Case No. 82467

IN THE SUPREME COURT OF NEVADA

UNITE HERE HEALTH, a multi-employer health and welfare trust, as defined in ERISA Section 3(37); and NEVADA HEALTH SOLUTIONS, LLC, a Nevada limited liability company,

Appellants,

vs.

STATE OF NEVADA EX REL. COMMISSIONER OF INSURANCE, BARBARA D. RICHARDSON, IN HER OFFICIAL CAPACITY AS STATUTORY RECEIVER FOR DELINQUENT DOMESTIC INSURER, NEVADA HEALTH CO-OP; and GREENBERG TRAURIG, LLP,

Respondents.

District Court Case No. A-15-725244-C, Department XXI

APPELLANTS' UNITE HERE HEALTH AND NEVADA HEALTH SOLUTIONS, LLC'S OPENING BRIEF

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June 14, 2021

NRAP 26.1 DISCLOSURE STATEMENT

Pursuant to Nevada Rule of Appellate Procedure 26.1, Appellants UNITE HERE HEALTH and NEVADA HEALTH SOLUTIONS, LLC (jointly, "UHH") submit this Disclosure Statement:

The undersigned counsel of record certifies that the following are persons and entities as described in NRAP 26.1(a), and must be disclosed. These representations are made in order that the judges of this Court may evaluate possible disqualification or recusal.

1. Unite Here Health is a multi-employer health and welfare trust, as defined in ERISA Section 3(37). It has no parent company, and no publicly held companies own ten (10) percent or more of its stock.

2. Nevada Health Solutions, LLC is a Nevada limited liability company. It is wholly owned by Unite Here Health. No publicly held companies own ten (10) percent or more of its stock.

3. The law firm of Bailey❖Kennedy represented UHH in the underlying action and continues to represent them for the purposes of this appeal.

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4. Neither Unite Here Health nor Nevada Health Solutions, LLC are using a pseudonym for the purposes of this appeal.

DATED this 14th day of June, 2021.

BAILEY❖KENNEDY

By: */s/ Dennis L. Kennedy*
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I. JURISDICTIONAL STATEMENT

This is an appeal from an Order denying Appellants Unite Here Health and Nevada Health Solutions, LLC's (jointly, "UHH") Motion to Disqualify Greenberg Traurig, LLP ("Greenberg") and to Disgorge Attorneys' Fees ("Order Denying Disqualification"). (13A.A.52[1].) The Order Denying Disqualification is appealable pursuant to NRS 696B.190(5), which provides that "[a]n appeal to the appellate court of competent jurisdiction pursuant to the rules fixed by the Supreme Court pursuant to Section 4 of Article 6 of the Nevada Constitution may be taken . . . from every order in delinquency proceedings having the character of a final order as to the particular portion of the proceedings embraced therein."

Pursuant to NRS 696B.060, the underlying action is a "delinquency proceeding" because it was commenced by Respondent State of Nevada ex rel. Commissioner of Insurance, Barbara D. Richardson, in her official capacity as a statutory receiver for the delinquent domestic insurer, Nevada Health CO-OP ("Receiver") against Nevada Health CO-OP ("CO-OP") for the purpose of

[1] For citations to the Appellants' Appendix, UHH will refer to "A.A." The number preceding "A.A." refers to the applicable volume of the Appellants' Appendix, and the number succeeding "A.A." refers to the applicable tab number of the exhibit.

rehabilitation or liquidation. (1A.A.3 at 0011:22-27; 1A.A.6 at 0072:26-0073:4.) While neither the Legislature nor this Court has yet addressed the types of orders which have the "character of a final order" in delinquency proceedings, this Court has defined a "final judgment" as a judgment or order that leaves no issues for future determination or consideration. *Valley Bank of Nev. v. Ginsburg*, 110 Nev. 440, 445, 874 P.2d 729, 733 (1994); *Lee v. GNLV Corp.*, 116 Nev. 424, 426, 996 P.2d 416, 417 (2000).

UHH's Motion to Disqualify Greenberg Traurig, LLP and to Disgorge Attorney's Fees ("Motion to Disqualify") raised very discrete issues — whether Greenberg should be disqualified for breaching its fiduciary duties due to its myriad conflicts of interest in representing the Receiver while also concurrently representing: (i) Valley Health System ("Valley"), one of the most significant creditors of the CO-OP's receivership estate ("Receivership Estate"); and (ii) Xerox State Healthcare, LLC ("Xerox"), a potential target defendant for the recovery of assets for the Receivership Estate and its creditors. (7A.A.37.) The Order Denying Disqualification fully and finally resolved the discrete issues raised in the Motion to Disqualify. (13A.A.52.) Thus, the Order Denying Disqualification has the character of a final judgment as to the issues raised in the Motion to Disqualify. As such, UHH has the right to appeal from

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the Order Denying Disqualification pursuant to NRS 696B.190(5). *See Fewell v. Pickens*, 39 S.W.3d 447, 449, 451 (Ark. 2001) (interpreting a virtually identical statute and holding that an order appointing a receiver and permanently enjoining a delinquent insurer's parent company and shareholder from transacting any business with the insurer had the character of a final order and was appealable); *see also In re Enron Corp.*, No. 02 Civ. 5638 (BSJ), 2003 U.S. Dist. LEXIS 1442, *6-9 (S.D.N.Y. Feb. 3, 2003) (holding that orders resolving motions to disqualify counsel are final and appealable in bankruptcy proceedings which allow appeals from orders which "finally dispose of discrete disputes within the larger case").

The Order Denying Disqualification was entered on January 15, 2021. (13A.A.52.) Pursuant to NRAP 4(a)(1), UHH timely filed a Notice of Appeal on February 8, 2021. (13A.A.53.)

On February 26, 2021, UHH also filed a Petition for Extraordinary Writ Relief (No. 82552), seeking a writ of mandamus reversing the Order Denying Disqualification and instructing the Receivership Court to grant the Motion to Disqualify and rule on the issue of disgorgement. On April 12, 2021, this Court granted UHH's Motion to Consolidate this Appeal and the Petition for Extraordinary Writ Relief and instructed UHH to file this Opening Brief.

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II. ROUTING STATEMENT

UHH believes that the issues raised in this appeal should be retained by the Supreme Court pursuant to NRAP 17(a)(11) and (12). This appeal does not fall within any of the categories of cases presumptively assigned to the Court of Appeals pursuant to NRAP 17(b). Moreover, this appeal presents as principal issues two questions of statewide public importance which are also issues of first impression:

- Whether fiduciaries (receivers and/or special deputy receivers and their counsel) have an obligation to disclose to the court in a receivership action, at the time of their appointment, actual or potential conflicts of interest.
- Whether attorneys with actual or potential conflicts of interest in a receivership action can be disqualified from representing the receiver (and special deputy receiver) and the receivership estate due to such conflicts of interest.

This Court has not yet addressed either of these issues, and both issues are of statewide public importance because they concern the obligations of attorneys, fiduciaries, and receiverships. Compliance with these obligations is

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of the utmost importance to maintaining the public's confidence in a fair and impartial judicial system, especially involving neutral receiverships.

III. STATEMENT OF ISSUES PRESENTED FOR REVIEW

UHH presents the following issues for review in this appeal:

1). Did the Receivership Court err when it ruled that fiduciaries (such as receivers and/or special deputy receivers and their proposed counsel) have no obligation to disclose conflicts of interest to the Receivership Court at the time of their potential appointment?

2). Did the Receivership Court err in denying the Motion to Disqualify given the Receiver's, Special Deputy Receiver's ("SDR"), and/or Greenberg's failure to disclose Greenberg's known conflicts of interest?

3). Did the Receivership Court err when it ruled that Greenberg did not have a "clear and substantial enough possible conflict" because Xerox was not currently a named party in any of the lawsuits in which Greenberg is counsel of record?

4). Did the Receivership Court err when it failed to consider whether Greenberg's concurrent representation of Valley, a significant creditor of the Receivership Estate, was another basis for Greenberg's disqualification?

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5). Did the Receivership Court err in denying the Motion to Disqualify based on Greenberg's multiple and known conflicts of interest?

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IV. STATEMENT OF THE CASE

On September 25, 2015, the Nevada Department of Insurance ("NDOI") commenced a delinquency proceeding against the CO-OP by filing a Petition for Appointment of its Commissioner as Receiver and Other Permanent Relief; Request for Temporary Injunction Pursuant to NRS 696B.270(1). (1A.A.3.) On October 1, 2015, the Receivership Court appointed the NDOI's Commissioner as the temporary Receiver for the CO-OP, and on October 14, 2015, the Commissioner was appointed as the CO-OP's permanent Receiver "for the purpose of conservation/rehabilitation." (1A.A.3 at 0011:22-0012:2; 1A.A.4 at 0056:26-0057:3; 1A.A.5 at 0060:9-10, 16-19.) The Texas law firm of Cantilo & Bennett was also appointed as the Permanent SDR of the CO-OP. (1A.A.5, at 0060:3-5, 9-10.)

On July 21, 2016, the Receiver filed a motion to declare the CO-OP insolvent and to place it into liquidation. (1A.A.6.) On September 21, 2016, the Receivership Court granted the motion. (1A.A.8, at 0114:2-5.)

On December 19, 2016, the Receiver filed a motion to approve the engagement of Greenberg as her counsel in the action. (1A.A.10, at 0192:24-25, 0193:1-2.) The Receivership Court granted the motion on January 23, 2017. (2A.A.12, at 0236:25-27.)

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On October 8, 2020, UHH filed the Motion to Disqualify, seeking disqualification of Greenberg as counsel for the Receiver and disgorgement of all fees and costs paid by the CO-OP to Greenberg. (7A.A.37.) The Receiver filed its opposition to the Motion to Disqualify on November 16, 2020, and UHH filed a reply in support of the Motion to Disqualify on December 8, 2020. (10A.A.45; 12J.A48.) The Receivership Court held a hearing on the Motion to Disqualify on December 15, 2020, and on January 15, 2021, the Court denied the Motion to Disqualify. (12A.A.49; 13A.A.52.)

V. STATEMENT OF FACTS

A. Background of the Silver State Health Insurance Exchange and the CO-OP.

In 2010, the United States enacted the Patient Protection and Affordable Care Act ("ACA"). 42 U.S.C. § 18001, et seq. In 2012, the CO-OP was created as a non-profit insurance company which offered health insurance to eligible individuals and small businesses under the ACA. (1A.A.3 at 0016:2-22; 2A.A.13 at 0239:2-4.) To assist with its operations, the CO-OP contractually retained Unite Here Health as a third-party administrator of some of its medical claims. (4A.A.22 at 0654:20-21, 0704:20-22, 0705:10-23.) Similarly, Nevada Health Solutions, LLC — an entity affiliated with Unite Here

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Health, was contractually retained by the CO-OP to perform utilization management services. (*Id.* at 0655:18-19, 0656:7, 0695:19-26.)

An essential aspect of the ACA was the marketplace in which consumers were required to purchase their health insurance. The ACA provided for the creation of American Health Benefit Exchanges, where consumers could evaluate and purchase insurance policies from various ACA insurers, including, but not limited to, the CO-OP. 42 U.S.C. § 18031(b). Nevada elected to create its own health exchange and created an agency, the Silver State Health Insurance Exchange ("Silver State"), to develop and oversee it. NRS 695I.200.

B. Xerox's Failures and the Damage It Caused to the CO-OP.

In 2012, Silver State awarded Xerox a $72 million contract to administer and operate Nevada's health exchange ("Xerox Exchange"). (1A.A.2, at 0008; 8A.A.38 at 1400, at ¶ 6; 12A.A.50 at 2307:26-27.) Some of Xerox's primary duties included ensuring that the Xerox Exchange promptly transferred accurate consumer data and premium payments to insurers and/or their vendors, including, but not limited to, the CO-OP and UHH. (8A.A.38 at 1410, 1414-1416, 1420-1422.)

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However, beginning with its initial rollout on October 1, 2013, the Xerox Exchange was a disaster.[2] (*Id.* at 1450-1540.) Xerox's failures led Silver State to engage Deloitte Consulting LLP ("Deloitte") to evaluate the Xerox Exchange, and Deloitte found more than 1,500 defects — over 500 of which were of a "higher severity." (*Id.* at 1452, 1459.) Ultimately, Silver State terminated Xerox and switched to a federally facilitated exchange. (1A.A.1 at 0004; 1A.A.2 at 0008.)

In order for the CO-OP and UHH to serve the CO-OP's insureds and process their claims timely and appropriately, the CO-OP and UHH were heavily reliant on Xerox to provide them with the necessary data and premium payments that Xerox gathered and received via the Xerox Exchange. (*See e.g.*, 8A.A.38, at 1554-1557; 12A.A.48 at 2160.) However, the CO-OP encountered severe difficulties from the poorly designed and poorly managed Xerox Exchange.

For instance, in early 2014 (a critical time for the CO-OP's initial enrollment), the CO-OP was experiencing "ongoing issues and challenges" with

[2] In fact, in 2014, Xerox even publicly admitted in a letter from its Chairman and CEO to "All Nevadans" that there were "challenges" associated with the Xerox Exchange, including, but not limited to, "website errors and other processing delays." *See https://www.xerox.com/downloads/usa/en/x/Xerox_Nevada_Healtlh_Link_Letter.pdf*

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the "enrollment process" through the Xerox Exchange. (8A.A.38 at 1542.) The issues and challenges were so pervasive that the CO-OP's CEO was participating in meetings with the Governor's office, other insurance carriers, and Xerox three times a week to discuss "the challenges the CO-OP [wa]s experiencing with data submission from Xerox." (2A.A.17 at 0356:11-15; 8A.A.38 at 1542-1543.) These issues and challenges included, but were not limited to, the fact that Xerox had failed to transmit any data to the CO-OP pertaining to over 3,000 of the CO-OP's members or "pending" members. (8A.A.38 at 1543.) Moreover, Xerox was not timely providing the CO-OP with "834" electronic transmissions of enrollment data or "820" electronic transmission of payments — and when this data was finally received by the CO-OP, it was routinely incomplete. (*Id.*) In fact, Xerox's failures were having such a significant impact on the CO-OP's operations that on February 24, 2014, the CO-OP sent a letter to the Governor and Xerox stating that despite the fact that the CO-OP had "attracted 37% of the [Xerox] Exchange market share," Xerox's "broken enrollment system" was "undeniably the greatest threat to [the CO-OP's] operations." (*Id.* at 1336.)

In or around May 2014, Xerox admitted that its "[premium] payment collection process [wa]s only working at 45% capacity to accept payments."

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(1A.A.1 at 0005; 9A.A.39 at 1600.) As a result, "over 4,000 consumers" were unable to pay their premiums "due to system errors with Xerox." (*Id*.) Further, when "Xerox presented the CO-OP with the [Xerox] Exchange's most recent [premium payment] delinquency report[, it included] over 900 [CO-OP] members dat[ing] back to January 2014[,] that were never reported and the CO-OP was unaware of." (*Id*.) This means that the CO-OP had been paying claims for members who had been ineligible for coverage for months. Strikingly, by May 2014, the CO-OP determined that "Xerox ha[d] drained the CO-OP's resources[,] as no less than 50% of the CO-OP's resources ha[d] been committed to Xerox and Xerox[-]related issues since October 2013." (*Id*.)

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C. <u>The Appointment of a Receiver for the CO-OP.</u>

The CO-OP began selling individual, small group, and large group managed health care insurance to Nevadans in January 2014. (2A.A.13, at 0239:15-17.) However, by August 2015, the CO-OP's Board of Directors voted to cease selling such insurance to new members and to voluntarily suspend its Certificate of Authority granted by the NDOI. (2A.A.17 at 0395:3-6.)

Consequently, on September 25, 2015, the then-acting Insurance Commissioner (Amy L. Parks) filed a Petition for appointment as Receiver of

the CO-OP "for the purpose of conservation/rehabilitation" and for permanent injunctive relief in order to "ascertain the CO-OP's true and current state of affairs, to conserve its assets, and [to] protect the policyholders and public from the dangers inherent to the delinquency" of the CO-OP. (1A.A.3, at 0011:22-0012:2.) On October 1, 2015, the Receivership Court entered an order appointing the Insurance Commissioner as the Temporary Receiver for the CO-OP and granting temporary injunctive relief. (1A.A.4.) On October 14, 2015, a permanent injunction was entered, the Insurance Commissioner was appointed as a Permanent Receiver for the CO-OP, and Cantilo & Bennett, L.L.P was named as the SDR. (1A.A.5 at 0060:9-10.) After Barbara Richardson was appointed as the new Commissioner of Insurance for the NDOI, she was substituted as the Receiver for the CO-OP. (2A.A.13 at 0239:26-0240:2.)

On July 21, 2016, the Receiver moved for a final order declaring the CO-OP to be insolvent and placing it into liquidation. (1A.A.6.) On September 21, 2016, the Receivership Court granted the motion. (1A.A.8 at 0114:2-5.)

D. Greenberg's Representation of Valley in the Delinquency Action.

On August 8, 2016, on behalf of Valley, Greenberg filed a response to the Receiver's motion for final order declaring the CO-OP to be insolvent and

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placed into liquidation. (1A.A.7.) Specifically, Greenberg, on behalf of Valley, requested that the declaration of insolvency and order for liquidation be held in abeyance until the Receiver could demonstrate that it had identified all potential sources for recovery of the assets of the CO-OP and could demonstrate all efforts undertaken to obtain those assets for the CO-OP's creditors. (*Id.* at 0102:5-10.) Greenberg represented that Valley was raising these concerns about efforts for asset recovery for the Receivership Estate because Valley had "a substantial claim exceeding $5 million in this case." (*Id.* at 0107:18.)

E. <u>The Appointment of Greenberg as Counsel for the Receiver.</u>

On December 19, 2016, ***just four months after Greenberg appeared in the delinquency proceeding <u>on behalf of Valley</u>***, the Receiver filed a motion in the delinquency proceeding seeking the Court's approval for the engagement of Greenberg as ***<u>her</u>*** counsel. (1A.A.10 at 0192:24-25, 0193:1-2.) The Deputy Attorney General, who served as the original counsel for the Receiver in the delinquency proceeding, asserted that Greenberg's representation was needed because "the Receiver does not have access to the legal resources necessary to evaluate the prosecution and defense of litigation." (*Id.* at 0190:11-12.) The Deputy Attorney General also claimed that the "Receiver needs immediate assistance of legal counsel and consulting firms with specialized expertise for

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the evaluation and resolution of [the creditors'] claims, which may also include the pursuit of related counterclaims." (*Id.* at 0190:12-16.)

In the motion to approve Greenberg's representation, neither Greenberg, the Receiver, nor the SDR made any disclosures regarding Greenberg's conflict of interest in representing Valley and seeking to represent the Receiver in the same action. (1A.A.10.) Thus, the Receivership Court only expressed concerns about Greenberg's substantial hourly rates and how such rates could deplete the CO-OP's assets and lead to reduced payments for the CO-OP's creditors. (9A.A.39 at 1663:22-1664:8.) Nonetheless, the Receivership Court approved Greenberg's engagement. (2A.A.12 at 0236:25-27.)

F. <u>Greenberg's Representation of Xerox.</u>

At the time the Receiver sought approval from the Receivership Court for Greenberg's appointment as its counsel in the delinquency proceeding, Greenberg was also serving as ***counsel for Xerox*** in the following ***related*** matters:

- *Basich v. State of Nevada ex rel. Silver State Health Insurance Exchange*, No. A-14-698567-C, Eighth Judicial District Court, Clark County, Nevada — a class action filed on behalf of all Nevada consumers who purchased insurance policies on the

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Xerox Exchange and did not receive the benefits of such policies, (9A.A.39 at 1674, 1676:1-4, 1677:7, 1693:18-23);

- *Casale v. State of Nevada ex rel. Silver State Health Insurance Exchange*, No. A-14-706171-C, Eighth Judicial District Court, Clark County, Nevada — a class action filed on behalf of all Nevada brokers owed unpaid commissions for the sale of insurance policies on the Xerox Exchange, (*id.* at 1675, 1676:1-4, 1677:7, 1693:18-25); and
- *In the Matter of Xerox State Healthcare, LLC*, No. 17-0299, State of Nevada, Department of Business and Insurance, Division of Insurance — a regulatory action involving Xerox's failures in developing, administering, and managing the Xerox Exchange, (*id.* at 1692:9-10, 1693:1-17).[3]

Undeniably, Xerox's various deficiencies in administering and operating the Xerox Exchange were well known to Greenberg — particularly given that the two class actions referenced above culminated in a settlement agreement whereby ***Xerox was obligated to pay up to $5,000,000 in damages and***

[3] Greenberg was also representing Xerox in two, unrelated matters, and it continued to represent Xerox in the unrelated matters until at least 2018. (9A.A.39 at 1708-1710, 1713-1719.)

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$1,750,000 in class counsel's attorneys' fees. (*Id*. at 1683:23-25, 1687:22-1688:18.) Despite this knowledge that Xerox was a substantial target for asset recovery for the Receivership Estate, neither Greenberg, the Receiver, nor the SDR ever disclosed to (and concealed from) the Receivership Court Greenberg's known conflicts of interest arising from its concurrent representation of Xerox in these related matters.

G. Greenberg Actively Conceals Its Representation of Xerox From the Receivership Court.

In the Receivership Court, the Receiver was required to file quarterly status reports. (*See*, *e.g.*, 1A.A.9 at 0128:2-3.) In the Eighth Status Report, filed on October 6, 2017, Greenberg, on behalf of the Receiver, disclosed that "Counsel for Xerox" in the *Basich* class action (*see* Section V(F), *supra*), "wrote to the [SDR] on June 14, 2017" concerning "'short-pay funds' that it claims 'represents payment[s that the CO-OP's] consumers submitted to Xerox for the 2014 coverage year that were less than that consumer's [*sic*] full premium payment[s which were] required to initiate transfer of the payment[s] to [the CO-OP].'" (3A.A.18 at 0461:2-8.) "Counsel for Xerox" further explained to the SDR that Silver State had instructed Xerox to remit the funds to carriers, like the CO-OP, so that the carriers could refund the consumers. (*Id.*

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at 0461:8-14.) Moreover, "Counsel for Xerox" informed the SDR that the CO-OP must also refund "other members for overpaid premiums that [the CO-OP] received from Xerox during the 2014 coverage year." (*Id.* at 0461:15-18.) Notably, when Greenberg, on behalf of the Receiver, disclosed these communications from "Counsel from Xerox" in the quarterly status reports, Greenberg failed to disclose the identity of the "Counsel for Xerox" who contacted the SDR. (*Id.* at 0461:1-18.)

In response to the letter from "Counsel for Xerox," Greenberg reported that the SDR had "asked for further clarification and documentation from Xerox" and was "evaluating the information." (*Id.* at 0461:13-14, 17-18.) However, Greenberg never again mentioned this correspondence from "Counsel for Xerox" or the funds to be returned to the CO-OP's members in any of the fourteen subsequent status reports filed over the course of the next three and half years. (3A.A.19; 3A.A.20; 3A.A.21; 4A.A.23; 5A.A.24; 5A.A.25; 5A.A.27; 6A.A.29; 6A.A.30; 6A.A.31; 7A.A.33; 10A.A.42; 13A.A.51; 13A.A.57.)

Tellingly, the correspondence from "Counsel for Xerox" was not attached to the Eighth Status Report. Thus, when Xerox's liability for the CO-OP's damages and demise came to light, UHH propounded discovery requests

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on the Receiver requesting communications between the CO-OP and Xerox which would have included this letter from "Counsel for Xerox." (9A.A.39 at 1705-1706.) While Greenberg, the Receiver, and the SDR, never produced this correspondence, (*id.*), they did produce the SDR's June 29, 2017 response to "Counsel for Xerox" requesting additional information regarding the "short-pay and overpayment refund amounts." (2A.A.15.) This response letter, ***addressed to Greenberg***, confirms that ***Greenberg*** is the "Counsel for Xerox" referenced in the Eighth Status Report ***filed by Greenberg on behalf of the Receiver***. (*Id.*; 3A.A.13 at 0461:1-18.)

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H. Greenberg Has Failed to Produce Any Evidence Demonstrating That Its Concurrent Representation of the Receiver, Valley, and Xerox Does Not Create Impermissible Conflicts of Interest.

Pursuant to the Receiver's obligation of transparency as a neutral and independent party, on June 16, 2020, UHH sent correspondence to Greenberg requesting an explanation as to why the Receiver has chosen not to pursue any claims against Xerox for the harm it caused the CO-OP. (9A.A.39 at 1721-1722.) Greenberg refused to provide a substantive response, claiming the information was protected by the attorney-client privilege and the work product

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doctrine, while also, contradictorily, claiming that UHH should seek this information "through the discovery process." (*Id.* at 1724.)

Therefore, in response, UHH propounded written discovery to the Receiver in a related action, (*see* Section V(J)(1), *infra*), to try to obtain information regarding any steps Greenberg may have taken to ameliorate its known conflicts. (9A.A.39 at 1726-1732.) Specifically, UHH propounded an interrogatory seeking information about any potential claims that the CO-OP had against Xerox which had been settled by the Receiver, the NDOI, or the CO-OP. (*Id.* at 1728:23-1729:2.) The Receiver ultimately confirmed that it had not settled any such claims and was not aware of the NDOI settling any similar claims. (*Id.* at 1729:3-10.)

Similarly, when asked to explain why the Receiver has not named Xerox as a defendant in any of the related asset-recovery actions, the Receiver again objected based on privilege and work product. (*Id.* at 1729:12-17.) However, the Receiver also stated that Xerox "had no direct contractual relationship with [the CO-OP]" and that "based on the merits and resources of the receivership, [the Receiver] elected to pursue those entities and individuals that were most

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directly responsible for [the CO-OP's damages, namely the [d]efendants [in the asset-recovery actions]." (*Id.* at 1729:20-1730:1.)[4]

Finally, UHH propounded requests for production on the Receiver seeking copies of engagement letters between the Receiver and Greenberg and conflict of interest waivers that Greenberg received from the CO-OP, Xerox, and Valley. (*Id.* at 1738:14-17, 1739:25-27, 1740:12-14, 1741:1-3.) The Receiver, via Greenberg, again refused to respond to these requests, objecting that the requests were irrelevant and sought privileged information or work product. (*Id* at 1739:18-28, 1740:1-11, 15-25, 1741:4-14.) Similarly, in opposition to the Motion to Disqualify, the Receiver and Greenberg failed to provide the Receivership Court with any engagement letters or conflict of interest waivers which would support their assertion that no conflicts of interest existed to warrant Greenberg's disqualification. (10A.A.45; 10A.A.46; 11A.A.47.)

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[4] Notably, this interrogatory response directly contradicted the Receiver's prior representation to the Receivership Court that "the Receiver does not have access to the legal resources necessary to evaluate the prosecution and defense of litigation," and that the Receiver needed Greenberg for the "evaluation and resolution of [the creditors'] claims, which may also include the pursuit of related counterclaims." (1A.A.10 at 0190:11-16.)

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I. Greenberg Has Earned Substantial Compensation as Counsel for the Receiver.

When Greenberg was appointed as counsel for the Receiver, the Receivership Court was concerned about Greenberg's "substantial hourly rates" depleting the Receivership Estate's assets and prejudicing the creditors. (Section V(E), *supra*.) The Receivership Court's concern was justified. Specifically, at the time the Motion to Disqualify was filed in October 2020,[5] Greenberg had already billed nearly $5 million in attorney's fees as counsel for the Receiver. (7P.A37 at 1378:18-1379:27; *see also* 2A.A.13 at 0281; 2A.A.16 at 0341-0347; 3A.A.18 at 0486-0499; 3A.A.19 at 0539-0542; 3A.A.20 at 0585-0589; 3A.A.21 at 0642-0644; 4A.A.23 at 0832-0836; 5A.A.24 at 0884-0886; 5A.A.26 at 0954-0970; 5A.A.27 at 1008-1018; 6A.A.29 at 1153-1160; 6A.A.30 at 1186-1188; 6A.A.31 at 1233-1245; 7A.A.33 at 1301-1307.) Since the filing of the Motion to Disqualify, Greenberg's fees now total $6,043,288.09.[6] (10A.A.42 at 1808-1815; 13A.A.51 at 2354-2370; 13A.A.57 at 2519-2526.) The amount of the fees is particularly concerning given that the Receiver

[5] These fees are based on Greenberg's invoices from January 2017 to May 2020.

[6] These fees are based on Greenberg's invoices through January 2021, which is the most recent invoice submitted to the Receivership Court with the Receiver's quarterly status reports.

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contends that the creditors' claims (exclusive of the federal government's claim for outstanding loans paid to the CO-OP) exceed $35 million (approximately $33 million in NRS 696B.420(1)(b) claims and approximately $2 million in NRS 696B.420(1)(c)-(l) claims), and the current cash assets of the Receivership Estate (as of February 28, 2021) are less than $4.5 million. (13A.A.51 at 2315:3-11, 2316:14-2317:2 & n.4, 2376, 2378; 13A.A.57 at 2462:17-19.)

J. The Receiver's Asset Recovery Lawsuits Filed by Greenberg.

Greenberg, on behalf of the Receiver, has filed several lawsuits allegedly designed to recover assets for the CO-OP's Receivership Estate. Xerox should be a substantial target defendant in each of these lawsuits. Despite the relevant allegations in each of these actions encompassing various issues for which Xerox was directly responsible, Xerox has not been named as a defendant in any of these actions due to Greenberg's conflict of interest as counsel for Xerox.

1. Milliman Lawsuit.

On August 25, 2017 — eight months after Greenberg's appointment as counsel for the Receiver — Greenberg, on behalf of the Receiver, filed *State of Nevada ex rel. Commissioner of Insurance, Barbara D. Richardson, in her official capacity as Receiver for Nevada Health CO-OP v. Milliman, Inc.*, No.

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A-17-760558-B, Eighth Judicial District Court, Clark County, Nevada ("Milliman Lawsuit"), against several of the CO-OP's former vendors, officers, and directors, including Nevada Health Solutions, LLC. (2A.A.17 at 0357:1-4.) Greenberg filed an Amended Complaint on September 14, 2018, adding Unite Here Health as a defendant. (4A.A.22.)

