professional Responsibility.")

28. 11 U.S.C. § 101(13) (1982), *see also* 11 U.S.C. § 324 (1982).

29. *Supra* note 25.

30. *In re* Combustion Equip. Assoc., Inc., 8 Bankr. at 568.

31. *See, e.g., In re* Paine, 14 Bankr. 272 (Bankr. W.D. Mich. 1981) *citing* Weil v. Neary, 278 U.S. 160 (1929). *But cf. In re* Laurent Watch Co., 539 F.2d 1231 (9th Cir. 1976); Stolkin v. Nachman, 472 F.2d 222 (7th Cir. 1973).

In a Chapter 7 case, section 702 requires the court to appoint a interim trustee after the order for relief. The interim trustee's services terminate when the creditors elect a trustee at a meeting of the creditors.[32] In addition to electing a trustee, the creditors may elect a creditors' committee (or continue a committee organized under Chapter 11 as discussed above).[33] The committee will have a generally advisory function.[34] The most difficult bankruptcy related conflict of interest cases arise when the trustee exercises his power to appoint professional persons by selecting the same attorney who represented the creditors' committee. The pertinent parts of 11 U.S.C. § 327(a) and (c) state:

> (a) . . . the trustee, with the court's approval, may employ one or more attorneys, . . . 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.
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> (c) In a case under Chapter 7 or 11 of this title, a person . . . may not, while employed by the trustee, represent, in connection with the case, a creditor.

The statutory language governing the selection of an attorney to represent the trustee does not automatically bar the employment of an attorney who previously represented a creditor. Section 327(c) represents a compromise between H.R. 8200 as passed by the House and the Senate Amendment. The provision states that former representation of a creditor, whether secured or unsecured, will not *automatically* disqualify a person from being employed by the trustee; but if such person is employed by the trustee, the person may no longer represent the creditor in connection with the case.[35]

Under prevailing practice, when the trustee appoints an attorney previously employed by an individual creditor or by the creditors' committee the attorney resigns from representation of the creditor(s). The trustee selects such an attorney to take advantage of his pre-existing knowledge and preparation. The motivation for the attorney to resign in favor of employment by the trustee lies somewhere between the altruistic goal of playing a larger role in the reorganization or orderly liquidation of the estate and the desire for larger fees.

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32. *Compare* 11 U.S.C. § 701 (1982) *with* Bankruptcy Rule 201.
33. 11 U.S.C. § 705 (1982); *see also* Bankruptcy Rules 207, 208.
34. *Compare* 11 U.S.C. § 705(b) (1982) *with* Bankruptcy Rule 214.
35. 124 CONG. REC. H. 11091 (Sept. 28, 1978).

Under the Model Code, a lawyer may withdraw if the client "knowingly and freely assents."[36] Since the protected interest is the client's confidentiality, clearly the client may consent and waive his right to object to successive representation.[37] The attorney must disclose completely any future potential conflicts of interest to insure an effective consent.[38] Under the Model Code, DR 5-105(c) places the burden of proof on the attorney and resolves doubts in favor of the client.[39] Model Rule 1.9 explicitly permits a former client to waive his right to disqualify his attorney.[40]

Model Rules 1.7 and 1.9 clarify the necessary mechanisms of client consent to successive representation that were somewhat vague in the Model Code.[41] The Official Comments to both 1.7 and 1.9 stress a case-by-case analysis and explain that mere possible conflict is insufficient to disqualify an attorney.[42]

Beyond the enabling effect of the statutory language, the courts are very deferential in allowing the trustee to select his counsel. To some extent, Bankruptcy courts have relied upon the freedom to select one's own counsel[43] and expanded the concept as a counterbalance to the general conflict of interest considerations.[44] This development appears to represent a general trend to accord greater freedom to retain counsel and lesser importance to the appearance of impropriety.

Bankruptcy courts are favorably disposed to permit the successive

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36. MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 4-110(C); 2-110 (1980).

37. *See, e.g., In re* Yarn Processing Patent Validity Litig., 530 F.2d 83, 89 (5th Cir. 1976); City of Cleveland v. Cleveland Elec. Illuminating Co., 440 F. Supp. 193, 205 (N.D. Ohio), *aff'd mem.*, 573 F.2d 1310 (6th Cir. 1977), *cert. denied*, 435 U.S. 966 (1978).

38. E.F. Hutton & Co. v. Brown, 305 F. Supp. 371, 400 (S.D. Tex. 1969).

39. *Id. See also* Note, *Attorney's Conflict of Interests: Representation of Interest to that of Former Client*, 55 B. U. L. REV. 61, 82 (1975).

40. MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.9 (1983).

41. *Id.*

42. *Id.*

43. *E.g., In re* Mandell, 69 F.2d 830, 831 (2d Cir. 1934); Hull v. Celanese Corp., 513 F.2d 751 (2d Cir. 1975); Emle Indus. v. Patentex, Inc., 478 F.2d 568, 572 (2d Cir. 1973).