One of the primary issues in the Milliman Lawsuit is who or what caused the CO-OP's insolvency and ultimate demise. (*Id.* at 0652:7-9.) Despite the fact that Greenberg failed to name Xerox (its client) as a defendant in the Milliman Action, the named defendants' experts (including UHH's experts) have unanimously opined that Xerox was primarily to blame for the CO-OP's problems. (*See, e.g.*, 9A.A.39 at 1598-1601, 1618-1619, 1655; 12A.A.48 at 2143-2144, 2158-2161, 2169-2171, 2177, 2187-2188, 2193.) Specifically, as one expert stated: "Despite public information and private discussions regarding the detrimental impact of Xerox's failure in its administration of the [Xerox] Exchange, [the Receiver and her expert witness] fail[] to acknowledge Xerox's ***catastrophic impact on CO-OP operations*** and carriers, in general." (12A.A.48 at 2158 (emphasis added).) Further, this expert opined that "[t]o attribute the failure of [the CO-OP] to [UHH], without regard for the CO-OP's and Xerox's evident failures, is an oversimplification of the facts, and the

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context in which they occurred. . . . ***[I]t is nothing more than a naked attempt to assign blame where it does not belong***." (*Id.* at 2161 (emphasis added).)

Moreover, one of the experts for another defendant in the Milliman Lawsuit opined:

> Nevada's failure to have a working information technology (IT) platform for its state-run health insurance marketplace [the Xerox Exchange] in 2013 and 2014 had ***disastrous consequences for a start-up like [the CO-OP]*** that was, under law, required to generate "substantially all" of its business from that market. The ***non-working website was likely the primary reason [the CO-OP] was not able to reach its enrollment targets***.

(*Id.* at 2171 (emphasis added).)

2. The Silver State Lawsuit.

On June 5, 2020, Greenberg, on behalf of the Receiver, filed *State of Nevada ex rel. Commissioner of Insurance, Barbara D. Richardson, in her official capacity as Receiver for Nevada Health CO-OP v. Silver State Health Insurance Exchange*, No. A-20-816161-C, Eighth Judicial District Court, Clark County, Nevada ("Silver State Lawsuit"). (7A.A.32.) The Receiver alleges that Silver State owes the CO-OP approximately $510,000.00 in unpaid insurance premiums. (*Id.* at 1254:15-17, 1254:24-1255:2.) In response, Silver State has alleged that ***Xerox*** is the entity that retained the insurance premiums at

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issue in that case. (7A.A.36 at 1359:24-27.) Despite this allegation and the significant overlap in Silver State's and Xerox's past misconduct, Greenberg again declined to sue Xerox in the Silver State Lawsuit.

3. WellHealth Lawsuit.

On July 16, 2020, Greenberg, on behalf of the Receiver, also filed *State of Nevada ex rel. Commissioner of Insurance, Barbara D. Richardson, in her official capacity as Receiver for Nevada Health CO-OP v. WellHealth Medical Associates (Volker), PLLC dba WellHealth Quality Care et al.*, No. A-20-818118-C, Eighth Judicial District Court, Clark County, Nevada ("WellHealth Lawsuit"). (7A.A.34.) The allegations in this action significantly overlap with the allegations in the Milliman and Silver State Lawsuits, yet Greenberg, again, failed to sue Xerox in the WellHealth Lawsuit. (*Id.* at 1313:17-20.)

K. Motion to Disqualify Greenberg as Counsel for the Receiver.

UHH filed the Motion to Disqualify on October 8, 2020. (7A.A.37.) UHH contended that Xerox should have been a primary target of Greenberg's investigation of individuals and entities with potential liability to the CO-OP; yet, Greenberg failed to bring any claims against Xerox due to its concurrent representation of Xerox in related litigation and administrative actions. (*Id.* at 1365:1-7.) UHH also contended that Greenberg's representation of Valley, a

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significant creditor of the CO-OP Receivership Estate, "rais[ed] the specter of preferential treatment in favor of Valley and to the detriment of all the remaining creditors who are not fortunate enough to also be represented by Greenberg." (*Id.* at 1365:10-13.) Because Greenberg, the Receiver, and the SDR failed to disclose to the Receivership Court these significant and known conflicts at the time of Greenberg's appointment as the Receiver's counsel — or at any time thereafter — UHH sought disqualification of Greenberg as counsel for the Receiver, as well as disgorgement of all of the attorneys' fees and costs paid to Greenberg from the assets of the Receivership Estate (approximately $5 million at the time of the filing of the motion). (*Id.* at 1365:15-19.)

In Opposition to the Motion to Disqualify, Greenberg, the Receiver, and the SDR asserted, for the first time, and ***in direct contradiction with the representations made to the Receivership Court at the time of Greenberg's appointment***, that:

> [Greenberg] was retained by the Receiver for the limited purpose of pursuing specific claims on the Receiver's behalf. Before [Greenberg] was retained, it fully advised the Receiver that [Greenberg] had a potential conflict with pursuing any claim against [Xerox]. The Receiver consequently did not retain [Greenberg] to evaluate or pursue any such claims.

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> Instead, the Receiver sought and received permission to also retain conflicts counsel, James Whitmire of Santoro Whitmire, Ltd., to handle any matters that were outside the scope of [Greenberg's] retention due to potential conflicts. Since its engagement, [Greenberg] had no involvement whatsoever in the Receiver's evaluation of its potential claims against Xerox. Similarly, the scope of [Greenberg's] representation of the Receiver did not include defending or administering the undisputed claims of members of [Valley] against the receivership or allocating assets among creditors like Valley.

(10A.A.45 at 1839:14-25; *see also* 1A.A.10 at 0190:11-16.)

However, Greenberg and the Receiver produced no engagement letters, conflict of interest waivers, billing invoices, or other correspondence to support these new (self-serving) assertions, not even for *in camera* review. Moreover, based on the Receiver's quarterly status reports to the Receivership Court, so-called conflicts counsel (Santoro Whitmire) has billed less than $2,000.00 to the Receivership Estate since January 2017, despite the abundance of issues relating to Xerox that have arisen in the asset recovery lawsuits. (2A.A.13 at 0280; 2A.A.16 at 0340.) Further, the Attorney General's Office — which represented the Receiver prior to Greenberg and filed the motion for the approval of the appointment of Greenberg as the Receiver's counsel — recently stated, in the Silver State Lawsuit, that it only discovered Greenberg's prior

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representation of Xerox ***after*** reviewing UHH's Motion to Disqualify. (10A.A.44 at 1833:9-25 & n.1, 1836:9-14.) In other words, the Receiver, SDR, and Greenberg ***concealed Greenberg's known conflicts of interest from the Attorney General, who was representing the Receiver at the time***.

Ultimately, on January 15, 2021, the Receivership Court entered an order denying the Motion to Disqualify. (13A.A.52.) Despite a wealth of authority disqualifying counsel for fiduciaries, like receivers, who fail to disclose actual or potential conflicts of interest, (7A.A.37 at 1381:16-1382:7, 1382:23-1385:17, 1386:6-14, 1387:7-1388:28; 1389:18-1390:2), the Receivership Court denied the Motion to Disqualify because of a lack of Nevada authorities or rules requiring disclosure of such known conflicts. (13A.A.52 at 2384:17-20 ("[UHH] have not been able to point to any binding authority that mandates the Receiver and her counsel, [Greenberg], disclose all possible conflicts to the Court. Because there is no explicit rule requiring disclosure, the Court cannot disqualify [Greenberg] on that basis.").) The Receivership Court also created a new requirement that a conflict had to be "substantial enough" to warrant disqualification, and it found that the Valley and Xerox conflicts were not "clear and substantial enough possible conflict[s] to justify disqualifying [Greenberg] as counsel in this Receivership matter." (*Id.* at 2384:21-22.)

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Finally, the Receivership Court denied the Motion to Disqualify because there were "no related matters where the CO-OP [wa]s adverse to Xerox," and UHH was "free to attempt to bring in Xerox as a third-party defendant and seek whatever relief they believe they are entitled to with the Judges overseeing those matters." (*Id.* at 2384:22-2385:1.)

Shortly after entry of the Order Denying Disqualification, the Receiver sought and received the Receivership Court's approval to retain the law firm of Lewis & Roca as "outside conflicts counsel" in the place and stead of Santoro Whitmire. (13A.A.55 at 2423:15-19; 13A.A.56 at 2441.) The Receiver vaguely and ambiguously explained the need to change conflicts counsel as follows: "Previously approved conflicts counsel for the CO-OP has declined further representation as additional parties added to related cases has [*sic*] caused such counsel to reconsider its ability or willingness to represent the CO-OP." (13A.A.55 at 2423:12-14.) However, it is unknown what caused Santoro Whitmire to "reconsider" its willingness to serve as conflicts counsel, as no additional parties had been added to any of the related actions at the time of its withdrawal.

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L. The Receiver and Greenberg Raised Additional Funds to Pay Its Attorneys' Fees to the Potential Detriment of the CO-OP's Creditors.

In April 2017, in the Sixth Status Report filed by the Receiver in the Receivership Court — which is also the first Status Report drafted by Greenberg as counsel for the Receiver — it was reported that the unrestricted cash assets of the Receivership Estate were $9,136,347.00. (2A.A.13 at 0251:20-21.) Just two and half years later, in October 2019, the Receiver reported that the unrestricted cash assets of the Receivership Estate were only $322,530.00. (6A.A.29 at 1123:23-24.) At that time, most of the cash assets appear to have been spent on the fees incurred by the SDR ($5,944,730.26); Palomar Financial, LC (a financial firm affiliated with the SDR) ($778,583.35); and Greenberg ($3,787,292.26) — as the cash flow analysis included with each status report does not include any payments to creditors of the Receivership Estate until the Twentieth Status Report in October 2020. (1A.A.9 at 0139-0187; 1A.A.11 at 0215-0232; 2A.A.13 at 0256-0278, 0281; 2A.A.16 at 0308-0338, 0341-0347; 3A.A.18 at 0466-0489; 3A.A.19 at 0513-0542; 3A.A.20 at 0570-0589; 3A.A.21 at 0614-0644; 4A.A.23 at 0786-0836; 5A.A.24 at 0864-0866; 5A.A.26 at 0912-0952, 0954-0970; 5A.A.27 at 0987-1018; 6A.A.29 at 1128-1160; 10A.A.42 at 1819.)

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Consequently, in desperate need of cash to continue paying the SDR, the SDR's financial affiliate, Greenberg, and, eventually, creditor claims, in September 2019, the Receiver filed a motion for leave to sell a $43 million federal receivable for a mere $10 million. (6A.A.28.) The Receiver claimed that the sale was necessary due to the "great uncertainty" that the CO-OP's position on the recoverability of this receivable would prevail in an appeal to the United States Supreme Court filed in an action brought by another insurer seeking to enforce its rights to the same type of federal receivable. (*Id.* at 1024:3-20.) However, approximately three months before the sale of the CO-OP's receivable, the United States Supreme Court had granted certiorari to address this issue. (5A.A.27 at 0982:6-9.) Moreover, approximately seven months after the Receiver sold the CO-OP's receivable, the United States Supreme Court ruled, ***in an 8-1 decision***, in favor of insurers and found that the federal government had an obligation to pay this type of receivable to insurers. *Maine Community Health Options v. United States*, 140 S. Ct. 1308 (2020). As a result, the company which purchased the CO-OP's federal receivable is likely to have gained a $33 million windfall to the detriment of the CO-OP's creditors. Although hindsight is 20/20, and no one could be sure that the Supreme Court would rule in favor of the insurers, the only reason that the Receiver, the SDR,

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and Greenberg were faced with the need to sell the receivable was because they exhausted the CO-OP's existing assets on their own substantial fees and expenses.

The potential harm to the creditors is compounded by the Receiver's use of the $10 million sale proceeds to date. From November 30, 2019, when the $10 million sale proceeds were first included in the Receivership Estate's cash flow analysis to February 28, 2021, the CO-OP's unrestricted cash assets have already decreased from $10,114,363.00 to $4,457,059.00. (6A.A.30 at 1178:10-11, 1196; 13A.A.57 at 2462:17-19.) However, of the $10 million in proceeds from the sale of the federal receivable, less than $1 million ($903,631.00) has been used to pay the claims of providers. (10A.A.42 at 1819; 13A.A.51 at 2378; 13A.A.57 at 2533.) The remainder of the funds appears to have been spent primarily on professional services fees, presumably for Greenberg, the SDR, and the SDR's financial services agent.

Specifically, in four months (between August 2019 and November 2019), the amount of cash spent on professional services fees increased $3,812,345.00 — far greater than that of the professional services invoices attached to the Eighteenth Status Report for the period. (6A.A.30 at 1196; 6A.A.31 at 1216-1245, 1250.) Presumably, a large percentage of these funds were used to pay

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for prior, outstanding invoices for Greenberg, the SDR, and the SDR's financial services agent that remained unpaid as cash assets dwindled. Moreover, the professional services invoices included with the Seventeenth Status Report (when the $10 million sale proceeds were first included in the CO-OP's cash analysis) through the most recent Twenty-Second Status Report (approximately September 2019 to January 2021) total $691,826.05 for the SDR, $208,395.50 for the SDR's financial services affiliate, and $2,241,035.83 for Greenberg. (6A.A.30 at 1183-1188, 1196; 6A.A.31, at 1216-1245; 7A.A.33 at 1273-1307; 10A.A.42 at 1792-1815; 13A.A.51 at 2333-2370; 13A.A.57 at 2466-2526.) Thus, a significant portion of the assets of the Receivership Estate continue to be spent on conflicted counsel (Greenberg) to the detriment of the CO-OP's creditors.[7]

M. The Continuing Impact of Greenberg's Conflicts of Interest on the Asset Recovery Lawsuits.

On October 15, 2020, prior to the Receivership Court's ruling on the Motion to Disqualify, UHH timely filed a Motion for Leave to File a Third-Party Complaint against Xerox and Silver State for contribution in the Milliman

[7] Moreover, as set forth in Section V(K), supra, the Receiver recently hired another law firm — due to Greenberg's undisclosed conflicts of interest — with significant hourly rates (e.g., $850 per hour for the lead partner) that will further exacerbate the CO-OP's dwindling assets. (13A.A.55 at 2423:10-19, 2432.)

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Lawsuit. (10A.A.41 at 1761:10-16.) UHH sought to file third-party claims rather than commence a separate lawsuit in order to promote judicial economy and avoid inconsistent judgments. (*Id.* at 1762:5-6.) UHH also timely filed, on October 19, 2020, a Motion to Consolidate the Silver State Lawsuit with the Milliman Lawsuit because the Receiver is seeking the exact same damages for the exact same alleged injury in each action. (10A.A.43 at 1822:3-7.) Specifically, the Receiver is seeking damages from both UHH and from Silver State for uncollected insurance premiums in the amount of $510,651.27. (*Id.*) Thus, in order to prevent the Receiver from obtaining a significant windfall through a double recovery, and in order to avoid inconsistent judgments, UHH moved to consolidate the two actions. (*Id.* at 1822:7-11.)

On May 26, 2021, following several months of delay due to the Receiver's need to retain a new law firm as "conflicts counsel," the District Court denied both the Motion for Leave to File a Third-Party Complaint and the Motion to Consolidate. (13A.A.58; *see also* 13A.A.55.) Despite finding that UHH's Motion for Leave to File a Third-Party Complaint "was timely and not the result of dilatory conduct," the Court was concerned that "impleader of a third party based on contribution claims would unduly complicate" the Milliman Lawsuit by "injecting tangential issues such as ***potential conflicts***

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resulting in the disqualification of [P]laintiff's counsel and impacting [P]laintiff's choice of counsel in the pending matter, potentially prejudicing the [P]laintiff." (13A.A.58 at 2538:16-19, 2538:25-2539:2 (emphasis added).) The Motion to Consolidate was denied for similar reasons. (*Id.* at 2539:14-15.) Thus, the District Court denied UHH leave to allege third-party claims against Xerox and the Exchange because the addition of Xerox and the Exchange in the Milliman Lawsuit would prejudice the Receiver by exposing Greenberg's undisclosed conflicts of interest and necessitating its disqualification.

VI. SUMMARY OF THE ARGUMENT

Greenberg's representation of the CO-OP's Receiver is marred with disabling conflicts of interest which have caused Greenberg to advance and/or pursue interests directly adverse to those of the Receivership Estate and the vast majority of the CO-OP's creditors, including UHH. During the period that Greenberg had the obligation to investigate all potential sources of assets for the Receivership Estate and to initiate litigation against various defendants who were each responsible for the CO-OP's demise or were otherwise obligated to the CO-OP, Greenberg was concurrently representing Xerox (a significant target defendant) in related litigation and administrative actions. Unsurprisingly, Greenberg declined to investigate and sue its own client,

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thereby eliminating a significant source of recovery for the Receivership Estate and its creditors.

Furthermore, prior to Greenberg's appointment as counsel for the Receiver, Greenberg was also representing one of the CO-OP's biggest creditors, Valley, in the delinquency proceeding. The fact that Greenberg owed fiduciary duties to a significant creditor of the CO-OP raised the specter of preferential treatment in favor of Valley and to the detriment of all the remaining creditors.

Greenberg had a fiduciary obligation to fully disclose both of these disabling conflicts of interest to both (i) the Receiver's then current counsel — the Attorney General, and (ii) more importantly, the Receivership Court, at the time it was being put forth for appointment as counsel for Receiver. Greenberg not only failed to do so, but it actively worked to conceal these conflicts from the Receivership Court by concealing relevant information from the quarterly status reports it filed with the Receivership Court.

Greenberg alleges that it was not required to make any disclosures to the Receivership Court because no conflicts of interest existed — it had allegedly been retained by the Receiver for only a limited purpose that did not conflict with its representation of Valley or Xerox. Not only is such a limited

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engagement virtually impossible in the face of ongoing, direct conflicts like this, but Greenberg has never produced any engagement letters or conflict of interest waivers to support its assertion. Moreover, the billing invoices of the alleged "conflicts counsel" purportedly retained by the Receiver to analyze whether there were any potential claims against Xerox do not support the assertion that any such analysis was actually conducted. More importantly, any attempt to cure such conflicts does not excuse Greenberg from its fiduciary obligation to inform the Receivership Court of the conflicts of interest. Only the court — not conflicted counsel — is qualified to determine if conflicts of interest exist and if sufficient actions have been taken to cure such conflicts.

Greenberg failed to comply with its duty to fully disclose this information, and its impermissible conduct has tainted the legitimacy of the delinquency proceeding and the related asset recovery actions. Given the insufficient assets to satisfy the creditors' claims, none of the creditors can be assured of a lack of preferential treatment of Valley and its claim. Creditors similarly cannot trust that all avenues of asset recovery have been explored and pursued, given that no claims have been alleged against a significant target defendant like Xerox. Further, the entities and persons named as defendants in the asset recovery lawsuits could be severely prejudiced if they are held liable

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for the harm caused by Xerox merely because conflicted counsel prevented the Receiver from pursuing claims against Xerox. In fact, in the Milliman Lawsuit, UHH is now prevented from bringing third-party claims against Xerox or Silver State because the District Court has held that Xerox's participation in the case will require Greenberg's disqualification. UHH is also prevented from consolidating the Receiver's claim against Silver State in the Silver State Lawsuit with the Milliman Lawsuit, despite the fact that the same damages are being sought in both actions against two different defendants, because Silver State has alleged, in the Silver State Lawsuit, that Xerox is the true party liable for the damages — therefore, consolidation would also result in Xerox's participation in the consolidated action and lead to Greenberg's disqualification.

Given Greenberg's failure to satisfy its fiduciary obligation to disclose its conflicts of interest to the Receivership Court at the time of its appointment, and the prejudice its conflicts have caused UHH and all of the other creditors and defendants in the asset recovery lawsuits, Greenberg should be disqualified as counsel for the Receiver.

VII. STANDARD OF REVIEW

"Although the district court has broad discretion in attorney disqualification matters, when the facts are undisputed and the appropriate

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standard for disqualification is based on interpretation of a disciplinary rule, *de novo* review applies." *State ex rel. Cannizzaro v. First Jud. Dist. Ct. ex rel. Cnty. of Carson City*, 136 Nev. Adv. Op. 34, 466 P.3d 529, 531 (2020) (citations omitted). Stated differently, the appropriate standard of review for attorney disqualification is "abuse of discretion, with the underlying factual findings reviewed for clear error and the interpretation of the relevant rules of attorney conduct reviewed *de novo*." *Id*. (quoting *Dynamic 3D Geosolutions LLC v. Schlumberger Ltd.*, 837 F.3d 1280, 1284 (Fed. Cir. 2016)).

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VIII. ARGUMENT

A. Legal Standard for Disqualification of Counsel.

The Court has "broad discretion in determining whether disqualification is required in a particular case." *Brown v. Eighth Jud. Dist. Ct. ex rel. Cnty. of Clark*, 116 Nev. 1200, 1205, 14 P.3d 1266, 1269 (2000). Under Nevada law, a disqualification analysis is two-fold: first, the court must find that there is a reasonable possibility that opposing counsel committed "some specifically identifiable impropriety"; and, second, the court must find that "the likelihood of public suspicion or obloquy outweighs the social interests which will be served by [opposing counsel]'s continued participation in [the matter]." *Id.* at

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1205, 14 P.3d at 1270. ***Any doubt must be resolved "in favor of disqualification."*** *Id.* (emphasis added).

As set forth in detail below, Greenberg committed a "specifically identifiable impropriety" by agreeing to represent the CO-OP's Receiver while also concurrently representing one of the CO-OP's largest creditors (Valley), as well as a significant target defendant (Xerox) for the asset recovery lawsuits for the CO-OP's Receivership Estate. Greenberg also engaged in a specifically identifiable impropriety by failing to disclose, and then actively concealing, its conflicts of interest to the Receivership Court.

There is also a substantial likelihood of "public suspicion or obloquy" caused by Greenberg's actions which significantly outweighs any social interests in Greenberg's continued participation as counsel for the Receiver. Specifically, Greenberg's undisclosed attempt to represent every side of the dispute in this case (neutral receiver, interested creditor, and substantial target defendant for asset recovery purposes), while earning more than $6 million in fees and costs from a Receivership Estate with limited cash assets — where a majority of the CO-OP's creditors will never receive any payments — raises great suspicion and concern as to whether the Receiver and her counsel are acting in the best interests of the Receivership Estate and its creditors. (1A.A.1

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at 0005; 1A.A.7; 1A.A.10; 2A.A.13 at 0281; 2A.A.15; 2A.A.16 at 0341-0347; 3A.A.18 at 0486-0489; 3A.A.19 at 0539-0542; 3A.A.20 at 0585-0589; 3A.A.21 at 0642-0644; 4A.A.23 at 0832-0836; 5A.A.24 at 0884-0886; 5A.A.26 at 0954-0970; 5A.A.27 at 1008-1018; 6A.A.29 at 1153-1160; 6A.A.30 at 1186-1188; 6A.A.31 at 1233-1245; 7A.A.33 at 1301-1307; 7A.A.37 at 1378:18-1379:27; 8A.A.38 at 1452, 1459, 1542-1543, 1554; 9A.A.39 at 1598-1601, 1618-1619, 1655, 1674-1675, 1692:9-10; 10A.A.42 at 1803-1815; 12A.A.48 at 2143-2144, 2158-2161, 2169-2171, 2177, 2188-2189, 2193; 13 A.A.51 at 2315:3-11, 2316:14-2317:2 & n.4, 2376, 2378, 2354-2370; 13A.A.57 at 2462:17-19, 2519-2526.) Under no set of facts can this public suspicion of impropriety be outweighed by the Receiver's interest in continued representation by Greenberg — particularly given the fact that Greenberg can be made to disgorge the $6 million in fees and costs it has received to date. Therefore, disqualification is warranted, if not mandated.[8]

[8] As set forth in Section VIII(B), *infra*, the unique conflicts of interest in this case are generally analyzed under receivership and/or bankruptcy law as opposed to the Rules of Professional Conduct. However, it is clear that Greenberg's concurrent representation of the Receivership Estate, Xerox, and Valley — all adverse parties — would be a specifically identifiable impropriety and would be precluded under Nevada Rules of Professional Conduct 1.7(a)(1) and (a)(2), and would be unwaivable pursuant to Nevada Rule of Professional Conduct 1.7(b)(3). Even if Greenberg's representation of Xerox or Valley ended at some point, Greenberg would still suffer from a conflict of interest pursuant to Nevada Rule of Professional Conduct 1.7(a)(2) and 1.9(a).

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B. The Failure to Disclose Greenberg's Conflicts of Interest (and Its Purported Attempts to Cure Such Conflicts) Warrants Greenberg's Disqualification.

1. Fiduciaries, Such as Receivers and Their Counsel, Have Affirmative Obligations to Disclose Pertinent Information, Including Conflicts of Interest.

A receiver is considered to be an "officer of the court." *Bowler v. Leonard*, 70 Nev. 370, 383, 269 P.2d 833, 839 (1954). It is "a neutral party appointed by the court to take possession of property and preserve its value for the benefit of the person or entity subsequently determined to be entitled to the property." *Anes v. Crown P'ship, Inc*., 113 Nev. 195, 199, 932 P.2d 1067, 1069 (1997). "[The receiver] is subject to the court's directions and orders and in the discharge of his official duties is entitled to apply to the court for instructions." *Jones v. Free*, 83 Nev. 31, 37, 422 P.2d 551, 554 (1967) (internal quotation omitted). Finally, "a receiver must act for the benefit of all persons interested in the property." *Fullerton v. Second Jud. Dist. Ct. ex rel. Cnty. of Washoe*, 111 Nev. 391, 400, 892 P.2d 935, 941 (1995). Thus, "a [r]eceiver owes [a] fiduciary duty to all the parties in interest, including the creditors . . ., and is under the duty to act impartially toward, and protect the rights of, all parties." *Hilti, Inc. v. HML Dev. Corp.*, No. 97271, 2007 Mass. Super. LEXIS 66 at *55-56 (Mass. Super. Ct. Feb. 5, 2007) (internal quotation omitted).

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Similarly, special deputy receivers, who are often appointed to stand in the shoes of the receiver, also owe fiduciary duties to all parties interested in the receivership. *McPherson v. U.S. Physicians Mut. Risk Retention Group*, 99 S.W.3d 462, 468 (Mo. Ct. App. 2003) (holding that because of the SDR's broad powers of the receivership estate, the SDR is a "fiduciary of all parties interested in the receivership"); *Pulitzer Publishing Co. v. Transit Cas. Co.*, 43 S.W.3d 293, 303 (Mo. 2001) (holding that an SDR is subject "to all of the duties imposed on the statutory receiver"). Furthermore, the ***receiver's counsel*** is also a fiduciary and must also be neutral and impartial. *KeyBank Nat'l Ass'n v. Michael*, 737 N.E.2d 834, 852 (Ind. Ct. App. 2000) ("[A]n attorney acting as counsel for the receiver should be held to the same standard of impartiality as that for the receiver."); *In re Coastal Equities, Inc.*, 39 B.R. 304, 309 (Bankr. S.D. Cal. 1984) ("A debtor-in-possession, as well as its counsel, owe undivided loyalty to the estate."); *McPherson*, 99 S.W.3d at 468 (confirming that an insurance receiver's counsel is also a fiduciary to the court).

Although few receivership courts have addressed the type of conflicts of interest at issue here, the United States District Court for the Eastern District of Pennsylvania addressed one of these conflicts in great detail. *See CFTC v. Eustace*, Nos. 05-2973, 06-1944, 2007 U.S. Dist. LEXIS 33137, at *1 (E.D. Pa.

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May 3, 2007). In *Eustace*, one of the defendants sued by the receiver — Man Financial, Inc. — argued that the receiver had a conflict of interest due to its preexisting attorney-client relationship with affiliated entities of a potential target of the receivership estate (UBS Cayman), and that disqualification was warranted. *Id.* at *4-8, 13. The CFTC (Commodity Futures Trading Commission), which originally sought the receivership, agreed, stating:

> [T]he Receiver is in a position similar to a bankruptcy trustee and has the duty to avoid even the appearance of possible impropriety, unfairness, or partiality. ***As such, the Receiver and any counsel employed by him were obligated to fully disclose to the Court his and his firm's prior relationships with certain UBS entities, which the CTFC characterizes as a potential conflict of interest***, and their failure to do so created an appearance of impropriety affecting the integrity of these proceedings.

Id. at *13, 19 (emphasis added). The court agreed, concluding that:

> [T]he previously undisclosed relationship between the Receiver and UBS entities other than UBS Cayman is not something that can be ignored. ***The continued prosecution of the case by a receiver with a history of UBS relationships cannot be squared with the goal of concluding this case free of any doubt as to whether***

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> ***these relationships have tainted the proceedings or prejudiced another party***.

Id. at *37 (emphasis added).[9]

Therefore, it is clear that fiduciaries (such as a receiver and/or a special deputy receiver and their appointed counsel) have mandatory, ongoing obligations to fully disclose material information to the receivership court. The only manner in which the court can supervise its fiduciaries and approve various actions is if all pertinent information is disclosed. *See Crites, Inc. v. Prudential Ins. Co. of Am.*, 322 U.S. 408, 414-15 (1944) (holding that "[t]he court, as well as all the interested parties, had the right to expect that its officers would not . . . fail to reveal any pertinent information or use their official position for their own profit or to further the interests of themselves or any associates"). It would be illogical to conclude that a fiduciary's disclosure

[9] Greenberg has previously contended that *Eustace* is inapposite because the receiver's counsel was permitted to remain as counsel of record. (10A.A.45 at 1851:22-1852:8.) Greenberg conveniently misses the point. In *Eustace*, counsel was only permitted to remain in that case because it had not represented the UBS entity at issue in the receivership, and, furthermore, no potential conflict of interest would exist once the receiver was no longer a client of the law firm. *Eustace*, 2007 U.S. Dist. LEXIS 33137, at *16, 40 (finding no conflict after "careful review of Rule 1.7 and comment 34," addressing affiliated and subsidiary organization representation). Here, Greenberg represented the *exact same Xerox entity* in the class actions and the administrative matter before the NDOI as the Xerox entity at issue in the Milliman Lawsuit and the Silver State Lawsuit. Thus, Greenberg not only has a full disclosure issue like that discussed in *Eustace*, but it also has a clear conflict of interest with no refuge in Comment 34 of Rule 1.7.

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obligation to the appointing court does not include actual or potential conflicts of interest which are undoubtedly at issue at the time the court is considering potential appointment of counsel.

2. Insurance Receiverships Are Akin to Bankruptcy Proceedings and Should Be Analyzed Similarly With Regard to the Disclosure of Actual and Potential Conflicts of Interest.

Additionally, compelling support for a receiver's, a special deputy receiver's, and their counsel's obligation to fully disclose potential and actual conflicts of interest to the receivership court at the time of their appointment can be found in the analogous bankruptcy arena. It is well recognized that "[a] state insurance receivership proceeding is similar to a federal bankruptcy proceeding: both the bankruptcy trustee and the Receiver (or SDR) have fiduciary obligations to the estates they are administering." *McPherson v. U.S. Physicians Mut. Risk Retention Group*, 99 S.W.3d 462, 483 (Mo. Ct. App. 2003); *see also Jo Ann Howard & Assocs., P.C. v. Cassity*, No. 4:09CV01252 ERW, 2012 U.S. Dist. LEXIS 52178, at *15-16 (E.D. Mo. Apr. 13, 2012). In fact, the only reason that insurance companies do not file for bankruptcy protection is because "federal bankruptcy laws are not available to insurance companies." *Smith v. Farm & Home Life Ins. Co.*, 506 S.E.2d 104, 107 (Ga.

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1998); *see also* 9 NEW APPLEMAN ON INSURANCE LAW LIBRARY EDITION § 96.01 ("Section 109(b) of the Bankruptcy Code expressly exempts a domestic insurance company from being a debtor under the Bankruptcy Code."). As a result, courts dealing with insurance receivership issues will often look to federal bankruptcy authority for guidance. *See, e.g., Kreidler v. Cascade Nat'l Ins. Co.*, 329 P.3d 928, 933 (Wash. Ct. App. 2014); *see also Jo Ann Howard & Assocs., P.C.*, 2012 U.S. Dist. LEXIS 52178 at *13-16.

With regard to the disclosure of conflicts of interest, bankruptcy authority could not be any clearer:

> In situations where counsel is aware of apparent conflicts which counsel believes are outweighed by other factors, ***the conflicts must be disclosed. The court then can exercise its independent judgment***. The decision concerning the propriety of employment ***should not be left exclusively with counsel***, whose judgment may be clouded by the benefits of the potential employment.

See, e.g., In re BH & P, Inc., 119 B.R. 35, 44 (D.N.J. 1990) (emphasis added) (internal quotation omitted). Such disclosure is required by counsel's fiduciary obligations to the Court. *In re Futuronics Corp.*, 655 F.2d 463, 470 (2d Cir. 1981) (reiterating that "the duty of counsel for the debtor in a bankruptcy proceeding to disclose fully to the court all connections that may exist between

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counsel and the debtor, the creditors, any party in interest, and their respective attorneys arises not solely by reason of the bankruptcy rules, but also is founded upon 'the fiduciary obligation owed by counsel for the debtor to the bankruptcy court'") (quoting *In re Arlan's Dep't Stores, Inc.*, 615 F.2d 925, 937 (2d Cir. 1979)); *see also In re Leslie Fay Cos.*, 175 B.R. 525, 537-38 (Bankr. S.D.N.Y. 1994) (holding that the debtor's counsel "was mandated to reveal any connections which might cast any doubt on the wisdom of its retention and leave for the court the determination of whether a conflict existed"); *In re Townson*, No. 12-03027-TOM-7, 2013 Bankr. LEXIS 853, at *20 (Bankr. N.D. Ala. Mar. 7, 2013) (holding, where counsel represented both the bankruptcy trustee and a defendant in an adversary proceeding, that "[i]f [counsel] believed it would have no conflicts in representing both clients, it is difficult to see how [counsel] would not disclose these connections so that the [c]ourt and other interested parties could examine the relationships and conclude for themselves that the representation of both is no cause for concern").

Thus, while the Receivership Court may have been correct that there is not an explicit Nevada rule or statute which addresses the disclosure of conflicts of interest in a receivership, (13A.A.52 at 2384:17-20), and this Court has not yet addressed this issue directly, nonetheless, the Receivership Court abused its

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discretion in ignoring the clear, undisputed, and overwhelming weight of authority requiring receivers and their counsel (or the analogous bankruptcy trustees and their counsel) to fully disclose all conflicts of interest (actual or potential) to the appointing court at the time of the appointment. Based on the fiduciary, receivership, and bankruptcy precedent set forth above, the Receiver, the SDR, and Greenberg had an unmistakable duty to fully disclose Greenberg's conflicts of interest so that the Receivership Court could exercise its independent judgment.

3. The Receiver's, the SDR's, and Greenberg's Failure to Disclose Greenberg's Conflicts of Interest Warrants Greenberg's Disqualification.

Not only is disclosure of conflicts of interest mandatory, the failure to disclose them is grounds for disqualification in and of itself. *See In re Envirodyne Indus., Inc.*, 150 B.R. 1008, 1021 (Bankr. N.D. Ill. 1993) (holding that "[f]ailure to abide by the disclosure requirements is enough to disqualify a professional and deny compensation, regardless of whether the undisclosed connections were material or *de minimis*"); *In re S. Kitchens, Inc.*, 216 B.R. 819, 830 (Bankr. D. Minn. 1998) (holding that a bankruptcy court has the discretion to "disqualify counsel[] or deny compensation[] as a sanction" for the failure to disclose actual or potential conflicts of interest to the court).

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The Receiver, the SDR, and Greenberg never made any conflict of interest disclosures to the Receivership Court (or the Attorney General) with respect to either Xerox or Valley, despite their ***admitted knowledge of the existence of these conflicts*** and their purported attempts to cure them. (10A.A.45 at 1839:14-18; 10A.A.46 at 1868:25-1869:26; 12A.A.49 at 2256:8-2259:3.) If, as Greenberg asserts, there were no conflicts to disclose because it was retained only for a "limited purpose" that would not involve evaluating or pursuing any claims against Xerox, or defending or administering Valley's claim against the Receivership Estate — and Santoro Whitmire was retained to "handle any matters that were outside the scope of [Greenberg's] retention" — then why was the Receiver's counsel at the time (the Attorney General's office) completely unaware of Greenberg's conflicts of interest? (10A.A.44 at 1833:9-13, 1836:9-14; 10A.A.45 at 1839:14-25.)

Similarly, if the Receiver and the SDR were tasked with evaluating (i) potential claims against Xerox, and (ii) Valley's claim against the Receivership Estate (as they now claim), why did the Attorney General's office represent to the Receivership Court that "the Receiver d[id] not have access to the legal resources necessary to evaluate the prosecution and defense of litigation," and that the "Receiver need[ed] immediate assistance of legal counsel and

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consulting firms with specialized expertise for the evaluation and resolution of [the creditors'] claims, which may also include the pursuit of related counterclaims"? (1A.A.10 at 0190:11-16; *see also* 9A.A.39 at 1729:20-1730:1 (stating that the Receiver made the decision as to which entities and individuals to pursue for the CO-OP's damages); 10A.A.46 at 1868:3-10 (discussing how the SDR evaluated the potential claims and chose which claims to pursue in the best interests of the receivership).) Finally, if no conflicts of interest existed, why did Greenberg actively conceal its representation of Xerox from the Receivership Court in the Eighth Status Report when it discussed the communications it had with "Counsel for Xerox" relating to short-pay funds and overpaid premiums? (*See* Section V(G), *supra*.)

Even if (*arguendo*) the Receiver, the SDR, and/or Greenberg could prove (with more than references to self-serving declarations) that they had cured Greenberg's conflicts of interests, the Receiver, the SDR, and Greenberg nonetheless had a fiduciary obligation to fully disclose the conflicts and their alleged cure to the Receivership Court for evaluation and approval. *In re Futuronics Corp.*, 655 F.2d 463, 470 (2d Cir. 1981); *see also In re BH&P, Inc.*, 119 B.R. 35, 44 (D.N.J. 1990) (holding that only the court — not counsel — can exercise independent judgment as to the existence of conflicts and whether

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any factors outweigh the conflicts); *In re S. Kitchens, Inc.*, 216 B.R. at 830 (finding counsel's failure to disclose its prior representation of a potential target defendant to be "stunning" and stating that even if the prior representation was not sufficient grounds for disqualification in and of itself (which it was), counsel's failure to disclose the representation would be); *In re Envirodyne Indus.*, 150 B.R. at 1021 (holding that regardless of whether a conflict of interest is *de minimis* or material, the failure to disclose the conflict is grounds for disqualification because only the court — not counsel — can determine if a conflict exists); *In re Leslie Fay Cos.*, 175 B.R. 525, 537-38 (Bankr. S.D.N.Y. 1994) (holding that counsel must disclose any actual or potential conflicts of interest so that the court may determine if a conflict exists and whether to approve counsel's retention); *In re Townson*, No. 12-03027-TOM-7, 2013 Bankr. LEXIS 853 at *20 (Bankr. N.D. Ala. March 7, 2013) (holding that even if counsel believes there are no conflicts of interest, the connections among counsel and the parties or other interested persons must be disclosed so that the court may determine if a conflict actually exists).

Not only was the Receivership Court denied the opportunity to analyze the conflicts and any purported attempts to cure, but creditors, like UHH, were also deprived of necessary information that would have allowed them to file an

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objection to Greenberg's appointment. Rather, the Receiver, the SDR, and Greenberg chose to proceed covertly, permitting Greenberg to bill the Receivership Estate for over $6 million while a substantial target defendant for asset recovery (Xerox) has been permitted to escape all liability to date. (7P.A37 at 1378:18-1379:27; *see also* 2A.A.13 at 0281; 2A.A.16 at 0341-0347; 3A.A.18 at 0486-0499; 3A.A.19 at 0539-0542; 3A.A.20 at 0585-0589; 3A.A.21 at 0642-0644; 4A.A.23 at 0832-0836; 5A.A.24 at 0884-0886; 5A.A.26 at 0954-0970; 5A.A.27 at 1008-1018; 6A.A.29 at 1153-1160; 6A.A.30 at 1186-1188; 6A.A.31 at 1233-1245; 7A.A.33 at 1301-1307; 10A.A.42 at 1808-1815; 13A.A.51 at 2354-2370; 13A.A.57 at 2519-2526.)

Based on the fiduciary, receivership, and bankruptcy precedent set forth above, the Receiver, SDR, and Greenberg had an unmistakable duty to fully disclose Greenberg's conflicts of interest to the Receivership Court and all interested parties (including creditors, like UHH).[10] Because Greenberg failed

[10] Greenberg previously contended that NRS 696B.255 does not explicitly require disclosure of conflicts of interest to the court, while the relevant bankruptcy rules do have an explicit rule requiring disclosure. (12A.A.49 at 2253:9-21.) However, NRS 696B.255 does explicitly require "approval of the court," which would require the disclosure of material information relating to the appointment. Further, the provisions in Chapter 696B, which are silent on conflict disclosure, do not absolve fiduciaries such as the SDR and Greenberg of their ***common law duties*** of disclosure. *McPherson v. U.S. Physicians Mut. Risk Retention Group*, 99 S.W.3d 462, 480 (Mo. Ct. App. 2003) (holding that "where the insolvency code is silent, the common law and general statutory authority should be applied") (internal quotation omitted).

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to disclose its conflicts of interest, and these conflicts have prevented Greenberg from fulfilling its obligations as a fiduciary as counsel for a statutory receiver for a delinquent insurer, disqualification was warranted.

C. Greenberg's Conflict of Interest Relating to Xerox Warrants Disqualification Because It Could Not Appropriately Analyze Harm to the CO-OP Separate and Apart From Xerox — Its Own Client.

It is well-accepted that an impartial receiver and her disinterested counsel are obligated to pursue all legal avenues which will maximize the receivership estate for the benefit of the creditors. *See Hilti, Inc. v. HML Dev. Corp.*, No. 97271, 2007 Mass. Super. LEXIS 66 at *52 (Mass. Super. Ct. Feb. 5, 2007) ("The objective of the [r]eceiver should be that of estate maximization."); *see also Phelan v. Middle States Oil Corp.*, 154 F.2d 978, 990 (2d Cir. 1946) (holding that a receiver (and by extension her counsel) have an "affirmative duty to endeavor to realize the largest possible amount for assets of the estate") (internal citation omitted). In its capacity as counsel for Valley, Greenberg agreed with this receivership principle. (1A.A.7 at 0102:10-12.)

Because a receiver and her counsel must be in a position to freely and fully investigate and pursue any and all culpable parties in order to maximize the assets of the receivership estate, they must not hold any prior allegiances to

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potential target defendants. For instance, in *Pressman-Gutman Co. v. First Union Nat'l Bank*, No. 02-8442, 2004 U.S. Dist. LEXIS 23991, at *1 (E.D. Pa. Nov. 30, 2004), the court determined that a law firm should be disqualified in an ERISA action from representing the profit-sharing plan as a plaintiff as well as two, third-party-defendant officers of Pressman-Gutman and its plan. *Id.* at *1-2, 15, 21. Specifically, the court concluded:

> Because of [the law firm's] duty of loyalty to [the officers] . . . [the law firm] could not recommend to the plan that it act against [the officers], as well as, or instead of, [defendants] First Union and Forefront. [The law firm] could only recommend to the plan that it proceed only against First Union and Forefront. Based on [the law firm's duty of loyalty to [the officers], who may well be liable for the plan's losses, . . . it was unreasonable for [the law firm] to believe it could adequately represent the plan.

Id. at *15.

Accordingly, Greenberg, ***before it accepted the appointment from the Receivership Court as counsel for the Receiver***, needed to ensure that it did not represent any parties that were ***potentially liable to the CO-OP and the Receivership Estate***. Unfortunately, Greenberg's duties as counsel for Xerox have prevented Greenberg from fulfilling its obligations as counsel for the

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Receiver and tainted the asset recovery lawsuits, particularly the Milliman Lawsuit and the Silver State Lawsuit.

Every receivership and bankruptcy court that has encountered this type of conflict of interest has confirmed that any attorney who endeavors to represent both a receiver/bankruptcy debtor as well as a potential target defendant of the estate suffers from a disabling conflict of interest. In *In re S. Kitchens, Inc.*, 216 B.R. 819 (Bankr. D. Minn. 1998), the Bankruptcy Court for the District of Minnesota analyzed a conflict of interest which is a mirror image of that arising from Greenberg's representation of Xerox. The bankruptcy trustee had proposed the retention of counsel (F&W) to file an adversary proceeding against various targets of the bankruptcy estate. *Id.* at 823-24. At the time of its proposed appointment, F&W represented to the court that it did not have any interests adverse to the estate, failing to mention its prior representation of Mr. Gunberg, a member of the debtor's board of directors. *Id.* at 824-25. F&W's prior representation of Mr. Gunberg later became the subject of a motion to disqualify. *Id.* at 825. In confirming that a conflict of interest existed, the court explained:

> ***Regardless of whom a trustee has identified as an opponent***, if a past or present client of proposed counsel was involved in any way with the events that

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> gave rise to the dispute or could otherwise be the subject of a claim based on those events, ***the client has an interest adverse to the estate and disqualification results***.

Id. at 827 (emphasis added). The court ultimately determined that because the defendants were pointing the finger at Mr. Gunberg as the true wrongdoer, F&W's prior representation of him amounted to a disabling conflict of interest warranting disqualification. *Id.* at 827-829 ("Litigation like this cannot go ahead under the pall that its architects may not have analyzed, structured, and pled it with full detachment, ***and may be influenced by continuing loyalty to an unsued agent of the Debtor's downfall***.") (emphasis added); *see also In re Bohack Corp.*, 607 F.2d 258, 264 (2d Cir. 1979) ("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.") (emphasis added); *In re Git-N-Go, Inc.*, 321 B.R. 54, 59 (Bankr. N.D. Okla. 2004) ("It is the duty of counsel for the debtor in possession to survey the landscape in search of property of the estate, defenses to claims, preferential transfers, fraudulent conveyances and other causes of action that may yield a recovery to the estate. ***The jaundiced eye and scowling mien that counsel for the debtor is required***

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to cast upon everyone in sight will likely not fall upon the party with whom he has a potential conflict.") (emphasis added) (internal quotations omitted).

In the underlying delinquency proceeding, the SDR has readily admitted that "[the Greenberg] attorneys are the ones handling the [Milliman Lawsuit], and they are the ones who are preparing the case for trial . . . ." (10A.A.46 at 1871:23-25.) The SDR has further admitted that "[t]he Receiver and SDR have ***relied significantly*** on Greenberg's advice and institutional knowledge regarding the [Milliman Lawsuit]." (*Id.* at 1871:25-27.) ***This is a staggering and insurmountable problem***. Greenberg, as the sole counsel of record for the Receiver — and pursuant to its NRCP 11 and other professional and fiduciary obligations — needed to determine the appropriate defendants to sue in the Milliman Lawsuit (and the other asset recovery lawsuits). However, Greenberg's "advice and institutional knowledge" were tainted by its then-***current representation*** of Xerox in multiple, ***related*** matters. Due to its duties of loyalty to Xerox as its client, Greenberg was (and still is) ethically prohibited from assigning any blame to Xerox with respect to the failures of the CO-OP and, therefore, would be (and has been) disposed to blame other parties, such as UHH. Greenberg is incapable of being an impartial arbiter of whether the CO-OP has valid claims against the defendants in the Milliman Lawsuit because it

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cannot appropriately analyze those claims in light of Xerox's substantial involvement and culpability. *See In re Bohack Corp.*, 607 F.2d 258, 263 (2d Cir. 1979) ("The conflict found by the Bankruptcy Court affects not merely a determination of the proper defendants in the action ***but whether it should have been commenced in the first place***.") (emphasis added).

The Silver State Lawsuit suffers from the same concerns. Silver State has explicitly alleged that Xerox — not Silver State — is in possession of the funds at issue. (7A.A.36 at 1359:24-27.) Yet, the Receiver and Greenberg have not asserted any claims against Xerox. Thus, this is just another example of Greenberg's conflicts of interest and its inability to sue Xerox resulting in Greenberg blaming and suing other entities for Xerox's wrongdoing.

The Receivership Court declined to disqualify Greenberg, in part, because Xerox was not a party to any of the pending asset recovery lawsuits in which Greenberg was counsel of record. (13A.A.52 at 2384:21-23.) ***Yet, that is precisely the problem***. The Receivership Court's simplistic analysis failed to recognize that the conflict does not arise once Xerox becomes a party; rather, it arose when Greenberg was evaluating and filing potential litigation and was ethically unable or unwilling to assign any blame to Xerox — ***its client*** — for the failure of the CO-OP.

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It is impossible for a fiduciary or an attorney to ethically and competently represent a receivership and/or bankruptcy estate — with ongoing duties of impartiality and estate maximization — while maintaining attorney-client relationships with parties who need to be investigated and possibly sued by the estate. *See Pressman-Gutman Co. v. First Union Nat'l Bank*, No. 02-8442, 2004 U.S. Dist. LEXIS 23991 at *1-2, 15, 21 (E.D. Pa. Nov. 30, 2004). Considering that the SDR and Greenberg were supposedly neutral and impartial, owing fiduciary duties to all of the creditors in the Receivership Estate (including UHH), they had an obligation to ***objectively*** analyze the true causes of the CO-OP's failure, including, but not limited to, Xerox's potential culpability. Because Greenberg was ethically unable or unwilling to do so, the Receivership Court erred and abused its discretion by refusing to disqualify Greenberg.

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D. <u>Greenberg's Representation of Valley — a Significant Creditor of the Receivership Estate — Also Warrants Disqualification.</u>

"It is the duty of the Receiver to determine the validity and the preference to be accorded to the claims of creditors." *Hilti, Inc. v. HML Dev. Corp.*, No. 97271, 2007 Mass. Super. LEXIS 66 at *53 (Mass. Super. Ct. Feb. 5, 2007). However, "[i]t is of paramount importance that during this process[,] . . . the

Receiver ensures that the creditors receive equality of treatment so far as is permissible under the law." *Id.* Thus, "***counsel for a creditor should not act as Receiver or be employed by the Receiver in <u>any</u> capacity because of the potential for conflicts of interest***." *Id.* at *88-89 (emphasis added).

The rationale for this rule is simple and straightforward. Creditors are generally adverse to one another because they are fighting over a limited pot of money. Accordingly, the receiver and her counsel must ensure impartiality and equal treatment of each and every creditor. If the receiver or her counsel owes fiduciary duties to one of the creditors based on an existing attorney-client relationship, it can be reasonably assumed that the particular creditor who is fortunate enough to be represented by the same counsel as the receiver could benefit from that arrangement. At a minimum, it taints the entire proceeding and calls into question the legitimacy of the receivership process. *See, e.g.*, *Scholes v. Tomlinson*, Nos. 90 C 1350, 90 C 6615, 90 C 7201, 1991 U.S. Dist. LEXIS 10486 at *23 (N.D. Ill. July 29, 1991) (holding that counsel's dual representation of the receiver and the account holder class "create[d] the unseemly appearance of partiality toward some of the creditors of the receivership entities"); *In re Envirodyne Indus., Inc.*, 150 B.R. 1008, 1019 (Bankr. N.D. Ill. 1993) (holding that where counsel represented the debtor and a

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substantial creditor of the debtor, the debtor's interests and the interests of the creditors as a whole were "not best represented at a negotiation table by a lawyer who faces a substantial client on the other side"); *In re Git-N-Go, Inc.*, 321 B.R. 54, 60 (Bankr. N.D. Okla. 2004) (holding that debtor's counsel could not "effectively object" to the claim of a substantial secured creditor of the debtor where counsel also represented the secured creditor, and noting that this conflict "could have a significant impact on the claims of unrelated unsecured creditors of the estate"); *In re Am. Printers & Lithographers, Inc.*, 148 B.R. 862, 865-66 (Bankr. N.D. Ill. 1992) (finding that disqualification was warranted due to the actual conflict of interest arising from counsel's representation of the debtor and a creditor, as counsel would not be able to "vigorously negotiate" with the creditor "in order to fulfill its duties" to the debtor without "jeopardizing its relationship" with the creditor who happened to be a large and important client of conflicted counsel).

At the time of Greenberg's appointment as receivership counsel, it was representing adverse parties on both sides of the receivership action. (1A.A.7; 2A.A.12 at 0236:25-27.) Greenberg could not fulfill its obligations to the Receivership Estate and its creditors because of fiduciary duties owed to one of the most significant creditors of the Receivership Estate — with a claim in

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excess of $5 million. (1A.A.7 at 0102:4-5.) How could the Receivership Court and other creditors be assured that Valley would not receive preferential treatment from Greenberg, especially considering there are limited assets in the Receivership Estate and creditors are likely going to have to accept claim discounts? Due to its allegiances and obligations to Valley, Greenberg cannot play "hardball" with Valley and its $5 million claim. It cannot threaten litigation against Valley or dispute its claim in any respect, as any such adverse action would be a breach of Greenberg's duties owed to Valley.

Even if Greenberg could obtain a waiver of the conflict of interest from Valley, numerous courts have rejected the effectiveness of any such waiver, finding this type of conflict of interest untenable and incurable. *See, e.g.*, *In re Git-N-Go, Inc.*, 321 B.R. at 60 (holding that the debtor, as a fiduciary, cannot waive conflicts of interest on behalf of the estate); *see also In re Project Orange Assocs., LLC*, 431 B.R. 363, 374-75 (Bankr. S.D.N.Y. 2010); *In re Am. Energy Trading, Inc.*, 291 B.R. 154, 158 (Bankr. W.D. Mo. 2003). For these reasons, the Receivership Court erred and abused its discretion by refusing to disqualify Greenberg due to its Valley conflict of interest.

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E. UHH Has Standing to Move for Greenberg's Disqualification.

Although Unite Here Health is not a former Greenberg client, it has standing to object to Greenberg's appointment and continuing role as the Receiver's counsel. As set forth in Section VIII(B)(1), *supra*, Greenberg is representing a receiver with fiduciary obligations to every single creditor of the Receivership Estate. In fact, on multiple occasions, ***Greenberg has claimed that the Receiver — and thus Greenberg by extension — represents all of the creditors***. (*See, e.g.*, 10A.A.40 at 1754:6-7; 13A.A.54 at 2415:7-9.) Thus, it logically follows that any creditor has standing to object to a court-appointed counsel's conflicts of interest that are affecting the receivership estate. *See, e.g.*, *In re Bohack Corp.*, 607 F.2d 258, 262 (2d Cir. 1979); *In re Envirodyne Indus., Inc.*, 150 B.R. 1008, 1011 (Bankr. N.D. Ill. 1993); *In re F&C Int'l, Inc.*, 159 B.R. 220, 222 (Bankr. S.D. Ohio 1993).

Moreover, both UHH parties have standing to object to Greenberg's conflicts based on their status as defendants in the Milliman Lawsuit. *See, e.g.*, *CFTC v. Eustace*, Nos. 05-2973, 06-1944, 2007 U.S. Dist. LEXIS 33137, at *13 (E.D. Pa. May 3, 2007); *In re S. Kitchens, Inc.*, 216 B.R. 819, 821 (Bankr. D. Minn. 1998); *In re Townson*, No. 12-03027-TOM-7, 2013 Bankr. LEXIS 853 at *2 (Bankr. N.D. Ala. Mar. 7, 2013). Just as in *Eustace*, *Southern*

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Kitchens, and *Townson*, UHH has been blamed for the wrongdoing of Greenberg's client. Specifically, UHH has been harmed by Greenberg's inability and unwillingness to acknowledge Xerox's responsibility for the CO-OP's insolvency and, accordingly, to hold Xerox accountable. Because UHH has been sued by conflicted counsel, it has standing to seek Greenberg's disqualification.

Moreover, Nevada specifically allows non-clients to seek the disqualification of counsel. "[I]f the breach of ethics 'so infects the litigation in which disqualification is sought that it impacts the [nonclient] moving party's interest in a just and lawful determination of her claims, she may have the . . . standing needed to bring a motion to disqualify based on a third-party conflict of interest or other ethical violation.'" *Liapis v. Second Jud. Dist. Ct. ex rel. Cnty. of Washoe*, 128 Nev. 414, 420, 282 P.3d 733, 737 (2012) (internal quotation omitted). Here, the just and lawful determination of Unite Here Health's claim as a creditor of the Receivership Estate is jeopardized by Greenberg's ever-growing legal fees and costs. Greenberg has already billed the Receivership Estate over $6 million in fees and costs between January 2017 and January 2021. (7P.A37 at 1378:18-1379:27; 2A.A.13 at 0281; 2A.A.16 at 0341-0347; 3A.A.18 at 0486-0499; 3A.A.19 at 0539-0542; 3A.A.20 at 0585-

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0589; 3A.A.21 at 0642-0644; 4A.A.23 at 0832-0836; 5A.A.24 at 0884-0886; 5A.A.26 at 0954-0970; 5A.A.27 at 1008-1018; 6A.A.29 at 1153-1160; 6A.A.30 at 1186-1188; 6A.A.31 at 1233-1245; 7A.A.33 at 1301-1307; 10A.A.42 at 1808-1815; 13A.A.51 at 2354-2370; 13A.A.57 at 2519-2526.) Over $35 million in creditors' claims have been made against the Receivership Estate, only $1 million in claims have been paid to date, and there is less than $4.5 million in unrestricted cash assets remaining in the Receivership Estate. (13A.A.51 at 2315:3-11, 2316:14-2317:2 & n.4, 2376, 2378; 13A.A.57 at 2462:17-19.)

Further, Greenberg's conflicts of interest have infected the receivership and its related asset recovery lawsuits. Specifically, the District Court in the Milliman Lawsuit has denied both UHH's motion for leave to file a third-party complaint against Xerox and Silver State for contribution and UHH's motion to consolidate the Silver State Lawsuit with the Milliman Lawsuit (since the Receiver seeks to collect the same damages in both actions), simply because granting the motions would require the District Court to disqualify Greenberg due to its conflicts of interest. (13A.A.58 at 2538:25-2539:2.) Thus, the just and lawful determination of UHH's defenses in the Milliman Lawsuit has been obstructed by Greenberg's failure to properly disclose its conflicts of interest

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over four years ago when it first sought approval as counsel for the Receiver in the delinquency proceeding.

IX. CONCLUSION

For the foregoing reasons, this Court should vacate the Order Denying Disqualification and order that Greenberg is disqualified to serve as counsel for the Receiver in the delinquency proceeding and all related asset recovery lawsuits brought by the Receiver. The action should also be remanded with instructions to the Receivership Court to rule on the issue of the disgorgement of the fees paid to date by the Receivership Estate to Greenberg.

DATED this 14th day of June, 2021.

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NRAP 32(a)(9) CERTIFICATE OF COMPLIANCE

1. I hereby certify that this Opening Brief complies with the formatting requirements of NRAP 32(a)(4), the typeface requirements of NRAP 32(a)(5), and the type-style requirements of NRAP 32(a)(6) because:

[x] This Opening Brief has been prepared in a proportionally spaced typeface using Microsoft Word for Office 365 in Times New Roman font 14.

2. I further certify that this Opening Brief complies with the page- or type-volume limitations of NRAP 32(a)(7) because, excluding the parts of the brief exempted by NRAP 32(a)(7)(C), it is proportionally spaced, has a typeface of 14 points or more, and contains 13,125 words.

3. I further he6reby certify that I have read this Opening Brief, and to the best of my knowledge, information, and belief, it is not frivolous or interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. I further certify that this Opening Brief complies with all applicable Nevada Rules of Appellate Procedure, in particular NRAP 28(e)(1), which requires every assertion in the Brief regarding matters in the record to be supported by a reference to the page

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and volume number, if any, of the appendix where the matter relied on is to be found.

I understand that I may be subject to sanctions in the event that the accompanying Opening Brief is not in conformity with the requirements of the Nevada Rules of Appellate Procedure.

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CERTIFICATE OF SERVICE

I certify that I am an employee of BAILEY❖KENNEDY and that on the 14th day of June, 2021, service of the foregoing **APPELLANTS' UNITE HERE HEALTH AND NEVADA HEALTH SOLUTIONS, LLC'S OPENING BRIEF and APPELLANTS' APPENDIX, VOLUMES 1 through 13,** was made by electronic service through Nevada Supreme Court's electronic filing system and/or by depositing a true and correct copy in the U.S. Mail, first class postage prepaid, and addressed to the following at their last known address:

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ADDENDUM

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CFTC v. Eustace

United States District Court for the Eastern District of Pennsylvania

May 3, 2007, Decided

CIVIL ACTION NO. 05-2973, CIVIL ACTION NO. 06-1944

Reporter
2007 U.S. Dist. LEXIS 33137 *

COMMODITY FUTURES TRADING COMMISSION v. PAUL M. EUSTACE, et al.; C. CLARK HODGSON, JR., RECEIVER, et al. v. MAN FINANCIAL INC., et al.