44. *See, e.g.*, W.T. Grant Co. 4 Bankr. 53, 82 (S.D.N.Y. 1980): "It is a cardinal principle of bankruptcy administration that a trustee in bankruptcy is entitled to engage attorneys of his choice, subject only to the approval of the court." (citing *In re* Magna Products Corp., 251 F.2d 423, 424 (2d Cir. 1957)); *see also In re* Columbia Iron Works, 142 F. 234 (E.D. Mich. 1904); *In re* Christ's Church of the Golden Rule, 157 F.2d 910 (9th Cir. 1946). *But see In re* Philadelphia Athletic Club, Inc., 20 Bankr. 328, 335 (Bankr. E.D.PA. 1982).

representation of the creditors' committee and the trustee for the purpose of efficiency—the same reason that the trustee selected the attorney. "There is . . . an overriding concern in the Act with keeping fees and administrative expenses at a minimum so as to preserve as much of the estate as possible for the creditors."[45] Obviously, the creditors' committee attorney will already be armed with the facts and circumstances of the estate and will be prepared to proceed in less time, thereby reducing expenses. This economy, however, is a two-edged sword. An attorney for the creditors' committee would have a reduced incentive to implement a successful reorganization plan in a bankruptcy court where the trustee employes the same attorney. A lucrative income stream can be assured by a failed reorganization, particularly in a complex case. Such incentives are clearly in derogation of Canon 5 and EC 5-15.[46] Further, it is reasonable to assume that the creditors' committee will consult their attorney with respect to their claims and their strategy for attaining a favorable reorganization plan. These matters are within the scope of the attorney-client relationship and are confidential.[47]

In addition to minimizing conflicts and the appearance of conflicts, another goal of sections 327 and 1103 is to reduce the scramble by lawyers for positions in bankruptcy or reorganization cases.[48] In an early application of section 327,[49] the court, in *In re Market Response Group, Inc.*, examined the factors discussed above and refused to grant the trustee's application to employ the former counsel to a Chapter 11 creditors' committee.[50] On a motion for reconsideration the court granted the application but only with great reluctance. The court concluded that the legislative mandate required the appointment, but only where the court is persuaded that no conflict of interest exists or will exist.[51] The court emphasized that appointment of the creditors' committee attorney will "not be made in a perfunctory, *pro forma* manner without full consideration of whether such employment is in the best

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45. Otte v. United States, 419 U.S. 43, 53 (1974).

46. *In re* Codesco, Inc., 18 Bankr. 997 (Bankr. S.D.N.Y. 1982).

47. *In re* Proof of Pudding, Inc., 3 Bankr. at 647 ("The attorney for a creditors' committee does not act in a vacuum; he is hired to pursue the interests of said committee.").

48. House Report, *supra* note 3, at 92, 96-97, 102-105.

49. *In re* Market Response Group, Inc., 20 Bankr. 151 (Bankr. E.D. Mich. 1982).

50. *Id.* at 152.

51. *Id.* at 153.

interest of the estate."[52] The trustee argued that representation by the former counsel to the creditors' committee would improve the efficiency of the administration of the estate and that the attorney was not an adversary to the creditors[53] and cited *In re W.T. Grant Co.*[54] where the court stated: "the role of counsel to an Official Creditors' Committee is not adverse to a bankruptcy trustee if liquidation should ensue."[55] The *Market Response* Court refused to adopt the *Grant* blanket categorization and concluded that it will approve such employment only after the "utmost scrutiny," when it is clear and certain that no conflict, or potential for conflict, exists.[56] The Court emphasized that it would resolve all doubts in favor of attorney disqualification.[57]

Subsequent to the *Market Response* decision there has been some deterioration of the "utmost scrutiny" standard. Courts have seized upon the "not per se in conflict" language found in, but not relied upon, by the *Market Response* Court.[58] Two cases are particularly illustrative of this trend. In *In re Codesco*,[59] the court enumerates some of the potential conflicts and endorses the conflict prevention principles discussed above, but then allows the representation in the face of a potential conflict of interest by stating that the mere possibility of conflict is not sufficient reason to deny the trustee his desired attorney. In *In re Whitney-Forbes*,[60] the court gives its interpretation of the rule of *Market Response* to be that "bankruptcy courts generally have allowed former counsel to the creditors' committee to represent the trustee."[61] This is an inaccurate statement of the holding. The utmost scrutiny standard is completely ignored and the acceptance of the creditors' committee has become exactly the type of pro forma action that the *Market Response* court held inadequate to protect the interests of the estate and the integrity of the bankruptcy bench and bar. An actual injury standard now replaces the prophylactic standard in *Whitney-Forbes* and the court refuses to disqualify an attorney until it finds true adversity of representation.

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52. *Id.* at 153 (emphasis in original).
53. *Id.*
54. *In re* W.T. Grant Co., 4 Bankr. 53 (Bankr. S.D.N.Y. 1980).
55. *Id.* at 83.
56. *Id.*
57. *In re* Market Response Group, 20 Bankr. at 153 (citations omitted).
58. *Id.* 151.
59. 18 Bankr. 997, 1000 (Bankr. S.D.N.Y. 1982).
60. *In re* Whitney-Forbes, Inc., 31 Bankr. 836 (Bankr. N.D. Ill. 1983).
61. *Id.* at 840.