Subsequent History: Objection overruled by *Hodgson v. Man Fin. Inc., 2007 U.S. Dist. LEXIS 35145 (E.D. Pa., May 7, 2007)*

Costs and fees proceeding at *CFTC v. Eustace, 2007 U.S. Dist. LEXIS 44757 (E.D. Pa., June 18, 2007)*

Prior History: *Hodgson v. Man Fin., Inc., 2007 U.S. Dist. LEXIS 15739 (E.D. Pa., Mar. 2, 2007)*
CFTC v. Eustace, 2005 U.S. Dist. LEXIS 40247 (E.D. Pa., Dec. 29, 2005)

Core Terms

appointment, entities, investors, disclosure, Offshore, litem, affiliate, disqualification, disqualify, replaced, third-party, Memorandum, court-appointed

Case Summary

Procedural Posture
Plaintiff Commodity Futures Trading Commission (CFTC) brought an action against defendants based on an alleged fraudulent trading scheme, and a receiver was appointed. The receiver brought a related action against a commission merchant, and the court considered whether to ***disqualify*** the ***receiver*** based on representation by the ***receiver*** and his ***counsel*** of entities related to a fund administrator named as a third-party defendant.

Overview
Although the receiver was aware of the administrator's involvement in the subject transactions, the receiver did not disclose the representation of the related entities. The receiver contended that he had no reason to anticipate the administrator being named a party in the action and that no conflict existed because the administrator was separate from the represented entities, even though they were in the same corporate organization. The court held that disqualification of the receiver was warranted, but only with regard to the litigation against the commission merchant in which the administrator was a party. Although the receiver was highly regarded and experienced in complex litigation, there was the potential for an appearance of impropriety in the event that the receiver prevailed against the merchant but the merchant did not prevail against the administrator. Nonetheless, the additional expense and delay which would be occasioned by appointment of a new receiver warranted retention of the receiver for all matters other than the litigation involving the merchant.

Outcome
A ***receiver*** ad litem was appointed to replace the ***receiver*** only in the litigation involving the merchant.

LexisNexis® Headnotes

Legal Ethics > Client Relations > Representation > Acceptance

Legal Ethics > Client Relations > Conflicts of Interest

HN1[] **Representation, Acceptance**

As reflected in Pa. R. Prof. Conduct 1.7, under certain circumstances a law firm that has a client relationship with a given corporation or other organization is not barred from accepting a representation adverse to an affiliate of that corporation or organization, such as an unrelated subsidiary of a large corporation.

Legal Ethics > Client Relations > Representation > Acceptance

Legal Ethics > Client Relations > Conflicts of Interest

HN2[] **Representation, Acceptance**

See Pa. R. Prof. Conduct 1.7.

Legal Ethics > Client Relations > Representation > Acceptance

Legal Ethics > Client Relations > Conflicts of Interest

HN3[] **Representation, Acceptance**

A lawyer who represents a corporation or other organization does not, by virtue of that representation, necessarily represent any constituent or affiliated organization, such as parent or subsidiary. Pa. R. Prof. Conduct 1.13(a). Thus, the lawyer for an organization is not barred from accepting representation adverse to an affiliate in an unrelated matter, unless the circumstances are such that the affiliate should also be considered a client of the lawyer, there is an understanding between the lawyer and the organizational client that the lawyer will avoid representation adverse to the client's affiliates, or the lawyer's obligations to either the organizational client or the new client are likely to limit materially the lawyer's representation of the other client.

Civil Procedure > Appeals > Standards of Review > Abuse of Discretion

Civil Procedure > ... > Receiverships > Receivers > General Overview

HN4[] **Standards of Review, Abuse of Discretion**

A court's actions with respect to a receiver are reviewed under an abuse of discretion standard.

Civil Procedure > ... > Receiverships > Receivers > Duties of Receivers

HN5[] **Receivers, Duties of Receivers**

A receiver, as an officer or arm of the court, is a trustee with the highest kind of fiduciary obligations. He owes a duty of strict impartiality, of undivided loyalty, to all persons interested in the receivership estate, and must not dilute that loyalty. He is bound to act fairly and openly with respect to every aspect of the proceedings before the court. The court, as well as all the interested parties, have the right to expect that all its officers, including the receiver, will not fail to reveal any pertinent information or use their official position for their own profit or to further the interests of themselves or any associates. A receiver has the affirmative duty to endeavor to realize the largest possible amount for assets of the estate. If he has vital information which, if disclosed, might bring a better price for property which is sold pursuant to court order, he must fully disclose it prior to the sale when the prospects are greater for successful bargaining.

Civil Procedure > ... > Receiverships > Receivers > General Overview

HN6[] **Receiverships, Receivers**

A claim against a derelict receiver is not against an ordinary trustee but against a court's officer. Who has

the right to assert such a claim is a question affecting the integrity of the court itself. The federal courts, in holding their own officers to accountability, should not be hampered by state court decisions relating to ordinary trustees. When a federal receiver incurs obligations through misconduct, the title thereto is similarly to be determined by federal law. The doctrine, relative to receivers, of strict accountability, and of opposition to divided loyalties, is prophylactic; it aims not merely to punish actual evil in cases where it occurs but to avoid the tendency to evil in other cases.

Civil Procedure > Attorneys > Disqualification of Counsel

HN7[] **Attorneys, Disqualification of Counsel**

Where a choice of counsel must be approved by a court as appropriate, such that the integrity of the judicial process is implicated, the cost and delay of replacing counsel with a conflict of interest may be outweighed.

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For SEP ALAVI, WILLIAM WAMBACH, TIMOTHY BRAUN, JODY MCMILLAN, JAMES ZAMORA, MAN FINANCIAL INC, Defendants: ABRAHAM C. REICH, LEAD ATTORNEY, JOSHUA HORN, FOX ROTHSCHILD O'BRIEN & FRANKEL LLP, PHILADELPHIA, PA; ANNALIESE F. FLEMING, BARACK FERRAZZANO KIRSCHBAUM PERLMAN & NAGELBERG, CHICAGO, IL; CHRISTOPHER P. GREELEY, DAVID M. ROSENFIELD, GRANT R. CORNEHLS, MATTHEW D. SOBOLEWSKI, SUSAN T. DWYER, THERESE M. DOHERTY, LEAD ATTORNEYS, HERRICK FEINSTEIN LLP, NEW YORK, NY; DAVID R. KING, LEAD ATTORNEY, HERRICK FEINSTEIN LLP, PRINCETON, NJ; MATTHEW D. PARROTT, LEAD ATTORNEY, KATTEN MUCHIN ROSENMAN LLP, NEW YORK, NY.

For MONICA RODRIGUEZ, Defendant: ABRAHAM C. REICH, LEAD ATTORNEY, JOSHUA HORN, FOX ROTHSCHILD O'BRIEN & FRANKEL LLP, PHILADELPHIA, PA; ANNALIESE F. FLEMING, BARACK FERRAZZANO KIRSCHBAUM PERLMAN & NAGELBERG, CHICAGO, IL; CHRISTOPHER P. GREELEY, DAVID M. ROSENFIELD, GRANT R. CORNEHLS, MATTHEW D. SOBOLEWSKI, SUSAN T. DWYER, THERESE M. DOHERTY, LEAD ATTORNEYS, HERRICK FEINSTEIN LLP, NEW YORK, NY; DAVID R. KING, LEAD ATTORNEY, HERRICK FEINSTEIN LLP, PRINCETON, NJ; MATTHEW D. PARROTT, LEAD ATTORNEY, KATTEN MUCHIN ROSENMAN LLP, NEW YORK, NY; CATHI A. HESSION, LEAD ATTORNEY, FLEMMING, ZULACK AND WILLIAMSON, NEW YORK, NY; JASON T. COHEN, LEAD ATTORNEY, FLEMMING, ZULACK AND WILLIAMSON ZAUDERER LLP, NEW YORK, NY.

For MCCARTER & ENGLISH, LLP, Respondent: LISA M. SALAZAR, LEAD ATTORNEY, MCCARTER AND ENGLISH, LLP, PHILADELPHIA, PA.

For DAVID SAWYIER, Movant: JOANNE R. DRISCOLL, LEAD ATTORNEY, KEVIN M. FORDE, LTD., CHICAGO, IL.

For JOHN WALLACE, EDWARD GOBORA, ThirdParty Defendants: CANDICE TOLL AARON, MICHAEL RAY ROBINSON, LEAD ATTORNEYS, SAUL EWING LLP, WILMINGTON, DE; TIMOTHY E. HOEFFNER, LEAD ATTORNEY, SHILOH DAWN THEBERGE, SAUL EWING, LLP, PHILADELPHIA, PA.

For DAVID LASHBROOK, SCOTT SOMERVILLE, ThirdParty Defendants: DAVID M. HOWARD, LEAD ATTORNEY, JOHN V. DONNELLY, III, DECHERT LLP, PHILADELPHIA, PA; MICHAEL S. DOLUISIO, LEAD ATTORNEY, DECHERT , PRICE & RHOADS, PHILA, PA; TIMOTHY E. HOEFFNER, LEAD ATTORNEY, SAUL EWING, LLP, PHILADELPHIA, PA.

For UBS FUND SERVICES (CAYMAN) LTD., ThirdParty Defendant: DAVID FLEISCHER, JONATHAN A. CHOA, KEITH W. MILLER, LAWRENCE J. CONLAN, LEAD ATTORNEYS, PAUL HASTINGS JANOFSKY & WALKER LLP, NEW YORK, NY; GAETAN ALFANO, LEAD ATTORNEY, WILLIAM L. CARR, MILLER ALFANO & RASPANTI, P.C., PHILADELPHIA, PA; TIMOTHY E. HOEFFNER, LEAD ATTORNEY, SAUL EWING, LLP, PHILADELPHIA, PA.

For MAN FINANCIAL INC, ThirdParty Plaintiff: JOSHUA HORN, LEAD ATTORNEY, FOX ROTHSCHILD O'BRIEN & FRANKEL LLP, PHILADELPHIA, PA; THERESE M. DOHERTY, HERRICK FEINSTEIN LLP, NEW YORK, NY.

For JODY MCMILLAN, JAMES ZAMORA, MONICA RODRIGUEZ, MAN FINANCIAL INC, SEP ALAVI, WILLIAM WAMBACH, TIMOTHY BRAUN, Counter Claimants: THERESE M. DOHERTY, HERRICK FEINSTEIN LLP, NEW YORK, NY; JOSHUA HORN, FOX ROTHSCHILD O'BRIEN & FRANKEL LLP, PHILADELPHIA, PA.

Judges: [*1] Michael M. Baylson, U.S.D.J.

Opinion by: Michael M. Baylson

Opinion

MEMORANDUM

Baylson, J.

These cases arise out of significant investor losses sustained in an allegedly fraudulent futures trading scheme, estimated at over $ 200 million. The issue discussed in this Memorandum is collateral to the merits of these cases and concerns whether the court-appointed Receiver, C. Clark Hodgson, Jr., Esquire ("Hodgson" or "Receiver"), and his law firm, Stradley, Ronon, Stevens and Young, LLP ("Stradley"), must be replaced because they failed to disclose prior client relationships with various UBS entities knowing that another UBS entity, UBS Fund Services (Cayman) Limited ("UBS Cayman"), participated in various aspects of the transactions underlying these cases. UBS Cayman has now been brought in as a third-party defendant in *Hodgson v. Man Financial, Inc.*, No. 06-1944.

I. *Factual Background* [1]

[*2] On June 22, 2005, the Commodity Futures Trading Commission ("CFTC") brought an action, *CFTC v. Eustace*, No. 05-2973, against Paul Eustace ("Eustace") and the Philadelphia Alternative Asset Management Co., LLC ("PAAMCO") for an alleged fraud resulting in significant investor losses. The CFTC sought, among other remedies, a Statutory Restraining Order ("SRO"), including appointment of a Receiver by the Court.

Before appointing Hodgson as the Receiver, Judge John R. Padova, to whom the case was originally assigned, advised Hodgson during a telephone conversation of the entities involved in the case, including Eustace, PAAMCO and the CFTC. There was no mention at that time of any other potential parties or the need for Hodgson to check any other conflicts. Hodgson sent Judge Padova a letter on the same day advising him no conflicts were found, and he could accept the appointment. Judge Padova accordingly issued an order on June 23, 2005 appointing Hodgson as a temporary receiver for Defendant PAAMCO and its "partners, affiliates or subsidiaries or related entities of the Defendants" with the full powers of an equity receiver.

On July 6, 2005, this case was reassigned to the undersigned, **[*3]** who made Hodgson's appointment permanent in an order dated September 21, 2005, and renewed that appointment in an order dated April 21, 2006. Since the beginning of these proceedings, the Receiver has been represented by Stradley, in which the Receiver was a partner until late December 2006 and currently holds the title of senior counsel.

A. *Early Stages*

In several hearings and orders entered in the CFTC case, the Court, particularly in the early stages, emphasized the need for the CFTC and the Receiver to work together and initially directed the CFTC, because of its initial investigation and its expertise in the subject matter, as well as because its counsel were paid by the government, to take the lead in ascertaining the factual background of the case. The Court charged both to consider whether additional actions should be brought to recover damages on behalf of the investors, but to seek Court approval before bringing any such suits. The Receiver acted promptly and appropriately in taking action, gathering together funds in different accounts, some located in Canada, pursuant to his obligations to secure assets belonging to investors. The Court was advised, at various **[*4]** hearings and in other communications, that although there were some problems in relations between the Receiver and the CFTC, progress was being made.

As part of his efforts, the Receiver sought sanctions in the CFTC action against a third party, Man Financial, Inc. ("Man"), a futures broker that had provided trading services to PAAMCO and its related entities. The Court held several hearings on the Receiver's motions to require Man to disclose information required by the SRO and ordered Man to comply with the SRO.

B. *Man Complaint*

Pursuant to the Court's above-noted requirement, the Receiver submitted a letter *in camera* briefly identifying certain civil actions that he intended to file. On April 28,

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[1] What follows is a brief summary of this case. Further details about the case are set forth in prior Memoranda of this Court, *see* 2006 U.S. Dist. LEXIS 92767, 2006 WL 3791341, 2006 U.S. Dist. LEXIS 72957, 2006 WL 2869532 and 2006 U.S. Dist. LEXIS 73063, 2006 WL 2707397. Details about the background facts on the conflict of interest issue are set forth in the Master's Report, discussed below, and filed at Doc. No. 351 in Civ. A. No. 05-2973 and Doc. No. 199 in Civ. A. No. 06-1944.

2006, the Court issued an order granting the Receiver permission to bring a separate action against Man and certain of Man's employees arising out of their alleged wrongful conduct in their relationship with PAAMCO and Eustace (Doc. No. 217).

On May 8, 2006, the Receiver initiated the action against Man and several of its employees, *Hodgson v. Man Financial, Inc.*, No. 06-1944. The Complaint alleges PAAMCO acted as manager for a number of offshore funds, including the **[*5]** major fund, entitled the Philadelphia Alternative Asset Fund Limited (the "Offshore Fund"), and Man acted as a futures commission merchant through which the Offshore Fund traded commodity futures and options. The Offshore Fund's Administrator, UBS Cayman, in turn was responsible for preparing monthly account or net asset value statements reporting the performance of the Offshore Fund to the Fund's investors.

UBS Cayman is mentioned throughout the Complaint, and its role in the overall business transaction was, according to the Complaint, a significant one. The Complaint paints UBS Cayman as one of the victims of the wrongdoing by Man. According to the Complaint, Man, among other things, allowed Eustace and PAAMCO to improperly open Offshore Fund accounts and to set up an account, known as the "50 Account," in which losses were allowed to accumulate, unknown to UBS Cayman and the investors, as well as PAAMCO's board of directors and employees. [2] In addition to asserting that Man concealed the 50 Account, the Complaint further alleges that Man made inaccurate trading results from another account, known as the 10 Account, available to UBS Cayman via an online system upon which Eustace **[*6]** knew UBS Cayman relied in preparing the monthly account or net asset value statements for the investors. (Compl. P 28.) The Complaint then continues, "Eustace caused Man Financial to convince UBS to back-date certain EFP trades . . . and to artificially report that numerous large trades occurred at market highs and lows on the last trading day of the prior month instead of the first day of the following month . . . in order to artificially boost the month-end returns of the 10 Accounts." *Id.* P 32. According to the Complaint, this backdating scheme falsely improved the performance of the Offshore Fund and again led UBS to report inaccurate net asset values to investors. *Id.* P 33.

[*7] The Receiver has candidly acknowledged that, shortly after his appointment by Judge Padova, he learned that UBS Cayman and another UBS entity, UBS Securities LLC ("UBS Securities"), had played a role in the underlying transactions and knew that Stradley attorneys, including the Receiver himself, represented other UBS entities, including several mutual funds bearing the UBS name and UBS Financial Services, Inc. (formerly UBS PaineWebber, Inc.) ("UBS Financial Services"). However, the Receiver and his counsel determined that they did not need to conduct a further conflict check because they were fully aware of Stradley's representation of the other UBS entities and determined that there was no conflict requiring disclosure to the court or withdrawal as the Receiver. According to the Receiver and his counsel, at that time, they did not have any reason to believe that any UBS entity would possibly be a party in the litigation. Even if such a possibility existed, they believed it would not present a conflict because the UBS entities represented by the Receiver and Stradley were completely separate affiliates in a larger corporate organization from UBS Cayman and UBS Securities.

At or **[*8]** about the time that the Receiver and Stradley were considering, getting permission for, and drafting the Complaint against Man, despite the many references to UBS Cayman in the Complaint and specifically the allegation that UBS backdated certain documents, albeit allegedly at the urging of Man, they continued to fail to disclose their UBS relationships to the Court or to the CFTC. On May 2, 2006, just prior to the Receiver filing the suit against Man, a meeting took place in the offices of the CFTC in Washington, DC, attended by the Receiver and his counsel, in which they discussed various entities involved in the CFTC case and the proposed lawsuit against Man. At this meeting, the role of UBS Cayman was discussed. The *in camera* letter to the Court outlining the actions the Receiver intended to file, and the meeting with the CFTC in Washington, DC on May 2, 2006, provided the opportunity for the Receiver and/or his counsel to make these disclosures in a confidential manner. The Court does not suggest that the Receiver or his counsel had any improper motives or intent, but the Court cannot ignore the fact that the disclosure was not made at that

[2] PAAMCO set up certain entities in the Cayman Islands, presumably to avoid taxes or other U.S. governmental regulations, and had arranged for UBS Cayman to administer that fund. After the Receiver was appointed in this Court, a court in the Cayman Islands established, authorized under Cayman Island law, a firm to act to act as a liquidator of the Cayman Island entities. This Court approved the protocol for coordination between the Receiver and the Cayman Islands liquidators, known as the Joint Liquidators.

time.

In November and December 2006, **[*9]** Man and other parties conducted depositions of several witnesses employed by UBS Cayman in the Cayman Islands. According to the Receiver, the first time that he or his counsel learned of any possible negligence on the part of UBS Cayman was during the November and December 2006 depositions of the UBS Cayman witnesses. On December 6, 2006, Lee Rosengard, Esquire, one of the attorneys for the Receiver at the Stradley firm, sent an email reporting on the testimony of one of those witnesses and indicating that, based on the failure of UBS Cayman to seek out independent information for verification of accounts operated by PAAMCO, "I continue to believe that the Joint Liqui[]dators in the Caymans have a malpractice claim against UBS. We need to discuss this with Clark." [3]

[*10] The Court held a hearing on the record on January 16, 2007. Initially, the Court summarized the content of the unrecorded telephone conference that had taken place the prior week on January 11, which generally concerned scheduling matters, but during which Man had advised the Court that it intended to bring UBS Cayman into the case as a third-party defendant. This had led to some discussion during the phone call about the impact the inclusion of UBS Cayman would have on both scheduling and settlement discussions. (Tr. 5-7, Jan. 16, 2007.) At the hearing, the Receiver advised the Court that he had retained an esteemed individual practitioner, Peter Hearn, to address issues relating to UBS Cayman. The Court asked Man's counsel if she knew why the Receiver had not named UBS Cayman as a defendant, and asked the same question of Receiver's counsel, at the same acknowledging that the Receiver's counsel may not want to answer that question "because of a conflict issue." The Court used the phrase "conflict issue" because counsel at the hearing implied that a conflict issue had led to the Receiver's retention of Mr. Hearn, who responded that he did not have any knowledge as to why Mr. Hodgson **[*11]** did not name UBS Cayman as one of the original defendants. *Id.* at 11. Instead, Mr. Hearn argued that it was too late to bring third-party claims against UBS Cayman.

Later in the hearing, the Court again inquired as to why, if Man believed there were grounds to bring in UBS Cayman as a party, the Receiver had not done so either in this Court or in conjunction with the Joint Liquidators. The Court prefaced this question by stating, "[n]ow, if you don't want to specifically answer that question because of your firm's conflict with UBS Cayman, I'll defer to Mr. Hearn." *Id.* at 30. Receiver's counsel stated: "I can't speak certainly to the issue of the merits of the claim against UBS or how that may compare on a relative basis with the claims that we have already asserted, . . . which is a significant piece of answering Your Honor's question but one I can't -- I can't obviously address. What I can say is this. We certainly factored that into the mix. The Receiver factored that into the mix in coming to the decision that he did in terms of the position to take on joinder and the timing of the trial." *Id.* The Court then asked, assuming UBS was sued, whether it should be in **[*12]** the same trial as Man or in a bifurcated trial that would take place after the trial against Man was completed. Receiver's counsel responded that the Receiver was intent on trying the case in spring 2007 and including both Man and the third party defendants. Mr. Hearn agreed with this statement and noted, "we sued the people who we sued because we felt they were the people who we ought to sue." *Id.* at 32. [4]

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[3] This phraseology suggests that Rosengard had reached and communicated this belief at a prior date, which the Master suggests was a few days prior. Rosengard's reference to the "Joint Liquidators" refers to the fact that, in the protocol between the Receiver and the Joint Liquidators, approved by this Court, the Joint Liquidators were given primary responsibility to institute litigation against entities in the Cayman Islands. However, nothing has been presented to this Court suggesting that the Joint Liquidators has ever started, let alone considered, litigation against UBS Cayman.

[4] Although an observer of the events that took place in the early part of this year might conclude that there were some inconsistencies in the Receiver and Stradley's positions concerning UBS Cayman, the Court does not fault them for retaining Mr. Hearn. As they told the Master, they did so out of an abundance of caution, given the fact that Man was seeking leave to name UBS Cayman as a third-party defendant, and they knew that questions would arise as to the timing of the trial, bifurcation issues, etc. At the hearing on April 18, 2007, counsel for the Receiver asserted that the Receiver and Stradley had no conflict with UBS Cayman and could sue it, but had decided on the merits of the question that it would be inadvisable to do so.

The Receiver had prepared a letter for the hearing explaining their position on this issue and offered to submit that letter to the Court *in camera*. Subsequently, the Receiver offered to share the letter with CFTC counsel as well. The Court is unwilling to have it filed of record because it obviously contains strategic attorney work product material. Man has opposed the Court receiving a letter on an *ex parte* basis. The

[*13] Several weeks later, counsel for Man sent a letter to this Court dated February 8, 2007 asserting that the Receiver and Stradley had a serious conflict of interest, drawing into question the Receiver's ability to continue to act as a receiver for PAAMCO and its related affiliates and subsidiaries. Man Financial pointed out that the Receiver and his firm had been representing several UBS clients since at least 2002, including UBS Financial Services and several UBS mutual funds, but this information was never disclosed to the Court, the CFTC or the investors in the Offshore Fund. The Receiver and his counsel responded to this letter on February 9 denying the existence of any conflict of interest. The CFTC then responded in a letter on February 13 in which it also expressed concern that a conflict of interest existed and continues to exist because of the Receiver's and his firm's representation of UBS entities. Additional letters were sent by Man and Stradley on February 13 and February 16, respectively. In response to this correspondence, the Court held a hearing on February 16, 2007 on whether the Court should appoint a Special Master under *Federal Rule of Civil Procedure 53* **[*14]** to investigate the factual underpinnings of the Receiver's and his firm's alleged conflict of interest. Later the same day, the Court issued an order appointing a retired Common Pleas Judge, Abraham J. Gafni, as a Master ("Master") to investigate these issues.

The Master then proceeded to conduct a thorough investigation into the factual circumstances underlying the Receiver's alleged conflict because of the UBS representation. The Master's Report (Doc. No. 199 in the Man action) was filed and served on March 30, 2007 and laid out in detail the facts underlying the contentions of the parties on the conflict issue, and the factual circumstances leading up to Man's letter informing the Court of Stradley's representation of several UBS-related entities. Because the Master's Report is on file, the Court need not further detail its contents in this Memorandum. The parties were given an opportunity to, and did, respond to this Report in writing and, on April 18, 2007, the Court held another hearing on the Master's Report and to hear argument as to what actions, if any, the Court should take with respect to the Receiver and his law firm. There were only a few minor corrections raised to **[*15]** the factual aspects of the Master's report in the parties' responses or at the hearing. However, the parties differ significantly on what should now happen based on those facts.

The Master did an excellent job of summarizing the parties' positions and the factual circumstances that now lead to the Court's present decision. For that reason, this Memorandum will focus on the legal issues raised by those facts.

II. *Contentions of the Parties*

The Receiver asserts that he has not done anything which requires the Court to take any action, and the case should proceed as before. The CFTC, and separately Man, assert that the Receiver's failure to disclose his own relationship and that of the Stradley firm with various UBS entities should lead to his disqualification and the appointment of a new Receiver. UBS Cayman did not take a position on this topic, and neither did any of the third party individual defendants. Various investors wrote to the Court, and although the Court does not have information as to the relative amounts of their investments or their alleged losses, most of the investors who communicated to the Court preferred that the Court allow the Receiver and his law **[*16]** firm to continue. However, one group of investors, the Edison Fund Limited, the Fairfax Fund Limited, and the Nucleus Fund Limited, represented by counsel, moved to intervene and suggested the appointment of an attorney from their counsel's law firm to take over as Receiver. They have since withdrawn that motion.

The Receiver and his law firm urge the Court to analyze this issue in connection with the Rules of Professional Conduct adopted by the Pennsylvania Supreme Court, which are applicable in this Court. *HN1*[↑] As reflected in Rule 1.7 [5] **[*18]** and Comment 34 [6], under certain

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CFTC also asserts that the contents of the letter are not relevant on the conflict issue. The Receiver advised the Court that he retained Mr. Hearn out of an abundance of caution because of the Stradley representation of other UBS entities completely separate from UBS Cayman. The record is also clear that the Receiver and his firm never sought any waiver from UBS. The Court agrees with Man and the CFTC that the absence of disclosure is the key issue in the resolution of the matter currently before the Court.

[5] Rule 1.7 of the Pennsylvania Rules of Professional Conduct provides:

> *HN2*[↑] (a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:
>
> (1) the representation of one client will be directly adverse to another client; or

circumstances, a law firm that has a client relationship with a given corporation or other organization is not barred from accepting a representation adverse to an affiliate of that corporation or organization, such as an unrelated subsidiary of a large corporation. The Receiver and his counsel argue that the UBS entities they represent and those entities which are involved in this litigation are separate legal entities, and there is no reason they should be treated as the same client. Moreover, according to the Receiver and his counsel, there was no expectation by UBS Financial Services that Stradley would avoid representations **[*17]** adverse to UBS Cayman.

The Receiver's legal position is supported by an expert report by Lawrence J. Fox, an attorney well known for his expertise in professional responsibility matters. If this dispute was merely an issue of whether a law firm could accept a representation adverse to a corporate affiliate of an entity **[*19]** when the firm has an ongoing client relationship with another unrelated affiliate of that entity, the Court would readily find that Mr. Fox's analysis and the Receiver's arguments were correct and that no disabling conflict existed.

The CFTC takes the position that Mr. Hodgson, as a court-appointed receiver, is subject to a higher standard of conduct with respect to handling conflicts of interest than that applied to private attorneys. The CFTC contends the Receiver is in a position similar to a bankruptcy trustee and has the duty to avoid even the appearance of possible impropriety, unfairness or partiality. As such, the Receiver and any counsel employed by him were obligated to fully disclose to the Court his and his firm's prior relationships with certain UBS entities, which the CTFC characterizes as a potential conflict of interest, and their failure to do so created an appearance of impropriety affecting the integrity of these proceedings. The CFTC concludes that the Receiver and his counsel should therefore be removed and a new Receiver appointed.

Man takes a position similar to the CFTC and relies in great part on the expert report of Professor Charles Wolfram. Professor Wolfram, **[*20]** also an esteemed and well known expert in professional responsibility matters, has authored several written opinions submitted to the Court on this matter, concluding that Mr. Hodgson and his firm should be disqualified because their prior client relationship with other UBS entities prevents them from performing independent services for the benefit of investors, and that they would be unable to act zealously on behalf of the Offshore Fund.

Both the CFTC and Man rely in part on cases decided in the bankruptcy context, and specifically, with reference to *Federal Rule of Bankruptcy Procedure 2014*, [7] **[*21]**

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(2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

(b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:

(1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;

(2) the representation is not prohibited by law;

(3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and

(4) each affected client gives informed consent.

[6] Comment 34 to Rule 1.7 provides:

HN3[⬆] A lawyer who represents a corporation or other organization does not, by virtue of that representation, necessarily represent any constituent or affiliated organization, such as parent or subsidiary. See Rule 1.13(a). Thus, the lawyer for an organization is not barred from accepting representation adverse to an affiliate in an unrelated matter, unless the circumstances are such that the affiliate should also be considered a client of the lawyer, there is an understanding between the lawyer and the organizational client that the lawyer will avoid representation adverse to the client's affiliates, or the lawyer's obligations to either the organizational client or the new client are likely to limit materially the lawyer's representation of the other client.

[7] *Bankruptcy Rule 2014(a)* provides:

(a) Application for an order of employment

An order approving the employment of attorneys, accountants, appraisers, auctioneers, agents, or other professionals pursuant to *§ 327*, *§ 1103*, or *§ 1114* of the Code shall be made only on application of the trustee or committee. The application shall be filed and, unless the case is a chapter 9 municipality case, a copy of the application shall be transmitted by the applicant to the United States trustee. The application shall state the specific facts showing the

which requires a detailed disclosure of representations, affiliations and other potential interests for a professional who is to be employed by a trustee or committee, and *11 U.S.C. § 327(a)* [8], which governs employment of professionals by a bankruptcy trustee. The bankruptcy cases generally hold that a failure of disclosure in this regard may merit disqualification.

III. *Legal Discussion*

The situation now before the Court does not fit precisely under either Rule 1.7 or bankruptcy doctrine. The issue here is not whether the Stradley firm took on a representation adverse to an affiliate of an existing client. The Stradley firm is representing the Receiver, who was for many years a partner in the firm and is now of counsel and still does work for clients of the Stradley firm, including UBS Financial Services. Although a client, the Receiver is also an attorney with the firm. Thus, Stradley's attorney-client relationship with the Receiver presents no conflict or even a potential conflict between the Stradley firm and any other **[*22]** clients. The Court cannot look at this matter exclusively as an issue of whether the Receiver in his role as an attorney and the Stradley firm have a conflict. For this reason, Rule 1.7 can only provide a reference, but not a final answer, as to whether the Receiver and his firm met their duties of disclosure to this Court.

Furthermore, this is obviously not a bankruptcy proceeding, and *Rule 2014* and *§ 327(a)* are inapplicable for that reason. It would therefore be unfair to decide this issue by reliance on the bankruptcy code or rules alone.

Hodgson's status as a court-appointed equity receiver changes the equation. As previously noted, *see* Memorandum of April 3, 2007 (Doc. No. 352 in the CFTC action), the Receiver is a fiduciary to the Court and to the investors, appointed on motion of the CFTC. Case law concerning receivers is therefore most applicable. Some bankruptcy cases, which discuss the duty of receivers and trustees appointed in bankruptcy proceedings, are relevant on the general policy factors, independent of *§ 327(a)* and *Rule 2014*.

In reviewing the case law on the issues raised by the various parties, and having received numerous briefs on the issue, neither the **[*23]** Supreme Court nor the Third Circuit have issued any specific holdings which govern the factual situation now before the Court. The general case law concerning court supervision of court-appointed receivers notes that ***HN4***[⬆] the court's actions with respect to the receiver are reviewed under an abuse of discretion standard.

Two Second Circuit cases provide helpful analysis. One deals with court-appointed receivers outside of a bankruptcy context; the second deals with a law firm's failure to sue a potentially responsible party in a bankruptcy case due to a conflict. We emphasize that the individual facts in these cases are egregious, and do not apply to the Receiver in this case, but the principles discussed cannot be ignored. The first case is *Phelan v. Middlestates Oil Corp., 154 F.2d 978 (2d Cir. 1946)*. Although the facts of this lengthy decision are largely inapposite, the court did set forth, in reliance on earlier Supreme Court cases, the general principles applicable to the appointment of a receiver:

> ***HN5***[⬆] A receiver, as 'an officer or arm of the court,' is a trustee with the highest kind of fiduciary obligations. He owes a duty of strict impartiality, of 'undivided **[*24]** loyalty,' to [all] persons interested in the receivership estate, and must not 'dilute' that loyalty. He is 'bound to act fairly and openly with respect to every aspect of the proceedings before the court. . . . The court, as well as all the interested parties,' have 'the right to expect that all its officers,' including the receiver, will not 'fail to reveal any pertinent information or use their official position for their own profit or to further the interests of

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> necessity for the employment, the name of the person to be employed, the reasons for the selection, the professional services to be rendered, any proposed arrangement for compensation, and, to the best of the applicant's knowledge, all of the person's connections with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee. The application shall be accompanied by a verified statement of the person to be employed setting forth the person's connections with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee.

[8] *Section 327(a)* provides:

> Except as otherwise provided in this section, the trustee, with the court's approval, may employ one or more attorneys, accountants, appraisers, auctioneers, 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.

> themselves or any associates.' A receiver has the 'affirmative duty to endeavor to realize the largest possible amount' for assets of the estate. If he has vital information which, if disclosed, might bring a better price for property which is sold pursuant to court order, he must fully disclose it 'prior to the sale when the prospects (are) greater for successful bargaining.'

Id. at 991 (internal quotation omitted).

In *Phelan*, it appeared that the receiver had previously represented interests potentially in conflict with those of the bondholders he represented in his role as a receiver. The court considered an argument as to whether a specific New York law would excuse the high standards **[*25]** the court held federal law applies to receivers. In rejecting this argument, the court noted the special status of a receiver expresses a different consideration from that applied to an ordinary trustee:

> HN6[] A claim against a derelict receiver is not against an ordinary trustee but against a court's officer. Who has the right to assert such a claim is a question affecting the integrity of the court itself. The federal courts, in holding their own officers to accountability, should not be hampered by state court decisions relating to ordinary trustees. . . . When a federal receiver incurs obligations through misconduct, the title thereto is, we think, similarly to be determined by 'federal law.'
>
> . . .
>
> The doctrine, relative to receivers, of strict accountability, and of opposition to divided loyalties, is prophylactic; it aims not merely to punish actual evil in cases where it occurs but to avoid the 'tendency to evil in other cases.'

Id. at 1000-1001 (footnotes and citations omitted).

The second case is Bohack Corp. v. Gulf & W. Indus., Inc., 607 F.2d 258 (2d Cir. 1979). Although this case arose out of a bankruptcy proceeding, **[*26]** and the facts contain egregious circumstances of wrongdoing not present in this case, the legal focus is relevant because the court found that the law firm appointed as special counsel for the debtor in possession had failed to sue a specific defendant. The bankruptcy judge found the law firm's decision was tainted by a conflict and disqualified the special counsel, but the district court reversed this holding. The Second Circuit, in turn, reversed and upheld the disqualification decision of the bankruptcy court.

The facts showed that the law firm had failed to sue a particular defendant with which the a partner in the firm had a close personal friendship and business association, and this had prejudiced the investors. The court concluded as follows:

> We have indeed been loathe to separate a client from his chosen attorney where the alleged misconduct does not prejudice an opposing party and taint the litigation in which he is appearing. The delay and additional expense created by substitution of counsel is a factor to which we have attached considerable significance in these cases. *See*, *e.g.*, Lefrak v. Arabian American Oil Co., 527 F.2d 1136, 1138-40 (2d Cir. 1975). **[*27]**
> However the disqualification here does involve a conflict of interest which goes to the core of the pending state action and which prejudices the defendants since it was authorized by the Bankruptcy Court only if appropriate. The conflict found by the Bankruptcy Court affects not merely a determination of the proper defendants in the action but whether it should have been commenced in the first place. Moreover, counsel here was not simply the choice of the client but was confirmed by the court. As such he is answerable not only to his client but to the Bankruptcy Court as well. Under these circumstances the possible delay and additional expense caused by replacement are clearly outweighed by considerations of the integrity of the judicial process. We find therefore no abuse of discretion in Judge Parente's determination that [the law firm] be removed as special counsel in the state court action.

Id. at 264.

Two other cases, although arising in the bankruptcy context, also shed light on the obligations placed on an attorney acting in the position of a fiduciary or trustee and the consequences of failing to conform to those obligations. In *In re The Leslie Fay* **[*28]** , a federal bankruptcy judge addressed a motion to disqualify a Chapter 11 debtor's counsel because the law firm had failed to disclose potential conflicts to the court when it initially sought to be appointed. *See* In re The Leslie Fay Cos., 175 B.R. 525 (Bankr. S.D.N.Y. 1994). Several months into the proceeding, an official committee of unsecured creditors began raising questions about the law firm's disinterestedness, and the bankruptcy court

appointed an examiner to look into those allegations. The examination revealed that the law firm had several relationships with members of the debtor's Audit Committee and with one of the debtor's largest creditors that, according to the examiner, if known, would have "cast substantial doubt on whether [the law firm] could conduct a fair and impartial investigation for the Audit Committee." *Id. at 530*. The law firm had failed to disclose any of these relationships in its retention affidavit submitted to the court and claimed, when these omissions were brought to light, that it did not have a conflict of interest and had met its disclosure obligations. *Id. at 534*.

Rejecting this rationale, **[*29]** the court noted, "[i]t was for the court, and not [the law firm], to determine whether in fact a conflict existed and, if so, what the remedy should be. The 'decision should not be left to counsel, whose judgment may be clouded by the benefits of potential employment.'" *Id. at 536* (internal quotation omitted). The court in *Leslie Fay* found that the law firm had failed to meet its disclosure obligations under the bankruptcy code and noted the very real harm that resulted from that non-disclosure, including the lengthy examination that had to be conducted into the allegations of a conflict. In fashioning a remedy, the court observed that, because the debtor was at the "critical juncture" in its reorganization efforts and would probably be unable to withstand the costs and delay caused by the departure of its longstanding counsel, it would allow the law firm to remain in the case to complete what it had begun. At the same time, the court ordered that new counsel must be brought in "to handle new matters such as litigation regarding claims, any avoidance actions and suits for relief arising out of the accounting regularities." *Id. at 539*. It reached **[*30]** this decision even though the court recognized the law firm had carried out its duties properly. The court dictated the law firm must bear its own expenses in educating any new counsel on the case and, moreover, it ordered the law firm to disgorge the costs resulting from the examiner's investigation and the failure to disclose. *Id.*

The *Leslie Fay* decision has implications beyond the bankruptcy setting. As the court in *Leslie Fay* observed, ***HN7***[] "where the choice of counsel must be approved by a court as appropriate, such that the integrity of the judicial process is implicated, the cost and delay of replacing counsel with a conflict of interest may be outweighed." *Id. at 538*.

Similar issues were raised by a case brought in the Northern District of Illinois involving a law firm's representation of a debtor in a bankruptcy proceeding. In *In re Envirodyne Industries, Inc.*, an unofficial committee of noteholders brought a motion to disqualify the debtor's counsel in a bankruptcy proceeding, and the United States Trustee brought a separate motion to reconsider the order authorizing the law firm's employment. *See In re Envirodyne Industries, Inc., 150 B.R. 1008 (Bankr. N.D. Ill. 1993).* **[*31]** In that case, the law firm had an ongoing and longstanding client relationship with a majority shareholder of the debtor's parent company that was also a creditor of the debtor. The firm did not disclose the relationship to the court when it sought employment in the bankruptcy proceeding.

The district court found that the law firm's representation was an actual conflict under the bankruptcy code and vacated its previous order appointing the firm as the debtor's counsel. In so deciding, it rejected the law firm's argument that concurrent representation in the bankruptcy context may sometimes be appropriate, "[m]ultiple representations which may be tolerable in a commercial setting after full disclosure are not permissible in a bankruptcy setting." *Id. at 1018*. The court further rejected the law firm's contention that any litigation against the creditor is a "remote contingency" therefore not impairing its ability to represent the debtor and noted that "this statement alone is evidence of a bias and demonstrates the [law firm's] already formed belief that [the client] has no liability to the estate." *Id. at 1019*.

In evaluating the implications **[*32]** of the firm's failure to disclose this information, the court noted that failure to disclose alone "is enough to disqualify a professional and deny compensation, regardless of whether the undisclosed connections were material or de minimus." *Id. at 1021*. Notwithstanding the law firm's assertions that it has acted with neutrality and vigorously represented the debtors up until that point, "it's is the court's role and not [the firm's] to determine whether a disqualifying conflict of interest exists." The court concluded that the law firm's vigorous representation of the debtors was irrelevant to a determination of whether it complied with the bankruptcy code and rules. *Id. at 1021*.

The Court also relies on another case arising in the bankruptcy context, which the Master quoted extensively in his report, *In re BH & P, Inc., 949 F.2d 1300 (3d Cir. 1991)* which emphasized the need to develop a remedy based on fact specific inquiry in which the "judge be given an immediate opportunity to make

an intelligent appraisal of the situation and to apply his experience, common sense, and knowledge of the particular proceeding to the request. **[*33]** " *Id. at 1312*. After reviewing the facts of that case, the Third Circuit affirmed the bankruptcy court's decision and the district court's affirmance of that decision to disqualify the trustee.

IV. *Analysis*

After recognizing these general principles, based on inapposite facts, this Court must take into consideration the Receiver's arguments that no significant damage has been done to the receivership efforts in this case. In coming to a decision, the Court must balance the lack of disclosure about UBS Cayman and consider how serious it is in the context of the actual events that have unfolded, and whether any party will be prejudiced [9] or whether the integrity of the proceedings themselves will be subject to question after the case is completed. Considering this matrix of various interests, the Court believes that it should also consider the interests of the investors, the position of the CFTC as the government agency designated by Congress with regulatory authority over futures markets (a multi-billion dollar industry), and the interests of the public.

[*34] Starting with the well known proposition that disqualification is disfavored, a change in Receiver and/or his counsel would require delay in the progress and ultimate termination of the case and additional expense incurred by appointment of a new Receiver. As stated in open court several times, the Receiver is a highly regarded and highly reputable attorney with experience in complex cases. The Stradley firm has done a very satisfactory job in the performance of its professional responsibilities as counsel for the Receiver -- as evidenced by a high degree of diligence in the handling of the cases before the Court, with well prepared briefs and highly respectable motions on matters ranging from discovery to more substantive motions.

The Court also considers potential downstream impact of the current situation, in which UBS Cayman is a party in the case. [10] Fast forwarding to the end of the case, let us assume that the case has continued to trial with UBS Cayman as a third-party defendant, Man has been found liable for significant damages, but has been unsuccessful in its third-party claim against UBS Cayman. In post-trial motions and/or on appeal, assume Man argues that the Receiver **[*35]** and his counsel, because of allegiances to other UBS entities, and although playing "hardball" against Man (as the Receiver is expected to do), framed questions and arguments to the jury in such a way as to encourage the jury to impose liability only as to Man and to prejudice Man's third-party claim against UBS Cayman.

It is, of course, possible that Man is exclusively liable and that UBS Cayman has no liability whatsoever. However, in the hypothetical situation posited above, including a large jury verdict against Man and the jury's exoneration of UBS Cayman, the judgment may be subject to attack and reversal because of the underlying **[*36]** facts concerning the Receiver's ongoing relationship with other UBS entities. Man's counsel has not shied from any arguments in favor of her client, cannot be expected to give up on the conflict issue, and the Court cannot conclude that such arguments are formalistic or frivolous.

The Court has also considered various other remedies to avoid disqualification. One would be a "Chinese wall" within the Stradley firm, but the Receiver was fully knowledgeable of and involved in representation of the UBS Financial Services relationship. Another remedy would be bifurcation of issues regarding UBS Cayman, but that may require two trials and additional expense.

After considering the facts, the law and the unique situation which is presented, the Court concludes that two issues provide the tipping point requiring disqualification of Mr. Hodgson but as to the Man litigation only. The first is the hypothetical posed above and the second is the position of the CFTC. As the government agency responsible for the institution of the case in which the Receiver was appointed, it has had numerous interactions with the Receiver over the course of this litigation, and has, for reasons which the

[9] Although Man injected this conflict issue into the case, and has submitted numerous arguments noted in the Master's Report and Memorandum, the Court gives its advocacy very little weight in view of the fact that the Receiver sued Man and contends Man is liable for significant damages. Man has an obvious motive to have Mr. Hodgson discharged.

[10] Although now designated as a third-party defendant brought into the case by Man, the Court noted the possibility of realigning UBS Cayman as a co-defendant to Man rather than as a third-party defendant, in which situation Man would be able to bring a crossclaim against UBS Cayman. UBS obviously opposes such a change in its status. What position Man would take on this is unknown.

Court **[*37]** cannot find vindictive or otherwise improper, maintained that the Receiver should be replaced, knowing of the detrimental impact this would have on the investors, if only because of the delay in the outcome.

Although not of such significant weight, there is potential prejudice to Man. Nonetheless, the overriding factor is the quite possible taint of the legitimacy of the verdict, which cannot be avoided if the current Receiver remains in place.

However, the factual situation only requires the Receiver be replaced as to the Man litigation. At the hearing on April 18, both counsel for Man and the CFTC agreed Mr. Hodgson could continue as Receiver for matters other than the Man litigation. In considering these potential downstream impacts, the Court concludes that the previously undisclosed relationship between the Receiver and UBS entities other than UBS Cayman is not something that can be ignored. The continued prosecution of the case by a Receiver with a history of UBS relationships cannot be squared with the goal of concluding this case free of any doubt as to whether these relationships have tainted the proceedings or prejudiced another party.

Although the Court is aware that **[*38]** after this possibility was posed to the Receiver's counsel at the last hearing, Receiver's counsel subsequently replied by letter that the Receiver would not want to continue in that capacity as to the non-Man litigation. However, the Court sees no justification for that position and believes that the Receiver and Stradley can continue their existing role on all aspects of this case except the Man litigation. There are proceedings in Canada, in the Cayman Islands and there is one other litigation pending in this district. The additional expense of appointing a new Receiver ad litem for the Man litigation only will itself cause added expense and the Court sees no reason why further additional expense would be required to replace the present Receiver as to the non-Man matters, and therefore, the Court will assume that Mr. Hodgson will continue in those roles.

However, the Court does not reach the same conclusion as to the Stradley firm continuing as counsel with the Man litigation, but reporting to a new receiver, a Receiver ad litem [11], who will have full and exclusive authority over the Man litigation, supervising counsel, communicating with investors, staying in liaison with the **[*39]** CFTC, while remaining ultimately responsible to this Court.

[*40] The Court finds that, once Mr. Hodgson is no longer the "client" of the Stradley firm, it is not in a conflict situation, under a careful review of Rule 1.7 and Comment 34. Thus, the Stradley firm, with the qualifications noted below, may continue to represent an independent Receiver ad litem under the specific facts of this case.

This Court exercises its considerable discretion for the following major reasons:

1. Stradley has significant knowledge of the case, acquired after almost two years as counsel to the receiver;

2. Stradley's performance, as noted above, has been

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[11] The Third Circuit in *Pressman-Gutman Co., Inc. v. First Union Nat'l Bank., 459 F.3d 383 (3d Cir. 2006)* discussed the differences between a court-appointed equity receiver and a guardian ad litem, although this discussion was largely dicta because of the court's ultimate determination that it did not have jurisdiction to hear the appeal. In that case, the plaintiff, the employer-sponsor of an employee profit-sharing plan, brought an interlocutory appeal seeking review of the district court's decision to disqualify its counsel because the counsel had also represented the plan's administrators, who had been brought into the case as third party defendants. The district court had removed the administrators and disqualified their counsel, and then appointed a guardian ad litem "who will replace the [administrators] and serve as administrator of the [P]lan for the limited purpose of this lawsuit" *Id. at 390*.

The plaintiff argued, among other things, that the district court had effectively appointed a receiver, not a guardian ad litem, giving the Third Circuit jurisdiction to hear the appeal under *28 U.S.C. § 1292(a)(1)-(2)*. The Third Circuit rejected this argument, reasoning that such an interpretation "would effectively eliminate the distinction between guardians ad litem and receivers, and, for that matter, between fiduciaries and receivers." *Id. at 394*. The court emphasized the limited nature of the duties of the guardian ad litem, "we note that even though the guardian ad litem has control over the cause of action in this case, there remain myriad duties, functions and responsibilities related to managing the Plan's assets over which the guardian ad litem does not have any control. For this reason, the district court's orders do not amount to orders appointing a receiver for the Plan . . ." *Id. at 394 n.10*. Because Mr. Hodgson will retain his position as Receiver in all other proceedings except for the Man litigation, the term "Receiver ad litem" is therefore appropriate to refer to the role that will be played by Mr. Hodgson's replacement in the Man litigation. The Court reiterates that is has no views as to the merits of the Man litigation.

very satisfactory;

3. Stradley has been paid significant sums, approximately two million dollars, and to replace it completely with another firm would require an additional expenditure of a similar proportion, as well as a substantial delay in this case. [12]

The responsibilities of the Receiver ad litem will be, generally, as follows, which duties **[*41]** may be supplemented or amended as the Man litigation continues:

1. continue to employ the Stradley Firm as counsel on the Man litigation, at least for purposes of continuing to complete expert reports and discovery (which are presently ongoing), and briefing on dispositive motions;

2. consult with Mr. Hodgson as to his views on all aspects of the Man litigation;

3. independently investigate and arrive at an independent judgment as to what course of action should be taken with regard to UBS Cayman in this case, moving forward;

4. develop a settlement strategy, and communicate as appropriate with counsel for other parties and Magistrate Judge Strawbridge;

5. prepare for trial, in the event that the decisions on dispositive motions will require a trial, that will not be substantially delayed from the current schedule;

6. prepare, in conjunction with Mr. Hodgson and counsel, the litigation budgets on a quarterly basis, which may be submitted to the Court in whole in or part in camera;

7. employ counsel of his choosing to work with the Stradley firm, as long as Stradley remains counsel in the Man litigation. This new counsel will exclusively advise the Receiver ad litem as to **[*42]** UBS Cayman issues;

8. the Receiver ad litem shall determine the responsibilities of counsel for trial preparation and the trial, if the case proceeds to tria,l particularly on UBS Cayman issues. [13]

The Court believes that the above determination of this issue is feasible and fair, and that it will ensure the integrity and finality of the proceedings in this Court **[*43]** and that all parties be treated fairly. The Court will retain responsibility to ensure that the Man case is litigated these principles in mind.

The Court believes that the appointment of the Receiver ad litem, and conscientious supervision of counsel from Stradley along with counsel selected by the Receiver ad litem, will allow this case to move forward towards conclusion in an expeditious manner that is appropriate for all parties. [14]

ORDER

In accordance with the foregoing memorandum, the Court appoints Stephen J. Harmelin, Esq. [15] as Receiver ad litem for all purposes of Civil Action 06-1944 only, in place of C. Clark Hodgson, Jr., Esq., who shall continue **[*44]** as Receiver for all other purposes. The Court will schedule a pretrial conference on scheduling issues for Monday, May 14, 2007 at 10:00am.

BY THE COURT:

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[12] A similar result for similar reasons was reached in *Leslie Fay, supra.*

[13] Specifically with regard to the hypothetical posed above, concerning UBS Cayman issues, the Court urges the Receiver ad litem to ensure that counsel other than the Stradley firm handle UBS Cayman issues at the trial, such as examination of any UBS Cayman witnesses, presentation of arguments to the Court and jury concerning UBS Cayman, and, if necessary and appropriate, taking charge of any specific claims against UBS Cayman on behalf of the Receiver ad litem. This Court has approved a similar arrangement of co-counsel handling specific witnesses in a criminal case. *See United States v. Hawkins, 2004 U.S. Dist. LEXIS 17732, 2004 WL 2102017 (E.D. Pa. 2004)*.

[14] The Court takes no position at this time as to any allocation of costs incurred by the Receivership estates because of additional counsel fees resulting from this situation. The Court requests the Receiver to supply a summary of accounts, showing all income, disbursements and funds on hand, as of April 30, 2007, or as soon as available.

[15] The Court has informed counsel for the CFTC as to the conclusions reached and the identity of the Receiver ad litem and his responsibilities, including his supervision of counsel. CFTC counsel shall serve their letter of May 2, 2007 on all counsel. Mr. Harmelin has alerted the Court that his firm, but not himself, has represented a UBS entity in isolated bond financing transactions but has not represented UBS Cayman, and, the firm will not accept any further representation of any UBS entity while this case is pending.

Date: 5/3/07

/s/ Michael M. Baylson, U.S.D.J.

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Hilti, Inc. v. HML Dev. Corp.

Superior Court of Massachusetts, At Worcester

February 5, 2007, Decided ; February 13, 2007, Filed

Opinion No.: 97271, Docket Number: 98-01029-B

Reporter
2007 Mass. Super. LEXIS 66 *; 22 Mass. L. Rep. 208

Hilti, Inc. v. HML Development Corp.

Core Terms

receivership, appointment, mortgage, Interim, fiduciary, Replace, Intervene, escrow, rents, Reconsideration, notice, foreclose, disbursements, foreclosure, vacation, Monthly, hiring, default, Contempt, liquidate, hourly, unliquidated, equitable, promptly, fulfill, sponte, rata, sua

Case Summary

Procedural Posture

Plaintiff creditor filed an action against defendant contractor asking the court to appoint a receiver for the contractor pursuant to *Mass. Gen. Laws ch. 156*(b), *§ 105*. Before the court were the contractor's motion to remove the receiver, an emergency motion to reconsideration staying two prior orders filed by the creditor's attorney, and motions to reconsider the escrow of fees by the creditor's attorney and the receiver.

Overview
The creditor secured a judgment against the contractor, and the receiver, who had over 30 years of experience receivership, was appointed to assist in collecting on the judgment. The court ordered that the receiver be replaced because he failed to properly carry out his statutory duty to expeditiously liquidate the assets of the contractor and make prompt payments to creditors, failed to adequately scrutinize the highly questionable request for payment of fees and expenses by the creditor's attorney, failed to ask the court for permission to hire attorneys to assist him and then billed the receivership estate for their time, failed to ask court permission to have the creditor's attorney act as receiver when he was on vacation, breached his duty to the contractor by submitting an affidavit for the creditor's attorney advocating the imposition of treble damages against the contractor in another case, acted improperly by employing the husband of an associate in his firm to act as property manager of a property owned by the contractor, and failed to provide the court with a detailed inventory of possessed property, or property as to which the receiver had a right to possession.

Outcome
The contractor's motion to replace the receiver was allowed. The emergency motion to reconsideration staying two prior orders was denied. The motions for reconsiderartion of the escrow of fees were denied. The receiver was discharged and a new receiver was appointed.

LexisNexis® Headnotes

Business & Corporate
Law > Corporations > General Overview

Civil Procedure > Parties > Real Party in Interest > Required Representation

HN1[] Business & Corporate Law, Corporations

A defendant corporation may not be represented in judicial proceedings by a corporate officer who is not licensed to practice law. It is well settled law in Massachusetts that corporations must appear and be represented in court, if at all, by attorneys. Individuals that accept the benefits of incorporation must bear the burden of hiring counsel to sue or defend in court. A defendant who fails to file an answer is subject to entry of default and a judgment of default. Mass. R.Civ.P. 55(a), 55(b).

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Appointment of Receivers

HN2[] Receiverships, Appointment of Receivers

A receivership is a prophylactic measure to protect assets in the event a particular creditor can prove that corporation is liable on a debt. The appointment of a Receiver for a domestic corporation rests within the sound discretion of the court, and should be exercised where it appears that the corporate property would be subject to waste or loss in the absence of a Receiver thereby impairing the ability of the corporation to pay its debts.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Appointment of Receivers

HN3[] Receiverships, Appointment of Receivers

A statutory Receiver may be appointed and dismissed only by order of the court. Mass. R.Civ.P. 66(a), Mass. Super. Ct. R. 51. A statutory Receiver may be appointed under Mass. Gen. Laws ch. 156B, § 105, If a judgment has been recovered against a corporation and it has neglected for 30 days after demand made on execution to pay the amount due with the officer's fees, or to exhibit to the officer real or personal property belonging to it and subject to be taken on execution sufficient to satisfy the same and the execution has been returned unsatisfied, one or more Receivers may be appointed with the powers and duties provided in, and subject to, Mass. Gen. Laws ch. 156B, § 104. For a court to grant the request of a creditor for the appointment of a statutory Receiver, there must be a valid unpaid judgment against the corporation. A creditor does not qualify as a "judgment creditor" until the judgment enters.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Appointment of Receivers

HN4[] Receiverships, Appointment of Receivers

The objective of the Receiver should be that of estate maximization. The objective of estate maximization is also secured in part by the "safeguard of court oversight" of any actions taken by a Receiver. Under the statute the Receiver has a duty to pay all debts due from the corporation if the funds in their hands are sufficient, and if they are not, to distribute the funds ratably among the court-approved creditors. Mass. Gen. Laws ch. 156B, § 106. If there is a balance remaining after the payment of the debts, the Receivers shall distribute and pay it to those who are justly entitled thereto as having been stockholders of the corporation, or their legal representatives. Ordinarily, the sale of assets should be upon such terms and conditions as will, within a reasonable time, convert the assets to cash and bring about a distribution of such assets to creditors and stockholders. It is the duty of the Receiver to determine the validity and the preference to be accorded to the claims of creditors. It is of paramount importance that during this process that the Receiver ensures that the creditors receive equality of treatment so far as is permissible under the law.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Appointment of Receivers

HN5[] Receiverships, Appointment of Receivers

Within 30 days of appointment, the Receiver must provide the court with a detailed inventory of possessed property, or property as to which the Receiver has a right to possession. Mass. R.Civ.P. 66(b) and Mass. Super. Ct. R. 51. This list must include a list of encumbrances on said property, along with estimated values. Mass. R.Civ.P. 66(b). If this cannot be accomplished within 30 days, the Receiver may seek an

extension of time from the court. The Receiver must also provide to the court a list of all known creditors, along with a list of those whose property is being held by the Receiver. The Receiver must file, not later than the fifteenth day of February of each year, a detailed account under oath, together with a report of the "condition of the receivership." Mass. R.Civ.P. 66(c). Further accounts and reports may be ordered by the court, although the court may relieve the Receiver of this requirement. Mass. R.Civ.P. 66(b) and (f). Once a Receiver distributes all of the assets of the corporation, the Receiver files the final account of the assets with the court and the court then discharges the Receiver. Mass. R.Civ.P. 66(e) and Mass. Super. Ct. R. 51. Both Mass. R.Civ.P. 66(d) and Mass. Super. Ct. R. 51 limit the ability of a Receiver who is an attorney from employing an attorney without order of the court.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Appointment of Receivers

HN6[] Receiverships, Appointment of Receivers

A court-appointed Receiver is a "full-fledged fiduciary." A Receiver does not act solely as the agent of the company for which they have been appointed Receiver. A Receiver is a representative of the court and of all parties with an interest in the litigation. Thus, a Receiver owes fiduciary duty to all the parties in interest, including the creditors and the shareholder(s), and is under the duty to act impartially toward, and protect the rights of, all parties.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Appointment of Receivers

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Liability of Receivers

HN7[] Receiverships, Appointment of Receivers

Due to the fiduciary nature of his or her duty to the parties, a Receiver is not permitted to deal with the trust estate for his or her own benefit and advantage. As a fiduciary, a Receiver must avoid all conflicts of interest, and cannot derive personal profit from the appointment, other than reasonable compensation. Under certain circumstances a Receiver may be held personally liable by the court for failure to properly perform his or her duties as Receiver.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Administrative Expenses & Fees

HN8[] Receiverships, Administrative Expenses & Fees

The compensation to be paid to a Receiver is not regulated by a fixed commission of the money that passes through his or her hands, but rather, what would be a reasonable fee for the services required and rendered by a person of ordinary ability and competent for such duties and services. What is a reasonable fee is a question that is to be determined by the sound discretion of the judge.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Administrative Expenses & Fees

HN9[] Receiverships, Administrative Expenses & Fees

In determining whether the fee paid to a Receiver as compensation for work done is reasonable a number of factors must be taken into consideration, including, the nature of the case and the issues presented, the time and labor required, the amount of damages involved, the result obtained, the experience, reputation and ability of the attorney, the usual price charged for similar services by other attorneys in the same area, and the amount of awards in similar cases. No single factor is determinative, and a factor-by-factor analysis, although helpful, is not required. In proving the amount of attorneys fees, contemporaneous time records, although not absolutely essential where there is other reliable evidence to support the claim, are very important.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > General Overview

HN10[] Dissolution & Receivership, Receiverships

In making a determination as to whether the Receiver should be removed, the court does not view each incident of alleged impropriety in isolation, but rather as a whole.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > General Overview

HN11 **Dissolution & Receivership, Receiverships**

When a Receiver requires another attorney to help him or her work on a receivership case, he or she is required to petition the court, stating the name of the attorney whom the Receiver desires to employ and showing the necessity of such employment. Mass. R.Civ.P. 66(e) and Mass. Super. Ct. R. 51.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > General Overview

HN12 **Dissolution & Receivership, Receiverships**

Both Mass. R.Civ.P. 66(d) and Mass. Super. Ct. R. 51 limit the ability of a Receiver who is an attorney from employing an attorney without order of the court. In the absence of such permission a person furnishing services to the receivership estate is a mere volunteer and cannot recover for such services. The court may allow a creditor petitioning for the appointment of a Receiver reasonable costs, including fees.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Appointment of Receivers

HN13 **Receiverships, Appointment of Receivers**

See Mass. R.Civ.P. 66(d) and Mass. Super. Ct. R. 51.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Appointment of Receivers

HN14 **Receiverships, Appointment of Receivers**

As a general rule, a court should not authorize the employment by the Receiver of an attorney who has been representing any of the parties, or whose interest is opposed to that of a party to the receivership. However, some courts have carved out an exception to the general rule, when there is a perfect identity of interests between the plaintiffs and the Receivers or where the parties have consented.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Appointment of Receivers

Legal Ethics > Client Relations > Conflicts of Interest

HN15 **Receiverships, Appointment of Receivers**

An attorney may not simultaneously represent differing interests that are adverse to one another, unless both parties consent to the dual representation. Massachusetts follows this rule, on the ground that the undivided loyalty that a lawyer owes to his or her client forbids the lawyer, without the client's consent, from acting for the client in one action and at the same time against the client in another action, even if the lawsuits are unrelated in subject matter. A lawyer shall not continue multiple employment if it would be likely to involve the lawyer in representing differing interests.