Section 327(d)[62] specifically permits the court to authorize the trustee to act as his own counsel with the qualification that self-representation be in the best interest of the estate. Such an appointment would be in the best interest of the estate where the trustee sought to reduce duplication of effort with a view towards reducing the costs of administration.[63]

The potential for abuse of this section has proved tempting to some trustee attorneys. These unscrupulous attorneys avoid the goals of section 327(d) by allocating to themselves, as attorney, functions that would normally be performed by the trustee in order to inflate their fees. Unless the services rendered by the trustee as trustee and those rendered by the trustee as his own counsel are distinguished, the limitations on trustee compensation established in 11 U.S.C. § 326 are completely circumvented.[64] The B.R.A. dealt with this problem by limiting the compensation of professional persons under 11 U.S.C. § 328(b). The purpose of section 328(b) was stated in the legislative history:

> Subsection (b) limits a trustee that has been authorized to serve as his own counsel to one fee for each service. The purpose of permitting the trustee to serve as his own counsel is to reduce costs. It is not included to provide the trustee with a bonus by permitting him to receive two fees for the same service or to avoid the maxima fixed in section 326.[65]

If a challenge to the allocation of fees and services develops, an inherent conflict arises between the trustee's duty to preserve the assets of the estate and the attorney's desire to be compensated. The complexity of the problem is graphically illustrated by the court in *In re First Colonial Corp. of America*:[66]

> [T]he rule does not resolve the problems that may arise when a trustee-attorney's personal interest in the amount of compensation

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62. 11 U.S.C. § 327(d) (1982). This section is essentially a restatement of Bankruptcy Rule 215(e).

63. *See In re* Smith, 8 Bankr. 699 (Bankr. D.R.I. 1981) (emphasizing that the purpose of permitting a trustee to serve as his own counsel was to reduce costs).

64. *See In re* McAuley Textile Corp., 11 Bankr. 646 (Bankr. D. Me. 1981) (The court sets out respective duties of trustee and attorney); *In re* Ira Haupt, 361 F.2d 164 (2d Cir. 1966); *see also In re* SMS, Inc., 15 Bankr. 496 (Bankr. D. Kan. 1981).

65. House Report, *supra* note 2, at 329; *see also* S. REP. No. 989, 95th Cong., 2d Sess. 39 (1978).

66. 544 F.2d 1291 (5th Cir.), *cert. denied*, 431 U.S. 909 (1977).

> he receives in exchange for his services as attorney leads him to take a position adverse to that of the bankrupt and its shareholders whose interests he is charged with protecting in his role as trustee. Where the trustee serves as his own attorney there is no disinterested trustee to ensure that the attorney is paid only for professional services necessary to the administration of the estate. In this situation it is unseemly, to say the least, for a trustee-attorney to urge on appeal, first, that the compensation he was awarded for furnishing legal services to the bankrupt estate should be increased, and second that the bankrupt and its shareholders have no standing to object to the amount of compensation because the Bankruptcy Act makes safeguarding their interests his responsibility.[67]

Weighed against these conflicts or appearance of conflicts is the explicit legislative directive to utilize the trustee-attorney arrangement to save costs where possible. The courts can minimize unseemly behavior by wielding the power of section 328(c) to deny compensation if the professional person is not disinterested or has a conflicting interest.[68]

If the trustee employs the debtor's attorney, 11 U.S.C. § 327(e) governs. The trustee may employ the debtor's attorney for a specified special purpose if the employment is in the best interest of the estate and the attorney is not adverse to the estate or does not represent an interest adverse to the estate with respect to the specific matter for which he is employed. This subsection is most often employed when the debtor is engaged in complex litigation at the time of the filing of the petition and changing of attorneys would be detrimental to the litigation.[69]

The Bankruptcy Appellate Panel of the Ninth Circuit held that a creditor's attorney who was, himself, a defendant in a suit by the debtor, could nevertheless be a special counsel to the trustee under section 327(e).[70] Analysis of section 327(e) by the court indicates that the section does not require that an attorney serving as the trustee's special counsel cease representing the creditors in the case because special counsel has a limited role and is therefore less adverse.[71]

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67. *Id.* at 1297.

68. House Report, *supra* note 3, at 329 ("This subsection provides a penalty for conflicts of interest.").

69. House Report, *supra* note 3, at 328.

70. *In re* Fondiller, 15 Bankr. 890, 892 (Bankr. 9 Cir. 1981).

71. *Id.*

Conclusion

This comment has attempted to illustrate the competition among various goals of the Bankruptcy Reform Act as related to conflicts of interest and, to a limited extent, their interrelationship with the Model Code and Model Rules. It is impossible to detail all the possible permutations of conflicts that may arise in bankruptcy. Attorneys must understand the underlying policy considerations of efficiency and freedom to choose an attorney and balance those against the interests of the parties and the appearance of impropriety. There is no clear answer or standard which may be applied. The bankruptcy lawyer must respond to two mandates: make the bankruptcy system more efficient, and maintain both the apparent and actual propriety of the legal profession. Careful analysis of the potential conflicts illustrated above will serve as a guide.

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