Legal Ethics > Client Relations > Conflicts of Interest

HN16 **Client Relations, Conflicts of Interest**

Mass. R. Prof. C. 1.7 states that a lawyer shall not represent a client if the representation of that client will be directly adverse to another client unless 1) the lawyer reasonably believes the representation will not adversely affect the relationship with the other client, and 2) each client consents after consultation. *Mass. R. Prof. C. 1.7(a)*. In addition a lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client, unless: 1) the lawyer reasonably believes the representation will not be adversely affected, and 2) the client consents after consultation. *Mass. R. Prof. C. 1.7(b)*. When an attorney represents multiple clients in a single matter the consultation shall include explanation of the implications of the common representation and

the advantages and risks involved. *Mass. R. Prof. C. 1.7(b)(2)*.

Legal Ethics > Client Relations > Conflicts of Interest

HN17 **Client Relations, Conflicts of Interest**

With respect to *Mass. R. Prof. C. 1.7(b)*, loyalty to a client is considered to be impaired when the lawyer cannot consider, recommend or carry out an appropriate course of action for the client because of the lawyer's other responsibilities or interests. *Mass. R. Prof. C. 1.7*, cmt. 4. Thus the crucial questions are: (1) the likelihood that a conflict would arise; (2) whether the conflict would materially limit the lawyer's independent professional judgment. *Mass. R. Prof. C. 1.7*, cmt. 4. Although due consideration should be given to whether the client wishes to accommodate the other interest involved. However a lawyer may not ask for a client to consent to a conflict when a disinterested lawyer would conclude that the client should not agree to the representation under the circumstances. *Mass. R. Prof. C. 1.7*, cmt. 5. When a conflict exists before the representation of the client exists, the representation should be declined. *Mass. R. Prof. C. 1.7*, cmt. 1. If the conflict arises after representation has begun, the lawyer should withdraw from the representation. *Mass. R. Prof. C. 1.7*, cmt. 2.

Business & Corporate Law > ... > Dissolution & Receivership > Receiverships > Payment & Presentation of Claims

HN18 **Receiverships, Payment & Presentation of Claims**

Pursuant to *Mass. Gen. Laws ch. 156B, § 106*, a Receiver is required to distribute the funds ratably among the court approved creditors.

Civil Procedure > ... > Service of Process > Proof of Service > General Overview

Civil Procedure > ... > Service of Process > Methods of Service > General Overview

HN19 **Service of Process, Proof of Service**

Under *Mass. R.Civ.P. 5(b)*, service may be made by mailing the paper to the party or attorney at his or her last known address; if no address is known, the paper may be left with the clerk of court. Notice is complete upon depositing the correctly addressed, postage prepaid notice in the mailbox. *Rule 5(d)* has been expanded to eliminate all formalities as to proof of service of papers upon other parties. If an adverse party challenges the adequacy of notice, the serving party will of course have to prove service. In order to minimize frivolous challenges, *Rule 5(d)* provides that a simple statement signed under the penalties of perjury will suffice to establish prima facie proof of service. The statement is designed to make explicit that the attorney's failure to supply proper proof of service does not invalidate the service if in fact it has been properly completed.

Judges: **[*1]** John S. McCann, Justice of the Superior Court.

Opinion by: John S. McCann

Opinion

MEMORANDUM OF DECISION AND ORDER ON DEFENDANT'S MOTION TO REMOVE RECEIVER

INTRODUCTION

Hilti, Inc. (Hilti) is represented by Jerrold N. Arnowitz, Esq. (Arnowitz). The receiver is Peter L. Zimmerman, Esq. (Zimmerman). HML Development Corp. d/b/a HML Development Company (HML) and James Xarras a/k/a Jimmy Xarras (Xarras) are represented by John M. Dombrowski, Esq. (Dombrowski).

BACKGROUND

This is a 1998 receivership collection case in which plaintiff, Hilti, Inc. ("Hilti") petitioned this court to appoint attorney Peter Zimmerman ("Zimmerman") to act as a statutory Receiver pursuant to *G.L.c. 156B § 105*, to assist in collecting on a judgment that Hilti secured against the defendant, HML Development Corp.

("HML").

Hilti is a foreign corporation having a usual place of business in Pittsburgh, Pennsylvania. HML was a closely held corporation and is a now defunct [1] Massachusetts corporation which had a usual place of business in Leominster, Massachusetts. HML formerly conducted business as a drywall contractor. James L. Xarras ("Xarras") was the sole shareholder, director and officer of HML. He is sometimes **[*2]** referred to as Jimmy Xarras.

The Complaint was filed on May 5, 1998. The receiver was appointed March 29, 1999.

In April 2006, seven years after Zimmerman's appointment as Receiver, HML filed a motion asking this court to replace the Receiver, alleging that Zimmerman, as receiver, and Hilti's counsel, had breached their fiduciary duty to HML, by conspiring to use the assets of the receivership to enrich themselves, while failing to liquidate and make timely payments to HML's creditors.

On May 15, 2006, the court, on a hearing for the approval of the fifth account by the receiver, ordered that the fees of Zimmerman and Arnowitz be placed in an interest-bearing escrow account with Arnowitz and Dombrowski as co-escrowees and fees of Zimmerman to be deposited likewise in that account until further order of the court without prejudice (Murphy, J.).

Murphy, J. referred **[*3]** the matter to the Regional Administrative Justice who at the time of the further hearing was McCann, J. After a hearing on September 19, 2006 (McCann, J.), the following motions were taken under advisement: (1) HML's Motion to Replace the Receiver; (2) Zimmerman's Motion for Reconsideration of the Escrow of his Fees; and (3) Arnowitz's Motion for Reconsideration of the Escrow of his Fees and Cross Motion for costs. [2] Now before the court is HML's Motion to Remove the Receiver and the Emergency Motion of Arnowitz for Reconsideration Seeking a Stay of the Court's Sua Sponte Order dated May 15, 2006 and the Court's denial of Arnowitz's Motion for Reconsideration. Arnowitz also filed a Notice of Appeal of the Order of McCann, J. dated March 13, 2006. For the following reasons HML's Motion to Replace the Receiver is allowed; Arnowitz's Emergency Motion In Reconsideration is denied; the Cross Motion of Arnowitz for Costs is denied; the Request for a Stay of the Order of Murphy, J. dated May 15, 2006 and the Order of McCann, J. dated November 9, 2006 are denied.

[*4] The District Court Judgment

On May 29, 1997, Hilti brought a breach of contract suit against HML in the Leominster District Court. On November 14, 1997, Hilti recovered a judgment in the amount of $ 26,139.99. The District Court issued an execution on November 24, 1997, execution issued and served on HML by service on Xarras on January 12, 1998. Neither HML nor Xarras on behalf of HML made any payments and failed to satisfy the execution within the required thirty (30) day period.

One year later, on May 5, 1998, Hilti filed this action in Worcester Superior Court against HML as the sole defendant, asking this court to appoint a Receiver [3] **[*5]** for HML pursuant to *G.L.c. 156B, § 105*. [4] Service was made on HML on May 8, 1998, with service returned on May 12, 1998. At the time this complaint was filed, Xarras was not named individually as a defendant in this action, and could not have been because he individually was not a judgment debtor. Hilti is represented in this action by Jerrold Arnowitz ("Arnowitz") of Arnowitz & Goldberg ("A&G") in Boston. [5]

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[1] HML ceased to accept business in mid-1996, and filed its final tax returns in 1996, although the corporation was never formally dissolved.

[2] On November 9, 2006, both Zimmerman's and Arnowitz's Motions to Reconsider were denied, McCann, J., and it was ordered that "deposits shall be made forthwith and that notice of the deposits shall be filed with the Court indicating the name, location and account number of the account." (McCann, J.).

[3] Receivers are now appointed from a court-approved list. However, at the time of the appointment of the Receiver in this case a court-appointed list did not exist, and counsel for the plaintiff could suggest the name of a Receiver for approval by the court. Arnowitz requested that Zimmerman be appointed as Receiver in this case.

[4] Under the statutory receivership protocol if a judgment has been recovered against a corporation and it has neglected for thirty days after demand made on execution to pay the amount due with the officer's fees, or to exhibit to the officer real or personal property belonging to it and subject to be taken on execution sufficient to satisfy the same and the execution has been returned unsatisfied, one or more Receivers may be appointed with the powers and duties provided in, and subject to section one hundred and four. See *G.L.c. 156B, § 105*.

[5] Arnowitz had been retained by another creditor of HML, Suffolk Construction ("Suffolk"), in April 1998. His relationship with Suffolk will be elaborated on hereinafter.

On May 21, 1998, Xarras, individually, filed a *pro se* answer to Hilti's complaint even though he was not named a party defendant. [6] On December 1, 1998, Hilti filed a Motion to Amend Complaint to Add Reach and Apply Defendant Xarras, individually. This motion was allowed on December 4, 1998, pursuant to *Superior Court Rule 9A*, with no **[*6]** opposition to the motion having been filed. At this point in the proceedings there does not appear there was any party who had been served to oppose the motion. It does not appear there was ever an attempt to make service on Xarras as a reach and apply defendant and the record does not reflect any service on Xarras.

The Appointment of Zimmerman as Receiver

Early on in the hearing for the appointment of a Receiver, the petition was continued a number of times between September 1998 and March 1999 for reasons not apparent on the record. The hearing on the appointment of a Receiver finally took place ten months after the filing of the Complaint on March 19, 1999. Hilti's motion to appoint Zimmerman of the law firm **[*7]** of Silverman & Kudisch, P.C. ("S&K") in Boston, was allowed (Toomey, J.). [7] Subsequently, Zimmerman filed a statutory receiver's bond of $ 500.00 with this court on March 29, 1999.

On April 14, 1999 Zimmerman notified Xarras by certified mail that he had been appointed as Receiver of HML by this court, and requested that all records and assets of HML be transferred to him by April 23, 1999. Zimmerman requested that Richard Kohn ("Kohn"), of Beacon Liquidators & Appraisers ("Beacon") visit the address of HML at 41 Balsam Drive, in Leominster. Kohn visited this address on April 29, 1999, and gave the company secretary the state receivership papers as Zimmerman requested. Not having heard from Xarras, Zimmerman sent another letter via certified mail on June 15, 1999, ordering Xarras to turn over all records and assets of HML by June 25, 1999. Xarras failed to comply with the court order.

The Assignment of Two HML Mortgages **[*8]** to Receiver

On November 9, 1999, Zimmerman filed a Receiver's Petition for Authorization to Receive Mortgage Payments Due HML and For Assignment of two (2) Mortgages. In this motion, Zimmerman stated he had examined the land records at the Worcester County Registry of Deeds, which had revealed that HML was the mortgagee on two separate properties, one in Westminster, and one in Fitchburg. A mortgage of $ 327,000 was given by HML to the Sargent Road Realty Trust [8] on March 9, 1992 on the property located at 88-100 Sargent Road, Westminster ("The Westminster Property"). The Westminster Property included apartment buildings of twelve units each and a restaurant.

The second mortgage in the amount of $ 1,232,071.00 [9] was given by HML to John C. Pappas and James C. Pappas ("Pappas Brothers") [10] on a property located at 19-49 Airport Road, in Fitchburg (the "Fitchburg Property"). The Fitchburg **[*9]** Property consisted of a strip mall known as Charles Park Plaza. Zimmerman requested that the two mortgagors be required to make their mortgage payments directly to him, and that said mortgages be assigned to him, with notice filed in the appropriate Registry of Deeds as these payments were assets of HML's and Xarras's estate. This request was allowed on March 24, 2000, upon motion filed in this court (Fecteau, J.).

Receiver's Motion for Contempt

On November 15, 1999, Zimmerman filed a Verified Complaint for Contempt against Xarras for failure to turn over all of HML's assets and books. A summons for contempt was issued on November 18, 1999, directing Xarras to appear for a hearing on Zimmerman's contempt motion on November 22, 1999. The hearing was continued until December 7, 1999, by agreement of the parties because Xarras desired to retain counsel. On December 7, 1999, Xarras failed to appear, and **[*10]** by default Zimmerman's Motion for Contempt was allowed.

On January 13, 2000, Hilti and Xarras filed an assented-to motion to remove the default, on the default entered

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[6] The docket entry incorrectly indicates that an Answer was received from "HML Development Corp (Defendant)" on May 21, 1998. The failure of HML, a corporation, to hire an attorney to represent it, and file an answer on behalf of the corporation defendant and HML will be elaborated on hereinafter.

[7] Silverman and Kudisch, P.C., 1320 Centre Street, Suite 203, Newton Center, MA 02459.

[8] A Massachusetts trust, under Declaration of Trust, a Massachusetts Trust, dated March 9, 1992, Louise M. Shea, Trustee.

[9] Dated January 17, 1991.

[10] The Pappas brothers, of Fitchburg, Massachusetts, are cousins of Xarras.

on Zimmerman's Motion for Contempt. HML & Xarras's motion was signed by attorney John M. Dombrowski ("Dombrowski"). [11] **[*11]** This motion was allowed on January 24, 2000. On February 28, 2000, Zimmerman filed a Motion for a Renewed Summons on Receiver's Complaint for Contempt. On March 10, 2000, Zimmerman filed a Motion for an Order Authorizing the Receiver to Enter the Premises of Petrullo Construction ("Petrullo"). Zimmerman stated that he had information that Petrullo had possession of equipment and other assets of HML that were being stored at a Petrullo facility. Petrullo failed to respond to Zimmerman's requests and the motion was allowed on March 24, 2000. [12] Petrullo was never added as a party in this action and the record does not reflect that it was served any documents by any party.

HML's Other Creditor: Suffolk Construction

Suffolk Construction ("Suffolk") and HML were involved in a breach of contract dispute that began in the early 1990s. On or about July 23, 1993, Suffolk filed suit against HML in Suffolk Superior Court [13] claiming damages in the amount of $ 122,745. The dispute was heard by a Special Master in October 1995, and on May 17, 1996, the Master entered judgment in favor of Suffolk in the amount of $ 469,706.00. Final judgment in that amount with interest at the rate of 12% from the date of the filing of the complaint and costs was entered on December 2, 1996 (Burnes, J.). On December 18, 1996, HML filed a notice of appeal, which was dismissed for lack of prosecution on January 7, 1998.

[*12] The Suffolk Case: Suffolk Attempts to Collect Judgment

In April 1998, Suffolk retained Arnowitz to help them collect the December 1996 judgment by filing an action in Suffolk Superior Court, *Suffolk Construction, Inc. v. HML Development Corp., James Xarras, Quintin Tigs et al*. (the "Suffolk case"). [14] Suffolk was also named as a reach and apply defendant. Suffolk was attempting to reach the assets of Xarras based upon claims of fraudulent transfers of corporate assets by Xarras, that Suffolk alleged had the effect of making HML insolvent. Arnowitz joined the law firm of Blank & Solomon ("B&S") as co-counsel to try the case. In September 2000, Zimmerman filed a Motion to Intervene [15] in the Suffolk case. The Suffolk case went to trial on or about January 21, 2003. In a decision, dated three years later on September 28, 2006, the court entered judgment in favor of HML on all of Suffolk's claims. On October 10, 2006, Suffolk filed a notice of appeal, which is still pending.

[*13] The Suffolk Case Decision

Although the Suffolk case decision is currently under appeal, certain findings from the Suffolk case are relevant to this case. The decision, among other things, stated that,

> On August 13, 1993, pursuant to an agreement between the parties, as prejudgment security HML assigned to Suffolk a first mortgage that it held on property located at 202 Park Avenue, Quincy, Massachusetts, [16] which mortgage has a face value of $ 220,000. In furtherance of this assignment, Suffolk and HML entered into an escrow agreement that provided for all mortgage payments to be held by an escrow agent pending the outcome of the case. The escrow agent was authorized, in the event of any default on the mortgage, to foreclose on the property and to hold all proceeds of the foreclosure pending the outcome of the case. [17]

On October 15, 1998, six months after the initiation of the Suffolk case, Suffolk received $ 44,212.17 **[*14]** from the escrow agent representing the mortgage payments receivable under the terms of the assignment made as prejudgment security. [18] The court noted that no explanation had been given for the ten (10) month delay in Suffolk receiving these funds, "which resulted in significant 12% interest unnecessarily being assessed against HML." [19]

On January 8, 1997 the Land Court issued a judgment permitting Suffolk to foreclose on the Quincy Property,

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[11] Dombrowski's Entry of Appearance is noted as January 13, 2000 on the docket, and this appears to be the first time that he appears for Xarras individually and HML in this case.

[12] In this hearing on March 24, 2000 Fecteau, J. also allowed Zimmerman's Motion to Receive Mortgage Payments and For Assignment of Said Mortgages as previously described.

[13] Suffolk Superior Court, Civil Action No. SUCV1993-04412.

[14] Suffolk Superior Court, Civil Action No. SUCV98-01235.

[15] This motion was granted on September 14, 2000.

[16] (the "Quincy Property").

[17] Memorandum of Decision, Pages 2-3.

[18] *Id.* at 11.

[19] Id.

but Suffolk did not foreclose on it until September 10, 1999, thirty-three (33) months later. The Quincy Property was sold at a foreclosure sale for $ 265,000, and these funds were paid to Suffolk on September 14, 1999. As a result, "by September 14, 1999, Suffolk had received a total of $ 309,212.17 on its judgment of $ 469,706," leaving a balance owed to Suffolk by HML of $ 160,493.83 [20] **[*15]** exclusive of interest. [21]

Receiver's Discovery of Additional Mortgage on the Fitchburg Property

On November 17, 2003, Zimmerman filed a 9(a) Motion for Authorization to Receive Mortgage Payments Due Defendant, for Turnover of Mortgage Proceeds Previously Received and For Assignment of Leases and Rents regarding the Fitchburg Property. In this motion Zimmerman stated that after the trial in the Suffolk case, he was informed by trial counsel, presumably Arnowitz, that there was an additional mortgage on the Fitchburg Property granted by the Pappas Brothers to HML. He stated that the additional mortgage "was on registered land and is part of the same parcel as the mortgage previously assigned to your Receiver in the recorded Land Court section of the Worcester County Registry of Deeds." In the motion Zimmerman stated that the additional mortgage on the Fitchburg Property "was dated January 17, 1999 and registered in the Land Court as Document No. 6020 from Pappas to HML to secure the payment of $ 1,232,071 with interest thereon." This motion was allowed on November 28, 2003 (Agnes, **[*16]** J.).

In its attempt to demonstrate that there is an additional mortgage, the motion refers to an attached Exhibit D, the Mortgage and Security Agreement. However the Mortgage and Security Agreement is dated January 17, 1991, not 1999, and appears to be exactly the same document that was used to refer to the first mortgage that was discovered on the Fitchburg Property. Thus it is not clear to this court whether in fact there was an additional mortgage on the Fitchburg Property, as represented to this court by Zimmerman.

The First Intervention of Nicole Moorshead as Trustee

On April 2, 2004 Nicole Moorshead ("Moorshead"), [22] as trustee of the Fitchburg Property, filed an Emergency Motion to Intervene, claiming that she had been the trustee since 2001, had managed the premises since the early 1990s, and was a tenant conducting business on the premises in question. Moorshead claimed that no debt was due HML. After a hearing on April 2, 2004, the motion to intervene was denied (Agnes, J.). Moorshead filed another Emergency Motion to Revoke Court's Order Granting Receiver Motion to Receive Mortgage Payments or in the Alternative, to Stay Implementation of Order, which was similarly denied **[*17]** the same day (Agnes, J.).

Receiver's Status Report

Zimmerman filed a Status Report on April 14, 2004 five years after his initial appointment as receiver. Zimmerman accounted for his actions to date by stating that he had obtained a list of all the tenants at the Fitchburg Property, and notified them that all rents and income should be paid to him. As of April 13, 2004, Zimmerman had received six rent checks from tenants, [23] and was attempting to determine the names and addresses of the remaining tenants who had not paid their rent to him.

Receiver's Foreclosure on the Westminster Property

Zimmerman became aware that Louise Shea had resigned as Trustee of the Sargent Road Realty Trust and had been replaced by Margo Xarras. On May 14, 2004, Zimmerman **[*18]** sent notice to Margo Xarras of his intention to foreclose on Westminster Property. On June 14, 2004, receiving no response to this notice, Zimmerman filed a motion requesting foreclosure on the mortgage from Sargent Road Realty Trust to HML at the Westminster Property, and for permission to use funds collected from the Fitchburg Property to cover his expenses incurred in the foreclosure proceeding. This motion was allowed on September 13, 2004 (McDonald, J.).

Zimmerman's First Application for Instructions

Zimmerman filed an Application for Instructions on July 13, 2004, five years after his appointment, requesting permission from the court to use rents received from the Fitchburg Property to pay the insurance and tax bills on that property, "bearing in mind that your Receiver has

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[20] Assuming 12 statutory interest on the $ 160,493.83 owed by HML as of September 14, 1999, HML would have owed the following to Suffolk: 9/1999: $ 160,493.83; 9/2000: $ 179,753.08; 9/2001: $ 201,323.46; 9/2002: $ 225,482.27; 9/2003: $ 252,540.14; 9/2004: $ 282,844.96; 9/2005: $ 316,786.36; 9/2006: $ 354,800.72.

[21] Memorandum of Decision, Page 11.

[22] Moorshead is Xarras's sister.

[23] The attached checks were valued at $ 13,860.75

never taken possession of the Premises as mortgagee in possession." On July 21, 2004, Moorshead, as sole beneficiary of the Charles Park Realty Trust at the Fitchburg Property, filed a statement in response to Zimmerman's Application for Instructions consenting to the payment of the outstanding tax and insurance bills on the Fitchburg Property, as such expenses were necessary to the continued operation of **[*19]** the plaza. This motion was allowed on September 3, 2004 (McDonald, J.). On July 13, 2004, Zimmerman also filed an application for an order requiring all governmental taxing authorities and general unsecured creditors of HML to file proof of claims. This motion was allowed on September 2, 2004 (McDonald, J.), five years after Zimmerman's appointment as receiver.

Attorney Arnowitz's Request for Fees and Expenses

On August 6, 2004, Arnowitz, and not Zimmerman who was receiver, filed a 9(a) Motion for Payment of Administrative Fees and For Monthly Interim Payments. [24] In this motion Arnowitz stated that to his knowledge only one other creditor of HML existed, which was Suffolk, whom he also represented. Arnowitz stated that as of June 14, 2004, HML owed Suffolk $ 1,020,584.32, [25] with a per diem interest of $ 335.53 or $ 122,470.10 per annum. [26] Arnowitz further stated that the assignment of the mortgage on the Fitchburg Property on April 11, 2000, had resulted in Zimmerman collecting rents from the tenants in the amount of $ 15,000-17,000 per month. However, despite the additional mortgage assignment to Zimmerman on the Westminster Property, no mortgage payments had been received from **[*20]** that property, and that Zimmerman was in the process of foreclosing on the mortgage after the Receiver's foreclosure motion was allowed on June 14, 2004.

Arnowitz stated that it would take seventeen years for the judgment against HML to be paid to Hilti, and that even if there was a foreclosure sale on the Westminster Property. It was his position;

> that after the administrative fees and expenses of the petitioning creditor, it's (sic) counsel, co-counsel and the Receiver are paid from the rental **[*21]** receipts and/or proceeds subject to foreclosure, then the Receiver should commence to pass the rental payments on the Airport Road property through to the creditors of HML and/or their attorneys . . . [27]

As such Arnowitz requested that this court: 1) authorize himself, as counsel for Hilti and intervening creditor Suffolk, and Zimmerman to file initial bills for professional services rendered; 2) that the Receiver Zimmerman be granted a cut-off date for all creditors of HML to come forward with proof of claims; and 3) after administrative payments had been paid, to begin paying the creditors of HML on a monthly basis.

On August 6, 2004 Arnowitz also filed the following 9(a) Motions: 1) Opposition of Moorshead to Plaintiff's Motion for Payment of Administrative Fees and for Monthly Interim Payments; 2) Motion to Strike Moorshead's Opposition to Plaintiff's Motion For Payment **[*22]** of Administrative Fees and For Monthly Interim Payments and Opposition to Moorshead's 2nd Attempt to Intervene; 3) Affidavit of Compliance with 9A and Certificate of No Opposition.

In Moorshead's opposition to Arnowitz's 9(a) motion for fees and expenses she stated that she was the sole beneficiary of the Fitchburg Property. [28] Moorshead opposed Arnowitz's motion on the basis that no money was owed to the mortgage holder because "no money or other consideration was ever given to create a binding obligation." [29] Furthermore, Moorshead stated that in the thirteen years since the mortgage was recorded, "no payments were made and . . . no demand for payment was ever made by any alleged holder of the Mortgage." Essentially, Moorshead claimed that despite the presence of a mortgage from the Pappases to HML as an encumbrance of record, no money ever changed

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[24] Notice of Filing was sent to all parties on August 5, 2004.

[25] The judgment of the Suffolk Superior Court found that the amount owed by Suffolk on September 14, 1999 was $ 160,212.17, which is $ 860,372.15 less than the amount that Arnowitz originally stated that was owed to this court.

[26] This amount was claimed even after allowing for the credit of certain escrowed funds in the amount of $ 44,212.17 and the application of the net proceeds of a mortgage owned by HML on real estate in Quincy.

[27] See Plaintiff's Motion for Payment of Administrative Fees and Monthly Interim Payments, August 6, 2004, Page 3, Paragraph 11.

[28] In her previous motions filed on April 2, 2004 Moorshead had claimed to be Trustee of the Charles Park Realty Trust, but did not claim to be the sole beneficiary.

[29] See Memorandum of Law in Support of Moorshead's Opposition to Plaintiff's Motion for Payment Motion for Payment of Administrative fees and For Monthly Interim Payments, Page 2.

hands between the Pappases and HML. In addition, Moorshead took the position that Zimmerman had failed to properly collect rents because he had not taken possession of the Fitchburg Property, and had failed and refused to pay the expenses of the property including the payment of insurance. Arnowitz's Motion for Payment of Fees and For **[*23]** Monthly Interim Payments and Motion to Strike Moorshead's Opposition was allowed on August 12, 2004 (McDonald, J.).

On August 23, 2004, Moorshead filed a Renewed Motion to Revoke Court's Order Granting Receiver's Motion to Receive Mortgage Payments, Or In the Alternative, To Stay Implementation of Order, and For Turnover of All Rents Received and a Renewed Motion to Intervene. Both motions were denied on September 2, 2004 for failure to comply with *Superior Court Rule 9D* (McDonald, J.). [30]

[*24] Zimmerman Employs Capitol to Manage the Fitchburg Property

On September 3, 2004, five years after Zimmerman was appointed receiver, Zimmerman filed an emergency motion pursuant to *Rule 9A* to: 1) take possession of the Fitchburg Property; 2) to employ Capitol Realty Group, Inc. ("Capitol") to manage the premises; and 3) for authority to expend funds for operation of the premises. Zimmerman stated that pursuant to court orders he had begun to collect rent from all the tenants at the Fitchburg Property except Moorshead, who operated two businesses on the premises. Zimmerman stated that Moorshead, as the self-admitted manager of the Fitchburg Property, had failed to maintain the premises resulting in violations from the City of Fitchburg for garbage violations. As such, Zimmerman requested that he be able to foreclose on the mortgage by entry pursuant to *G.L.c. 241, § 1*. Zimmerman also requested that he employ Capitol to manage the Fitchburg Property, for a fee of 8.5% of gross rents, and that he be authorized to pay the ordinary and usual expenses incurred in the operation of the Fitchburg Property without further order of the court. [31] This motion was allowed **[*25]** after a hearing on September 10, 2004 (Kern, J.).

Zimmerman's First Interim Expense Report

On September 28, 2004, five years after his appointment as receiver, Zimmerman filed his First Interim Report and Request for Payment of Fees and Expenses pursuant to *Superior Court Rule 9A*. This report covered the period April 12, 2004 through September 13, 2004. Zimmerman reported that he had collected $ 89,564.50 in rent from the tenants of the Fitchburg Property. Zimmerman also claimed that between March 24, 1999 and August 31, 2001 (sic) [32] he had accumulated fees and expenses during his work as HML's Receiver in the amount of $ 41,462.74. [33] He stated that he had worked 133 hours on the case, and provided documentation detailing the rental receipts from the Fitchburg Property tenants. No disbursements were listed. He also asked **[*26]** the court for permission to pay his fees and expenses from the rent receipts. The First Interim Report was unopposed and was allowed on October 19, 2004 (Kern, J.).

Court Approves Payment of Arnowitz's Fees From Receivership Estate

Arnowitz had already received the court's prior approval to pay any fees and expenses that might be incurred by Zimmerman or Arnowitz with regard to HML's receivership estate. [34] On September 28, 2004, Zimmerman filed a 9(a) Application for Instructions with his first Interim Report in which he noted that Arnowitz had emailed him an invoice requesting payment of administrative expenses in the amount of $ 20,250.50 from the receivership estate. [35] Attached to the Application for Instructions was a memorandum submitted by Arnowitz **[*27]** in support of the payment of his fees from the HML estate. [36]

Zimmerman petitioned this court as to whether he could

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[30] In rejecting the motions McDonald, J. stated in a margin entry that, "this is nothing more than a motion to reconsider with nearly identical affidavit and memorandum. i.e. nothing new of substance."

[31] Gross rents were then $ 14,660.75, resulting in a monthly management fee of $ 1,246.86. Zimmerman states that this is below the industry standard of 10.

[32] It should be noted that the time log attached to the report actually includes Zimmerman's time until August 31, 2004. It is assumed that the reference to 2001 on page 3, paragraph 3 is a typo.

[33] $ 40,848.50 in fees plus $ 614.24 in expenses.

[34] See Arnowitz's Motion for Payment of Administrative Fees and For Monthly Interim Payments, allowed on August 12, 2004 (Kern, J.).

[35] Arnowitz's firm billed 54.1 hours at $ 275.00 per hour and 21.5 hours at $ 250.00.

[36] See Memorandum of Facts and Law in Support of Petitioning Creditor's Counsel Fees in Support of Receiver's Request for Instructions.

use the rent receipts from the Fitchburg Property to pay Arnowitz and for approval of the plaintiff's invoice. [37] Arnowitz claimed in his memorandum that he was only "requesting payment of those fees that it generated which directly resulted in aiding the Receiver in locating, confirming and preserving assets that the Receiver currently has in his possession for the benefit of all the creditors of the estate of HML." Arnowitz stated that he was not seeking payment for the "numerous hours" of consultation between himself, B&S and **[*28]** the Receiver, but only "for the most direct and proximate efforts associated with the Receiver obtaining and preserving the current estate." Zimmerman's motion was unopposed and was allowed on October 19, 2004 (Kern, J.).

An Accounting of Arnowitz's Fee Request

Arnowitz sought fees from four separate parts of the case: (1) the time expended researching at the Worcester Registry of Deeds in November 2003; (2) work completed in opposition to the Emergency Motions of Moorshead in April 2004; (3) work completed in opposition to Moorshead's subsequent Motions to Intervene and Stay the Receiver in July and August 2004; (4) online research at the Registry of Deeds and an affidavit of John L. Hause. [38]

[*29] First, Arnowitz stated that as a result of the Suffolk case, he and Zimmerman became aware that Xarras had put mortgages on certain real estate that Arnowitz claimed were being used to hide funds from the creditors of HML. Arnowitz claimed that as a direct result of his firm's research of the Charles Park Realty Trust at the Registry of Deeds, and a visit to the Fitchburg Property, Zimmerman was able to secure rents for the HML mortgage that had been assigned to him for the benefit of HML's creditors. In so doing, A&G Attorney John Hause billed $ 1,375.00 for his research at the Worcester North Registry of Deeds and a visit to the Fitchburg Property in November 2003.

Second, Arnowitz states that just prior to the tenants sending payments to Zimmerman, Moorshead claimed that she was the Trustee of the Fitchburg Property and tried to intervene in the case. Arnowitz alleged that Moorshead advised the tenants that they should pay the rents to the Trustee and not to Zimmerman. Because this happened just before Zimmerman was alleged to be going on vacation, he (Zimmerman) was unable to attend Moorshead's Emergency Motions hearing on Friday April 5, 2004. [39] Arnowitz states that he thus **[*30]** had to spend considerable time in opposing these motions that were subsequently defeated. Arnowitz states that "when it became apparent that A&G would have to appear in court on Moorshead's Emergency Motions, A&G began to treat that aspect of the case as billable to the receivership estate, as it was acting in the interest of all the creditors." As a result Arnowitz billed a further $ 7,072.50 in preparing for and attending the hearing regarding Nickless' Emergency Motion to Intervene in April 2004.

In July 2004, Arnowitz billed a further $ 5,500.00 to oppose Moorshead's opposition to his Motion for Payment of Administrative Fees and for Monthly Interim Payments. In August 2004, Arnowitz billed a further $ 5,500 **[*31]** in Opposition to the Renewed Motion of Nicole Moorshead to Intervene and Revoke. [40] Finally in August 2004, Arnowitz billed $ 787.50 for online research at the Registry of Deeds and for drafting the affidavit of John Hause.

Zimmerman's Second Interim Expense Report

On December 29, 2004, five years after his appointment as receiver, Zimmerman filed his Second Interim Report and Request for Payment of Fees and Expenses pursuant to *Rule 9A*. Zimmerman reported his activities between September 1, 2004 and December 13, 2004. During this time period he claimed fees and expenses of $ 13,318.68 for forty-two hours work, and stated that after paying fees and expenses he had a total of $ 44,597.26 in his possession. Zimmerman provided an accounting of his income and disbursements. This accounting **[*32]** shows that between April 12, 2004 and December 9, 2004, Zimmerman collected $ 133,691.16 in receipts and had disbursements of $ 89,093.90. The disbursements consist of Zimmerman and Arnowitz's fees, taxes, insurance, and two payments to Capitol. There does not appear to have

[37] See Receiver's Application for Instructions, September 28, 2004, Page 2, Paragraph 6.

[38] Hause is an associate attorney at Arnowitz's firm.

[39] There is no suggestion as to why Arnowitz could not have appeared and asked for a continuance to allow Zimmerman to go on vacation and return, or even that Zimmerman could not have done so. What are referred to by Arnowitz as "emergency motions," this court determines they are not emergency motions.

[40] Moorshead's Motion to Intervene and Revoke Court's Order Granting Receiver's Motion to Receive Mortgage Payments, or, in the Alternative, to Stay Implementation or Order, and for Turn Over of All Rents Received, August 23, 2004.

been any disbursements to the creditors up to this point.

Zimmerman noted that he had received two proofs of claims, one from Beacon in the amount of $ 1,082.24, and a second, from the Department of Revenue of the Commonwealth of Massachusetts in the amount of $ 2,215.69. He requested permission from the court to pay these two proofs of claims. In addition, Zimmerman stated that he had received proofs of claims from two unsecured creditors: one from Suffolk in the amount of $ 1,049,439.30, and another from Hilti in the amount of $ 47,461.62. [41] As such, Zimmerman requested permission from the court to make monthly pro rata payments to the unsecured creditors after taking fees and expenses of the receivership estate and the cost of operating the Fitchburg Property into account. The amount to be paid to Suffolk and Hilti would be at Zimmerman's "sole discretion." After a hearing, and no opposition having been filed, **[*33]** Zimmerman's Second Interim Report was allowed on January 19, 2005 (MacDonald, J.).

It should be noted that Hilti was a judgment creditor of HML and therefore the receivership clearly fell under the umbrella of an appointment of a statutory receiver under *G.L.c. 156B, § 105*.

However, it is now very clear that Suffolk is not and was never a judgment creditor. Suffolk had an original unliquidated claim of approximately $ 122,000 against HML. However, Arnowitz reported to Zimmerman as receiver that Suffolk was owed $ 1,020,584.32 with a per diem interest of $ 335.53 or $ 122,470.10 per annum by HML. Zimmerman and Arnowitz both misled the court by not being frank and disclosing that the debt was unliquidated, in litigation and ultimately determined to be an amount of $ 122,000 by the trial justice instead $ 1,020,584.32. They, Arnowitz and Zimmerman, thus integrated an **[*34]** equity receivership, an unliquidated debt, under the umbrella of a statutory receivership without disclosing the difference to the court. It would seem to be much more proper and candid with the court to either (1) file a separate equitable proceeding with Suffolk as an unliquidated debtor and then move to consolidate; or (2) file an amended complaint in the original action so as to include Suffolk under the umbrella of a separate equitable creditor, as opposed to a statutory creditor, receivership. This does not include the thought of the court in regard to Arnowitz who this court construes as having a substantial conflict of interest because he represents both creditors Hilti and Suffolk who have very different competing interests, one as an established judgment creditor; and Suffolk as an unliquidated contract creditor involved in litigation.

Zimmerman's Third Interim Report

Zimmerman's Third Interim Report and Request for Payment of Fees and Expenses pursuant to *Rule 9A* was filed on May 19, 2005. This report covered the period December 14, 2004 through May 5, 2005. The report indicated that he had moved ahead with foreclosure proceedings on the Westminster Property (six years **[*35]** after his appointment as receiver). In so doing Zimmerman had filed a request at the Land Court Case to remove a cloud on the title on the Westminster Property; he also filed and received a lis pendens on same. Zimmerman stated that he had $ 35,029.68 in his possession after payment of authorized expenses and attached an accounting. Between December 14, 2004 and May 5, 2005, Zimmerman claimed to have incurred expenses of $ 27,477.12 after a total of 98 hours work. His accounting shows that between April 12, 2004 and April 28, 2005, Zimmerman had collected $ 196,679.88 and made disbursements of $ 161,650.20.

The attached accounting indicated that two payments were made from the HML's receivership estate account to "Arnowitz & Goldberg/Hilti, Inc./Suffolk": one payment in the amount of $ 15,000.00 on February 2, 2005, and another payment in the amount of $ 10,000 on March 29, 2005. Thus, as of April 28, 2005, on its face, it appears that Zimmerman has paid approximately 12.71% of the total receivership receipts to the creditors, Hilti and Suffolk, [42] care of Arnowitz. Zimmerman sought approval of the report and his fees and expenses. Zimmerman's Third Interim Report and Request for Payment **[*36]** of Fees and Expenses was allowed on May 31, 2005, with no opposition having been filed (Connor, J.).

Trustee Curry's and Beneficiary Moorshead's Third Attempt to Intervene

On June 6, 2005, Alexis Curry ("Curry"), as Trustee of the Fitchburg Property, and Moorshead, as sole beneficiary of the Fitchburg Property, moved for leave to file a complaint for declaratory judgment against

[41] Hilti was the original creditor who in 1997 was owed $ 26,139.99 as a judgment creditor, and filed this Petition for a Statutory Receivership.

[42] Payment was made as noted above to "Arnowitz & Goldberg/Hilti, Inc./Suffolk" and not directly to the creditors.

Zimmerman. Curry and Moorshead disputed whether there was in fact any debt owed on the mortgage that Zimmerman had collected rents on as part of his receivership duties. The motion was opposed by Zimmerman. Arnowitz also filed an opposition and a cross motion to Strike the Motion to File a Complaint for Declaratory Judgment Against Receiver. [43] On June 22, 2005, in denying Curry's and Moorshead's motion this court noted in a margin entry that,

> This motion has been brought and denied twice without appeal or request **[*37]** for reconsideration. The moving party has also failed to comply with *Superior Court Rule 9A* requirement of filing pleadings within 10 days. Parties will have opportunities to assert their defenses when a foreclosure is commenced.

Arnowitz's opposition and cross motion were allowed on the same day. On June 6, 2005, he also filed a Cross Motion for Sanctions that Curry and Moorhead opposed. In this motion, Arnowitz asked for sanctions against Moorshead and Curry as a result of their various motions to intervene and attempts to file suit against Zimmerman. Specifically Arnowitz asked that: 1) Curry and Moorshead be enjoined from filing any further legal proceedings that might interfere with Zimmerman's duties; 2) that Curry and Moorshead be assessed $ 80,000 in legal fees to repay the estate of HML; 3) and that Zimmerman be appointed as Receiver of the Fitchburg Property **[*38]** since the Trust could no longer pay its debts as they came due.

On June 30, 2006, Arnowitz's motion was allowed in part, assessing legal fees in the amount of $ 3,650 to Zimmerman and Arnowitz for defending Curry's and Moorshead's declaratory judgment motion (Connor, J.). Curry and Moorshead filed a notice of appeal of this order denying their motion to file, and granting in part, Arnowitz's motion for sanctions.

Receiver's Fourth Interim Report and Request for Expenses

On November 22, 2005, Zimmerman filed his Fourth Interim Report and Request for Expenses pursuant to *Rule 9A*. This report covered the period May 12, 2005 through November 3, 2005. Zimmerman stated that he had $ 23,000.99 in his possession. After 41.5 hours work on the receivership estate, he claimed fees and expenses of $ 11,848.21 between May 12, 2005 and November 3, 2005. The accounting provided by Zimmerman shows that an additional three payments were made to "Arnowitz & Goldberg, Attys/Hilti/Suffolk.": 1) $ 12,000.000 on June 23, 2005; 2) $ 10,000 on August 11, 2005; and 3) $ 10,000 on October 11, 2005. As of November 1, 2005 Zimmerman's accounts show that he has collected $ 290,437.85 in receipts and paid out $ 267,436.86 **[*39]** in disbursements. Zimmerman had paid out a total of $ 57,000 to "Arnowitz & Goldberg, Attys/Hilti/Suffolk", which accounted for only 21.31% of total monies collected up to this point. None of these reports suggest to the court how much was distributed to Hilti and how much to Suffolk. This report was allowed on December 16, 2005 (Agnes, J.).

Receiver's Fifth Interim Report and Request for Expenses

On June 8, 2006, Zimmerman filed his Fifth Interim Report and Request for Expenses pursuant to *Rule 9A*. This report covered the period November 4, 2005 through May 19, 2006. He stated that he had $ 30,856.10 in his possession. After 82 hours work on the receivership estate, Zimmerman claimed fees and expenses of $ 22,813.80 for the period. The accounting further shows that an additional two payments were made to Hilti and Suffolk: 1) $ 10,000.00 on December 22, 2005; and 2) $ 12,000 on March 28, 2006. Again these entries were marked as disbursements to "Arnowitz & Goldberg, Attys/Hilti/Suffolk." This report has yet to be approved by this court.

Xarras's Motion to Replace the Receiver

On April 20, 2006, Xarras filed a Motion to Intervene [44] and a Motion to Replace the Receiver. Both Zimmerman **[*40]** and Arnowitz filed motions in opposition. [45] In his Motion to Replace the Receiver Xarras alleges that Zimmerman had "engaged in a consistent and continuous pattern of breaching the fiduciary duty he owes HML and the court." Specifically, Xarras alleges that Arnowitz and Zimmerman have a "close relationship," that Zimmerman has demonstrated self-dealing, favoring entities related to him, and favoring the law firm that requested his appointment.

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[43] It is not clear why it was necessary for both Arnowitz and Zimmerman to both be filing oppositions.

[44] The Motion to Intervene was allowed by Murphy, J. on May 15, 2006, is not before the court and was not addressed in this memorandum.

[45] Again, it is not clear why both Arnowitz and Zimmerman needed to file opposition and therefore incur fees for both.

Xarras claims that Zimmerman breached the fiduciary duty he owes to HML in three ways. First, Xarras states that Zimmerman and Arnowitz have conspired to use monies collected for the receivership estate of HML to pay themselves excessive fees. Xarras alleges that from September 13, 2005 through November 2005 **[*41]** Zimmerman paid himself $ 94,106.75 from the funds he collected on behalf of HML. Xarras also alleges that from September 13, 2004, through November 2005, Zimmerman paid A&G $ 77,250.50 from receivership funds he had collected. Xarras further alleges that monies paid to Zimmerman and A&G account for approximately 60% of the total monies collected.

Second, Xarras alleges that "very little, if any monies," have been paid to the creditors of HML. At the hearing on September 19, 2006, Xarras alleged that "not one nickel has gone to a creditor." [46] Xarras states in an attached affidavit to his motion that he does not believe that any of the monies Zimmerman collected have been paid to the creditors because he continues "to receive documents from the various relevant courts that indicate that both Hilti and Suffolk are still owed the same amount from HML, with interest accumulating daily."

Third, Xarras contends that from September 13, 2004 through November 2005, Zimmerman **[*42]** paid $ 15,224.06 to Capitol for management services of the Fitchburg Property. Xarras alleges that Capitol's property manager is the husband of an attorney in Zimmerman's office, and that as the properties are located in Worcester County it would be "more practical and cost effective to appoint a Receiver who is more locally situated." Finally, Xarras contends that Zimmerman, as receiver, filed an affidavit in the Suffolk case whereby he advocated that the court assess treble damages against HML, thus breaching the fiduciary duty that Zimmerman owes to HML.

Arnowitz's and Zimmerman's Position

In his opposition, Zimmerman stated that he made great efforts to collect money on behalf of the HML estate and had collected over $ 355,000 by April 1, 2006. In so doing Zimmerman states that he has filed four Interim Reports and Request for Expenses with the court, all of which have been approved. Zimmerman states that despite serving these reports on Dombrowski, Xarras's counsel of record, Dombrowski never filed an opposition to the request for fees. Zimmerman contends that much of the time expended was in opposing litigation that has been initiated by "Xarras, his wife, his two sisters and **[*43]** various entities controlled by Xarras, including evicting Xarras's sister from a store in on the Fitchburg Property."

With regard to Capitol's employment to manage the Fitchburg Property, Zimmerman further states that the job was not a "plum assignment." Indeed, Capitol was not his first choice; rather other property managers refused to accept the assignment because of the "turmoil" at the property. The "others" were never identified. Zimmerman also avers that Capitol has provided services for their monthly fee, and that Xarras has not challenged the quality or timeliness of the services. With regard to his affidavit, Zimmerman states that an affidavit, signed under penalties of perjury, is not a *per se* breach of fiduciary duty.

Arnowitz contends that Xarras's motion is "untimely and frivolous" because Xarras has been involved in the proceedings for the past seven years and Dombrowski, as Xarras's attorney, had been given notice of all pleadings since he entered his appearance on the matter but has taken no action on the matter. Arnowitz contends that the creditors, Suffolk and Hilti, have in fact received funds from the HML receivership estate, without revealing to the court **[*44]** how much or what percentage, despite the large amount of legal fees generated in thwarting the "frivolous" litigation initiated by Xarras. Arnowitz states that the monies paid to Suffolk and Hilti from the HML estate were split on a pro rata distribution of 95% and 5% respectively. As such, Arnowitz claims that as of the date of the motion, April 20, 2006, the creditors had been paid a total of $ 69,000 through Zimmerman, with Suffolk receiving $ 65,550 and Hilti receiving $ 3,450.

The May 15, 2006 Hearing before Judge Murphy

On May 15, 2006, a hearing was held before Judge Murphy. Four motions were addressed at this hearing: 1) Xarras's Motion to Intervene; 2) Xarras's Motion to Replace the Receiver; 3) Receiver's Opposition to Xarras's Motion to Intervene and Motion to Replace the Receiver; 4) Hilti's Opposition to Xarras's Motion to Intervene and Motion to Replace the Receiver and Cross Motion for Costs. The docket reflects that the court allowed Xarras's Motion to Intervene [47] on May

[46] Transcript of Hearing, page 76, Lines 23-24.

[47] It is not clear why Xarras's counsel would have needed to file a Motion to Intervene as he had been the counsel of record since January 13, 2000, and had been receiving notice of all motions and orders in this case.

15, 2006 and *sua sponte,* entered a margin entry on that motion stating as follows:

> It is ordered that the fees of Atty. Arnowitz for representation of Hilti & Suffolk Construction are to **[*45]** be held in an interest bearing account w/ Attys. Arnowitz and Dombrowski as co-escrowers. The fees of Atty Zimmerman, as Receiver, shall henceforth likewise, be deposited in the same account. Without Prejudice, and until further order of the Court. (Murphy, J.)

The docket does not reflect the issuing of any other orders as a result of the May 15, 2006 hearing. [48]

Zimmerman's **[*46]** Motion to Reconsider Escrow of His Fees

On June 7, 2006, Zimmerman filed a Motion for Reconsideration of Judge Murphy's *sua sponte* escrow order. Zimmerman stated that all fees he had received were for previously provided rather than prospective services, and that he did not file fee requests on a regular basis, but only when "substantial fees [had] been incurred, there [were] funds available to pay the fees and in conjunction with a report to the Court of the status of the proceedings." Furthermore, Zimmerman stated that he had two proceedings in Land Court that could create additional funds for HML's creditors that would incur substantial expenses. Zimmerman alleged that the escrow of his fees in this case would not allow him to pay the necessary costs of operation of his law office. He further noted that he had the court's authority to make periodic payments to creditors of the receivership estate, and that any fees due to Arnowitz were a matter of contract between Arnowitz and Hilti, and therefore were "not subject to this Court's supervision." As such, Zimmerman requested that the *sua sponte* order be vacated, or that a hearing be conducted on the reconsideration of **[*47]** the escrow order, either by Judge Murphy or the Regional Administrative Justice, Judge McCann.

Xarras's Opposition to Zimmerman's Motion to Reconsider

On June 15, 2006, Xarras filed an opposition to Zimmerman's Motion for Reconsideration. Xarras contends that no new information was submitted to the court in Zimmerman's Motion for Reconsideration, and that Zimmerman had failed to explain why "significant monies" were paid to him and Arnowitz, without any monies being paid to creditors.

In addition, Xarras states that Zimmerman has failed to adequately explain why he advocated against HML in the Suffolk case, or why it would not be more practical and cost effective to appoint a local Receiver.

Arnowitz's Motion to Reconsider Escrow of His Fees

On June 27, 2006, Arnowitz also filed a Motion for Reconsideration. Arnowitz suggested that the placing of his fees for the representation of Hilti and Suffolk in an escrow account prejudices his client in this matter. Arnowitz further stated that the escrow of his fees in this matter violates the *Contracts Clause of the United States Constitution*, and that the court does not have the authority, either by statute or case law, to escrow his **[*48]** fees. Arnowitz requested that the order be vacated.

The September 19, 2006 Hearing

On June 27, 2006, Judge Murphy took no action and referred all pending motions to the Regional Administrative, McCann, J., for a hearing. That hearing took place on September 19, 2006 ("the Hearing"). Attorneys Zimmerman, Arnowitz, Dombrowski and Nickels [49] appeared before the court at the Hearing. Judge McCann heard arguments on four motions: 1) Xarras's Motion to Replace the Receiver; 2) Zimmerman's Motions for Reconsideration of the Escrow of His Fees; 3) Arnowitz's Motion for Reconsideration of the Escrow of his Fees and Cross Motion for Costs; and 4) Motion of Alexis Curry to File a Counterclaim in Land Court. [50] The motions were taken under advisement, and Judge Murphy's Escrow Order was left in full effect.

DISCUSSION

Xarras's Answer on Behalf of **[*49]** HML

As a preliminary matter it is apparent that Xarras's *pro se* answer to Hilti's complaint to appoint a Receiver should not have been accepted by the Clerk's Office, or

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[48] Zimmerman contends that Judge Murphy actually denied Xarras's Motion to Replace the Receiver and took no action on Arnowitz's cross motion for costs. See Transcript, Page 23, Lines 21-23. The record does not reflect that to be the case.

[49] Nickels represented Alexis Curry as Trustee of the Charles Park Realty Trust.

[50] This motion was allowed (McCann, J.), and is not discussed in this memorandum.

at least stricken from the record by motion of Hilti, which was never filed. ***HN1***[⬆] A defendant corporation may not be represented in judicial proceedings by a corporate officer who is not licensed to practice law. HML Development Corp. should then have been defaulted. It never was. It is well settled law in Massachusetts that "corporations must appear and be represented in court, if at all, by attorneys." *Driscoll v. T.R. White Company, Inc., 441 Mass. 1009, 1010, 805 N.E.2d 482 (2004)* (quoting *Varney Enters, Inc. v. WMF, Inc., 402 Mass. 79, 82, 520 N.E.2d 1312 (1988)*; see also, G.L.A. 221, § 46. Individuals that accept the benefits of incorporation must "bear the burden of hiring counsel to sue or defend in court." *Id.* (citing *Walacavage v. Excell 2000, Inc., 331 Pa.Super. 137, 142-43, 480 A.2d 281 (1984))*. A defendant who fails to file an answer is subject to entry of default and a judgment of default. See *Mass.R.Civ.P. 55(a)*, *55(b)*.

It appears **[*50]** that Xarras, President of HML, filed an answer to Hilti's complaint to appoint a Receiver. This complaint was filed against a corporation and James L. Xarras was not named as a defendant at that time. Xarras could not properly answer a complaint on behalf of the corporation unless he was a licensed attorney in Massachusetts. Thus HML was required to hire an attorney to represent it in this case, including the filing of an answer. This did not occur. HML's answer to the complaint should have been stricken and a default judgment properly entered thereon. Arnowitz took no such remedial action.

The Duty of a Statutory Receiver

HN2[⬆] A receivership is a prophylactic measure to protect assets in the event a particular creditor can prove that corporation is liable on a debt. See *Charlette v. Charlette Bros. Foundry, Inc., 59 Mass.App.Ct. 34, 793 N.E.2d 1268, (2003)*, quoting Shapiro, Perlin, & Connors, Collection Law § 13.1 (3d ed. 2000); see *New England Theatres, Inc. v. Olympia Theatres, Inc., 287 Mass. 485, 492, 192 N.E. 93 (1934)*, cert. denied sub nom. *E.M. Loew's, Inc. v. New England Theatres, Inc., 294 U.S. 713, 55 S. Ct. 509, 79 L. Ed. 1247 (1935)*; *Lopez v. Medford Community Center, Inc., 384 Mass. 163, 169, 424 N.E.2d 229 (1981)*; **[*51]** *Jae Corp. v. Massachusetts Port Realty Co., 3 Mass.App.Ct. 704, 704, 322 N.E.2d 426 (1975)*.

The appointment of a Receiver for a domestic corporation rests within the sound discretion of the court, and should be exercised where it appears that the corporate property would be subject to waste or loss in the absence of a Receiver thereby impairing the ability of the corporation to pay its debts. *New England Theatres, Inc. v. Olympia Theatres, Inc., 287 Mass. 485, 492, 192 N.E. 93 (1934)*. ***HN3***[⬆] A statutory Receiver may be appointed and dismissed only by order of the court. See *Mass.R.Civ.P. 66(a)*, *Superior Court Rule 51*. A statutory Receiver may be appointed under *G.L.c. 156B, § 105*,

> If a judgment has been recovered against a corporation and it has neglected for thirty days after demand made on execution to pay the amount due with the officer's fees, or to exhibit to the officer real or personal property belonging to it and subject to be taken on execution sufficient to satisfy the same and the execution has been returned unsatisfied, one or more Receivers may be appointed with the powers and duties provided in, **[*52]** and subject to, section one hundred and four.

See also, *Pouliot v. West India Fruit Co., 283 Mass. 182, 184, 186 N.E. 52 (1933)*; *George Altman, Inc. v. Vogue Internationale, Inc., 366 Mass. 176, 178-79, 314 N.E.2d 913 (1974)*. For the court to grant the request of a creditor for the appointment of a statutory Receiver, there must be a valid unpaid judgment against the corporation. See *George Altman, Inc. v. Vogue Internationale, Inc., 366 Mass. 176, 180, 314 N.E.2d 913 (1974)*. A creditor does not qualify as a "judgment creditor" until the judgment enters. *Smola v. Camara, 16 Mass.App.Ct. 908, 909, 449 N.E.2d 678 (1983)*.

HN4[⬆] The objective of the Receiver should be that of estate maximization. *Fleet Nat. Bank* at *96 F.3d at 540*. The objective of estate maximization is also secured in part by the "safeguard of court oversight" of any actions taken by a Receiver. *Id.* Under the statute the Receiver has a duty to pay all debts due from the corporation if the funds in their hands are sufficient, and if they are not, to distribute the funds ratably among the court-approved creditors. [51] See *G.L.c. 156B, § 106*. "If there is a balance remaining after the payment **[*53]** of the debts, the Receivers shall distribute and pay it to those who are justly entitled thereto as having been stockholders of the corporation, or their legal representatives." *Id.* Ordinarily, the sale of assets should be upon such terms and conditions as will, within a reasonable time, convert the assets to cash and bring about a distribution of such assets to creditors and

[51] In this case Hilti was a judgment debtor. Suffolk was an unliquidated contract creditor which was in ongoing litigation with BML.

stockholders. Boucher v. Hamilton Mfg. Co., 259 Mass. 259, 268-69, 156 N.E. 424 (1927) (the terms of any sale by Receivers must be such as to convert the property within a reasonable time into cash, so that distribution can be made to those in interest). It is the duty of the Receiver to determine the validity and the preference to be accorded to the claims of creditors. Old Colony Trust Co. v. Puritan Motors Corporation, 244 Mass. 259, 261, 138 N.E. 321 (1923). It is of paramount importance that during this process that the Receiver ensures that the creditors receive equality of treatment so far as is permissible under the law. New England Theatres, Inc. v. Olympia Theatres, Inc., 287 Mass. 485, 494, 192 N.E. 93 (1934).

[*54] HN5[] Within thirty days of appointment, the Receiver must provide the court with a detailed inventory of possessed property, or property as to which the Receiver has a right to possession. See MassR.Civ.P. 66(b) and Sup.Ct. Rule 51. This list must include a list of encumbrances on said property, along with estimated values. Mass.R.Civ.P. 66(b). If this cannot be accomplished within thirty days, the Receiver may seek an extension of time from the court. The Receiver must also provide to the court a list of all known creditors, along with a list of those whose property is being held by the Receiver. *Id.* The Receiver must file, not later than the fifteenth day of February of each year, a detailed account under oath, together with a report of the "condition of the receivership." See Mass.R.Civ.P. 66(c). Further accounts and reports may be ordered by the court, although the court may relieve the Receiver of this requirement. See Mass.R.Civ.P. (b) and (f). Once a Receiver distributes all of the assets of the corporation, the Receiver files the final account of the assets with the court and the court **[*55]** then discharges the Receiver. See Mass.R.Civ.P. 66(e) and Sup.Ct. Rule 51. Both Mass.R.Civ.P. 66(d) and Superior Court Rule 51 limit the ability of a Receiver who is an attorney from employing an attorney without order of the court.

The Fiduciary Duty of a Receiver

No Massachusetts state court has addressed the fiduciary duty of a Receiver. The dearth of case law, statutory provisions, or treatises have made the analysis of these motions difficult. This court has drawn what it can from Massachusetts as well as other jurisdictions. Nevertheless there is no doubt that HN6[] a court-appointed Receiver is a "full-fledged fiduciary." Fleet Nat. Bank v. H&D Entertainment, Inc., 96 F.3d 532, 540 (1st. Cir. 1996). A Receiver does not act solely as the agent of the company for which they have been appointed Receiver. Rochester Tumbler Works v. Mitchell Woodbury Co., 215 Mass. 194, 198, 102 N.E. 438 (1913). A Receiver is a representative of the court and of all parties with an interest in the litigation. Wellman v. North, 256 Mass. 496, 501, 152 N.E. 886 (1926). Thus, a Receiver owes **[*56]** fiduciary duty to all the parties in interest, including the creditors and the shareholder(s), and is "under the duty to act impartially toward, and protect the rights of, all parties." 16 Fletcher Cyc. Corp. § 7813. See also, Phelan v. Middle States Oil Corp., 154 F.2d 978, 991 (2d Cir. 1946) (Receiver owes a duty of strict impartiality and undivided loyalty to all parties interested in the receivership estate, and must not dilute that loyalty).

HN7[] Due to the fiduciary nature of his duty to the parties, a Receiver is not permitted to deal with the trust estate for his own benefit and advantage. See *Id.*; Sanders v. Stevens, 51 F.2d 743, 744 (D.Miss. S.D. 1931); In re Singer Furniture Corp., 47 F.2d 780, 784 (DCt. S.D.N.Y. 1931); In re Insull Utility Investments, 6 F. Supp. 653, 660 (D.C. Ill. 1933). As a fiduciary, a Receiver must avoid all conflicts of interest, and cannot derive personal profit from the appointment, other than reasonable compensation. See, Magruder v. Drury, 235 U.S. 106, 119-20, 35 S. Ct. 77, 59 L. Ed. 151 (1914) (trustee cannot make personal profit from managed estate); Phelan v. Middle States Oil Corp., 154 F.2d 978, 991 (2d Cir. 1946) **[*57]** (Receiver must act openly and fairly, and must not use position for their own profit or to further the interests of themselves or any associates); Lowder v. All Star Mills, Inc., 309 N.C. 695, 701-02, 309 S.E.2d 193 (1983) (no one should be appointed Receiver whose personal interests would substantially conflict with his or her unbiased judgment and duties as a Receiver). Under certain circumstances a Receiver may be held personally liable by the court for failure to properly perform his duties as Receiver. American Bridge Products, Inc. v. Decoulous, 328 B.R. 274 (Bkrtcy. D.Mass. 2005).

HN8[] The compensation to be paid to a Receiver is not regulated by a fixed commission of the money that passes through his hands, but rather, what would be a reasonable fee for the services required and rendered by a person of ordinary ability and competent for such duties and services. Jones v. Keen, 115 Mass. 170, 181 (1871), Grant v. Bryant, 101 Mass. 567, 570 (1869). What is a reasonable fee is a question that is to be determined by the sound discretion of the judge. Berman v. Linnane, 434 Mass. 301, 302-03, 748 N.E.2d 466 (2001) (citing McGrath v. Mishara, 386 Mass. 74,

87, 434 N.E.2d 1215 (1982)). **[*58]**

HN9[] In determining whether the fee paid to a Receiver as compensation for work done is reasonable a number of factors must be taken into consideration, including, "the nature of the case and the issues presented, the time and labor required, the amount of damages involved, the result obtained, the experience, reputation and ability of the attorney, the usual price charged for similar services by other attorneys in the same area, and the amount of awards in similar cases." Berman, 434 Mass. at 303, (quoting Linthicum v. Archambault, 379 Mass. 381, 388-89, 398 N.E.2d 482 (1979)). No single factor is determinative, and a "factor-by-factor analysis, although helpful, is not required." *Id.* (citing Margolies v. Hopkins, 401 Mass. 88, 93, 514 N.E.2d 1079 (1987)). In proving the amount of attorneys fees, contemporaneous time records, although not absolutely essential where there is other reliable evidence to support the claim, are very important. Handy v. Penal Institutions Commissioner of Boston, 412 Mass. 759, 767, 592 N.E.2d 1303 (1992).

Zimmerman and Arnowitz's Relationship

HML alleges in his Motion to Replace the Receiver that Arnowitz's "close relationship" with **[*59]** Zimmerman is central to this case, and that Zimmerman and Arnowitz's actions must be viewed in light of that alleged relationship. It is undisputed that Arnowitz asked this court to appoint Zimmerman as Receiver in this case, that they have a professional relationship going back twenty years, and that during this time Arnowitz used Zimmerman as a Receiver in other matters. Arnowitz and Zimmerman worked together during the Suffolk case in which Zimmerman actually intervened, and Zimmerman submitted an affidavit in support of Arnowitz's claim for an assessment of treble damages. Similarly, the record reflects that Zimmerman and Arnowitz have worked together in tracking down the assets of HML, and that Arnowitz even appeared for Zimmerman as Receiver in this case when he (Zimmerman) was on vacation in April 2004. Zimmerman also submitted a fees and expenses request for Arnowitz. The record reflects, and this court has no doubt, that Arnowitz and Zimmerman have a close and longstanding professional relationship that has influenced their actions in this case.

Zimmerman's Fiduciary Duty

Zimmerman owes a fiduciary duty to this court, HML, Hilti, Suffolk and all other creditors to maximize **[*60]** HML's estate, as well as the stockholders, or former stockholders of HML and to avoid waste or loss that might occur if a Receiver was not appointed. Xarras makes four main allegations against Zimmerman for breach of fiduciary duty; (1) that Zimmerman has abused his position as Receiver, and due to his "close relationship" with Arnowitz has enriched himself and Arnowitz by running up large legal fees which have been paid out of the estate of HML; (2) that little if any monies have been paid to the creditors of HML; (3) that Zimmerman abused his position as Receiver by hiring Capitol to manage the Fitchburg Property, and paying them $ 15,224.06 from HML funds, when Capitol is owned and operated by an associate of Zimmerman's, rather than hiring a local and cheaper property manager; and (4) that Zimmerman breached his fiduciary duty to HML by filing an affidavit against HML in the Suffolk case. It should be stressed thatHN10[] in making a determination as to whether the Receiver should be removed, this court does not view each incident of alleged impropriety in isolation, but rather as a whole.

Zimmerman's Delay: Milking the Receivership

Zimmerman appears to have used his position as Receiver **[*61]** as a vehicle for generating fees for himself and his associates, rather than as means to promptly, fairly and adequately compensate HML's judgment creditors. Upon his appointment as Receiver in March 1999, Zimmerman was required by statute to promptly liquidate HML's assets and make appropriate distributions to creditors within a reasonable time on the judgment involving Hilti. In regard to Suffolk, his duties were equitable in nature and required a different reporting procedure to the court. See G.L.c. 156B, § 106. This court is of the opinion that Zimmerman failed to carry out his statutory and equitable duties. Moreover, the March 19, 1999 order appointing Zimmerman as Receiver required him to file with the court within 30 days of the issue of the order: 1) a detailed inventory of the property within his possession or that he had a right to possess; 2) the value of that property; 3) a list of encumbrances on the property; and 4) a list of known creditors of the receivership. [52] See, MassR.Civ.P. 66(b) and Sup.Ct. Rule 51. There is no evidence in the record that Zimmerman complied with this part of the order.

[*62] In 1999 Zimmerman became aware that HML was the mortgagee on two properties, the Westminster

[52] See Order Appointing Receiver, Paragraph 4, March 19, 1999 (Toomey, J.).

and Fitchburg Properties respectively, with a combined value of $ 1,559,071.00. It is difficult to see why Zimmerman would not have moved expeditiously to foreclose on the Fitchburg and Westminster Properties in 1999, as he was required to do as Receiver. In September 1999, six months after Zimmerman's appointment, HML owed $ 160,493.83. In November 1999 HML owed Hilti $ 32,789.00. With the total amount owed by HML being less than $ 200,000 at the end of 1999, it is entirely conceivable that Zimmerman could have foreclosed on the properties and easily have satisfied the full judgment amounts owed to Hilti and Suffolk.

However, rather than ask this court to foreclose the mortgages on the two properties, Zimmerman merely filed a motion to receive mortgage payments that were due to HML, and to have the mortgages assigned to HML. [53] Thus Zimmerman did not act in the best interests of HML, and did not fulfill his duty to liquidate the assets of the HML and make prompt payments to the creditors of HML. Indeed, Zimmerman did not begin to foreclose on the Westminster Property until 2004, and does not **[*63]** appear to have begun the foreclosure on the Fitchburg Property at all. It is apparent that Zimmerman has delayed the process in an effort to maximize his own and his associates' fees from the HML estate. Zimmerman's failure to carry out the basic duty of a statutory Receiver weighs very heavily against his removal as Receiver in this case.

Money Paid to Creditors by Zimmerman

Xarras claims that little or no money has been paid to HML's creditors from the receivership estate. A review of the Interim Reports provided show that as of May 16, 2006, Zimmerman had paid out a total of $ 79,000.00 to Arnowitz as attorney for Suffolk and Hilti, which accounted for 20.1% of total monies collected by Zimmerman for the HML estate. At the Hearing Zimmerman stated that approximately $ 70-80,000 had been paid to Hilti and Suffolk. [54] When asked what proportion had been paid to Hilti **[*64]** and Suffolk respectively Zimmerman stated that he did not know because he had simply made the check payable to Arnowitz who would then pro-rate it between the two creditors, with Suffolk presumably receiving 97% and Hilti receiving 3%. [55] This is consistent with Zimmerman's reports that show seven payments to: "Arnowitz & Goldberg, Attys/Hilti/Suffolk."

Presumably, Xarras read these entries as payments to Arnowitz alone rather than payments to Hilti and Suffolk, c/o Arnowitz. Hence it would appear Xarras believes that the accounts Zimmerman provided reflect no payments to Hilti or Suffolk. Nevertheless, Xarras alleges in his affidavit, and Dombrowski alleged in the Hearing, that Hilti and Suffolk had in fact not been credited any payments and that interest had continued to be charged on the principal amounts.

With this concern in mind, a further step is needed. It does not appear that Zimmerman has offered any documentation **[*65]** to prove that the monies that he paid to Arnowitz's firm on behalf of Hilti and Suffolk from the HML estate have actually reached these creditors. Zimmerman should have provided further documentation to this court, demonstrating that the disbursements made to Arnowitz on behalf of Suffolk and Hilti, have actually been paid to the respective creditors' accounts, and not to an attorney who is not a creditor. Zimmerman's duty is not to Arnowitz but to Hilti and Suffolk directly.

Zimmerman's Fees

The fees paid to Zimmerman from the receivership estate, while not by themselves excessive, must be viewed in light of the fact that they were earned during a receivership which this court finds to be excessively long. Zimmerman is an experienced Receiver who has engaged in this type of work for over thirty years. [56] A review of the record indicates that Zimmerman charged $ 300.00 an hour for his services. Xarras does not allege that Zimmerman charged an excessive hourly rate, and Zimmerman's hourly rate of $ 300 was found to be reasonable by this court when it approved Zimmerman's motion for costs against Alexis Curry.

[*66] A review of Zimmerman's Fifth Interim Report, which is pending before this court, reveals that between April 12, 2004 and May 16, 2006, Zimmerman collected receipts of $ 392,924.41 on behalf of the HML estate, mostly by collecting rents from tenants at the Fitchburg Property. The accounting also shows that Zimmerman made disbursements of $ 362,068.31 within the same time period. Zimmerman was paid a total of $

[53] See Receiver's Petition for Authorization to Receive Mortgage Payments Due Defendant and For Assignment of Said Mortgages, November 9, 1999.

[54] Hearing transcript, page 17, lines 8-9.

[55] Hearing transcript, page 18, lines 4-8.

[56] Hearing transcript, page 69, line 17.

116,718.25 in court-approved fees and expenses for his law firm from the receivership estate of HML. Thus, as of May 16, 2006, Zimmerman's fees account for 29.7% of all monies he collected for the HML estate.

Zimmerman has submitted five separate Interim Reports and Requests for Payment of Fees and Expenses, four of which were approved by this court, and one of which is pending. In each report Zimmerman has documented the work that was carried out on the receivership estate, has attached detailed accountings of the receipts and disbursements of the receivership estate, and has completed detailed time sheets for his fees and expenses. During his time as Receiver Zimmerman has: 1) received an assignment of a mortgage from HML on the Fitchburg Property which has provided substantial **[*67]** funds for the HML estate in excess of $ 355,000; 2) has taken steps to clear title on the Fitchburg Property by filing an action in land court; 3) forced an assignment of the mortgage held by HML on the Westminster Property, and filed a complaint to foreclose said mortgage in land court; and 4) has defended three motions to intervene on behalf of Nicole Moorshead and Alexis Curry respectively.

Xarras states that between September 13, 2004 and November 2005 Zimmerman paid himself $ 94,106.75. [57] A review of Zimmerman's accounts shows that he actually paid himself $ 82,258.54 during this period. In any event, Xarras's statement is misleading. The payments that Xarras refers to, although made between September 2004 and November 2005, were actually authorized for work performed between March 24, 1999 and May 2005. Indeed, the approved First Interim Report for Payment of Fees and Expenses which requested $ 41,462.74 in fees covered a period of over 5 1/2 years, from March 1999 through August 2004. Thus, Zimmerman did not request fees for the first 5 1/2 years of the receivership.

[*68] Zimmerman made further requests for payment of fees in subsequent Interim Reports. However, these subsequent requests must be viewed in light of the fact that April 2004 saw the advent of repeated attempts by Moorshead and Curry to intervene in the case and prevent Zimmerman from collecting rents on the Fitchburg Property. All of these attempts were repeatedly denied by the court. This obviously required extensive litigation and Zimmerman had a fiduciary duty to thwart Moorshead and Curry in their attempts to prevent HML from recovering assets. However, as previously noted, it is not clear to this court why the receivership found itself in this position in 2004, when Zimmerman could have promptly foreclosed on the Fitchburg and Westminster properties, as assets of HML, after his appointment as Receiver in March 1999.

Zimmerman's Employment of Others

Zimmerman's employment of attorneys in his office, without prior approval of this court, for which he billed the receivership estate, adds weight to a finding that he should be removed as Receiver. It appears from the time sheets submitted with the Receiver's Interim Reports that Zimmerman has employed various attorneys and paralegals **[*69]** in his office to carry out work on the HML receivership estate, and as such, the various interim reports that have been submitted have requested that these fees be paid out of the receivership estate. *HN11*[↑] When a Receiver requires another attorney to help him work on a receivership case, he is required to petition the court, "stating the name of the attorney whom he desires to employ and showing the necessity of such employment." See *Mass.R.Civ.P. 66(e)* and *Sup.Ct. Rule 51*.

In an order dated November 9, 2006, this court noted that his Fifth Interim Report listed four individuals in his expenses time sheet: LBD, PLZ, JR. and RLB. Zimmerman was ordered to report back to the court their identity, relationship to the Receiver, and normal hourly rate (McCann, J.). On November 28, 2006, Zimmerman identified the following: (1) LBD is Lisa Darman, an attorney and partner at S&K, with an hourly rate of $ 250.00, whose "primary responsibility . . . is to be the lead attorney in the two Land Court Cases filed by the Receiver; (2) PLZ is Peter Zimmerman, who charges an hourly rate of $ 325.00; (3) JAR is Janine A. Rzasa is a paralegal and employee of S&K, with an hourly **[*70]** rate of $ 125.00; and (4) RLB is Richard L. Blumenthal, an attorney and partner at S&K, with an hourly rate of $ 295.00, whose primary responsibility is to prepare legal memoranda for the Receiver. [58] There is no evidence that Zimmerman ever petitioned this court for permission to authorize Lisa Darman, Richard Blumenthal or any other attorneys. Similar comments about payments to Arnowitz on the same issue had been previously addressed. Such a finding adds weight to a finding that Zimmerman should be removed as

[57] See Xarras's Motion to Remove Receiver, Page 2, Paragraph 6(a).

[58] See Receiver's Response to Order Entered on November 9, 2006 and Receiver's Request for Clarification Thereof, November 28, 2006.

Receiver as he has failed to comply with his duty as a statutory Receiver.

The Appointment of Capitol to Manage the Fitchburg Property

Zimmerman's employment of the husband of a member of his firm to manage a property that should have been foreclosed on, liquidated and paid to creditors, lends weight to a finding that Zimmerman should be replaced as Receiver. Xarras alleges **[*71]** that Zimmerman also breached his fiduciary duty to HML by paying Capitol $ 15,224.06 to manage the Fitchburg Property in fees between September 13, 2004 and November 2005. Specifically Xarras alleges that Capitol was "owned and operated by an associate of Zimmerman's," [59] and was thus making decisions in his management of the receivership estate to favor "entities related to him" [60] rather than make decisions that would benefit the estate.

At the Hearing, Attorney Nickless stated that the manager of the Fitchburg Property was "Zimmerman's partner or associate." [61] Zimmerman indicated that the property manager was the husband of a member of his firm. [62] Zimmerman stated that he asked the court for permission to appoint a property manager, but that nobody in the Fitchburg area would do the job because he could not guarantee that they would be paid. [63] He did not disclose to the court who else had been asked. **[*72]** As such, Zimmerman asked the husband of one of his firm colleagues out of Boston to manage the property and he agreed. [64] Zimmerman stated that this was all disclosed to the court. [65] The property manager was paid at 8.5% of gross rents, [66] which Zimmerman claims is below the 10% industry standard rate of for managing property. [67]

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[59] See Motion to Remove Receiver, Page 2, Paragraph 7.

[60] *Id.* at page 2, Paragraph 5.

[61] Hearing Transcript, page 53, lines 7-9.

[62] *Id. at page 53*, line 10.

[63] *Id.* at page 56, lines 20-23.

[64] *Id.* pages 56-57, lines 23-24, line 1.

[65] *Id.* at page 57, lines 1-3.

[66] *Id.* at page 68, line 9.

[67] *Id.* at page 68, lines 6-9.

A review of the accounting of HML's accounts provided by Zimmerman indicate that between April 2004 and May 2006, Capitol was paid $ 23,617.43 from the HML receivership estate. Xarras has not disputed that Capitol carried out its duties satisfactorily or that the fee charged by Capitol is excessive. Instead he relies on the fact that the property manager is the husband of an associate **[*73]** in Zimmerman's firm to raise an inference of a breach of fiduciary duty on the part of Zimmerman. The property manager Zimmerman employed was not a member of his law firm, and there is no evidence that fees or expenses were paid to Zimmerman or his firm in connection with the management of the Fitchburg Property. Zimmerman stated that Capitol would send him a bill and he would pay the funds out of the receivership estate. He had already received approval of the court to pay for the running expenses of the Fitchburg Property, and was thus authorized to make this payment. The amount of payment does not appear to be excessive and is not challenged as such by Xarras.

Nevertheless, this court concludes that this is another example of Zimmerman using the Receivership estate as a vehicle for which to generate income for associates. In effect, Zimmerman's failure to promptly foreclose on the Fitchburg Property enabled him to help the husband of a member of his law firm get their nose in the HML receivership trough. If a property manager was needed it is entirely reasonable for HML to wonder why Zimmerman did not make an effort to find a property manager in the north Worcester County area. **[*74]** There is no indication from Zimmerman as to which other property managers he contacted and how much they charged for their services. As such, Zimmerman's hiring of the husband of an S&K attorney to manage the Fitchburg property adds weight to a finding that he should be replaced as Receiver.

The Payment of Fees to Arnowitz

The unquestioned request for authorization to pay a substantial fee to Arnowitz from the receivership estate of HML, supports a finding that Zimmerman should be replaced as Receiver. In his Motion to Replace the Receiver, Xarras alleged that Zimmerman paid Arnowitz $ 77,250.50 in fees from HML's receivership estate between September 13, 2004 and November 2005. The record reflects that Arnowitz initiated the payment of his fees and expenses from HML's receivership estate by filing a Motion for Payment of Administrative Fees and For Monthly Interim Payments on August 6, 2004, that was subsequently approved on August 13, 2004.

Having gained court approval to submit bills for fees, Arnowitz then emailed an invoice to Zimmerman for $ 20,250.50. Zimmerman then asked the court to approve payment of this $ 20,250.50 fee to Arnowitz in his First Interim Report, filed on September 28, 2004. Zimmerman's **[*75]** request to pay Arnowitz's fee was subsequently approved by the court on October 19, 2004. Zimmerman's accounts reflect a payment of $ 20,250.50 to Arnowitz on October 20, 2004. This is the only payment that was made to Arnowitz from HML's receivership estate, and Zimmerman and Arnowitz made representations at the Hearing that there are no further requests for fees to be paid to Arnowitz from the receivership estate.

In the hearing on September 19, 2006 McCann, J. probed the issue of Zimmerman's payment to Arnowitz from HML's receivership estate;

The Court: Why did you as the Receiver pay a legal fee to Mr. Arnowitz?

Mr. Zimmerman: Because the court ordered me to do so Judge.

The Court: Why did you ask the court to authorize payment?

Mr. Zimmerman: I didn't ask them, Mr. Arnowitz asked the Court to authorize payment.

The Court: Did you think it unusual that if he had an independent fee arrangement with Hilti that it might be inappropriate to pay an attorneys fee out of funds that are being held by a Receiver?

Mr. Zimmerman: Well, he received funds being held by the Receiver for work that he had done for the benefit of his client which was Hilti.

The **[*76]** Court: Well, then--but Hilti paid it, why the Receiver, that's the question?

Mr. Zimmerman: Judge, I think Hilti was entitled to file a petition for the fee, he did the work, it was work in defending motions basically filed by Attorney Nickless on behalf of his clients. [68]

Zimmerman's Failure to Scrutinize Arnowitz's Fee Request

Zimmerman cannot simply state, as he did at the Hearing, that he was simply following a court order to pay Arnowitz. The method used by Zimmerman and Arnowitz was an end run on the court on essentially unopposed motions. As fiduciary to all parties, including HML, but more importantly the court, Zimmerman had a duty to preserve the estate from unnecessary waste, and to maximize the assets available to creditors. One of the ways this is done is by having the Receiver alone carry out all the work necessary to accomplish this goal, thus avoiding duplication of fees. That is why a Receiver is required to ask the court for permission **[*77]** before he hires anyone to assist him with his work, and why a Receiver has a duty to carefully scrutinize any fee requests that come before him. If the Receiver fails to fulfill this duty, it is incumbent on this court to ensure that the assets of the receivership estate are not wasted. The receiver in this case advocated on behalf of Arnowitz.

As such, Zimmerman had a duty to closely examine all requests for fees to be paid from the receivership estate, whether from Arnowitz or any other source. Thus Zimmerman had a duty to closely examine the propriety of Arnowitz's fee request at the time that Arnowitz made that request on August 6, 2004 when Arnowitz filed a Motion for Payment of Administrative Fees and For Monthly Interim Payments, or alternatively when Arnowitz sent Zimmerman an invoice. It is evident that Arnowitz's request for legal fees were requests for work that either should have been carried out by Zimmerman or if carried out for Hilti, should have been billed to Hilti and not the receivership estate.

There is little doubt that Arnowitz and Zimmerman have known each other for many years, have worked together on many other cases, and have cooperated with each other and **[*78]** worked closely together in this case. It appears that Zimmerman turned a blind eye to Arnowitz's fee request, or at the very least, did not give it the scrutiny that he would have, if it had been made by an attorney for another creditor that he did not know.

This court has no doubt that Zimmerman's relationship with Arnowitz contributed to this oversight. There is more than a whiff of suspicion that Zimmerman was simply trying to share some of the wealth of the HML estate with Arnowitz when in fact Hilti should have paid approximately $ 13,162.50 of the bill. The remaining $ 7,072.50 charged for the April 2004 representation could have been paid out of the HML receivership estate if it had been approved by the court in advance, but this request was never made.

The Legitimacy of the Fee to Arnowitz

[68] Hearing transcript, Pages 83-83, Lines 19-17.

Arnowitz asserts that all the fees paid to him were legitimate because they were for work that was of principal benefit to the estate, and were therefore payable from HML rather than from Hilti. [69] Arnowitz cites a number of cases in support of this position. See *Shannon v. Shepard Mfg. Co., 230 Mass. 224, 119 N.E. 768 (1918)*, *In re American Tissue Mills, 120 F. Supp. 950 (D.C.Mass. 1954)*, **[*79]** *Louisville, E. & St. L.R. Co. v. Wilson, 138 U.S. 501, 11 S. Ct. 405, 34 L. Ed. 1023 (1891)*, and *Antoine v. James E. Nelson, 265 Mass. 214, 218, 163 N.E. 903 (1928)*.

In *Shannon* the SJC held that the Superior Court had the jurisdiction to allow attorneys fees in a receivership action when the fees were for actions that were carried out "for the common benefit of many persons." *Id. at 236*. In *Shannon* an attorney had claimed fees for bringing the original motion which asked for a Receiver to be appointed in the case. *Id. at 228*. As such, the court determined that the fees for such a motion should be borne by the receivership **[*80]** estate rather than one of the creditors. *Id. at 236*.

Shannon is easily distinguishable from this case. In *Shannon* the attorneys fees were for an original petition to appoint a Receiver. In this case Arnowitz is asking to be compensated for actions taken years after the appointment of a Receiver. Inapposite to *Shannon*, where many other creditors benefited from the filing of the aforementioned motion, this case involves only two creditors of HML, Hilti and Suffolk, both of whom are represented by Arnowitz. Thus the reasoning behind allowing the fees to be paid for from the receivership estate is less readily apparent. This court declines to stretch the reasoning in *Shannon* any further than was stated in the *Shannon* case, but certainly not this case.

In *In re American Tissue* compensation was allowed for services in reorganizing an insolvent corporation to a petitioning creditor's counsel who had spent approximately 63 hours preparing a petition for receivership, and who had numerous conferences after the petition was filed. The court ruled that the lawyer, who was counsel for the petitioning creditors, could be compensated for services that were **[*81]** of principal benefit of the estate. *Id. at 952*. Services were deemed to be of principal benefit to the trustee when they were performed before the appointment of the trustee, and where the attorney was counsel for the creditors' committee. *Id.* Here, Arnowitz is attempting to be compensated for fees gained five years after Zimmerman's appointment as Receiver, and where the only two creditors who are both represented by Arnowitz. As such, *In re American Tissue* if anything, weakens Arnowitz's claim that his fees should have been paid out of the receivership estate.

An overriding principal in a receivership proceeding is that the receiver owes a fiduciary duty to all creditors as well as the court. Payment to Hilti and to Suffolk were not payments directly to those creditors. Payments were made to Arnowitz who represented both creditors. The fact that Arnowitz represented both creditors who have conflicting interests is problematic to begin with. But what compounds the problem more is that Arnowitz when questioned by this court about what the fee arrangement was between him and his two competing clients he refused to disclose that to the court claiming the attorney client **[*82]** privilege. This court assumes he also refused to disclose that information to Zimmerman, the receiver, for the very same reasons. Leave of court to pay Arnowitz directly was never sought nor obtained by Zimmerman. Zimmerman's fiduciary duty ran directly to Hilti and to Suffolk, and not to Arnowitz. It also runs directly to the court. In the absence of such permission any person furnishing services to the receivership estate is a mere volunteer and cannot recover for such services. 31 Mass. Prac., Equitable Remedies § 200 (2d ed.); *Superior Court Rule 51 (1974)*.

The April 2004 Fee: Lack of Court Permission [70]

HN12[↑] Both *Mass.R.Civ.P. 66(d)* and *Superior Court Rule 51* limit the ability of a Receiver who is an attorney from employing an attorney without order of the court. [71]

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[69] Arnowitz does not cite any legal authority for the payment of his fees from the receivership estate in his Motion to Reconsider. However Arnowitz did cite authority for the payment of his fees in a memorandum attached to Zimmerman's First Interim Report and Request for Payment of Expenses, and it is these authorities that are now addressed.

[70] Although Arnowitz denied that he was paid a fee at the hearing, it would appear to be a fee by any modern understanding of the word.

[71] M.R.C.P. 66(d) and *Sup.Ct. Rule 51* are identical and state that,

> ***HN13***[↑] When an attorney at law has been appointed a Receiver, *no attorney shall be employed by the Receiver or Receivers except upon order of court,* which shall be made only upon the petition of a Receiver, stating the name of the attorney whom he desires to employ and

In the absence **[*83]** of such permission a person furnishing services to the receivership estate is a mere volunteer and cannot recover for such services. See Super Ct. *Rule 51* (1974); *In re Whittemore, 157 Mass. 46, 47, 35 N.E. 93 (1892)*. The court may allow a creditor petitioning for the appointment of a Receiver reasonable costs, including fees. *Shannon v. Shepard Mfg. Co., 230 Mass. 224, 236, 119 N.E. 768 (1918)*. Although Massachusetts has not ruled on the payment of other fees to attorneys for creditors, outside of the original petition for appointment of a Receiver, the Second Circuit addressed this issue in *Davis v. Seneca Falls Mfg. Co., 17 F.2d 546 (2d. Cir. 1927)*. The court found that the allowance of fees to attorneys for unsecured creditors, whose labor benefited other creditors to be improper. *Id. at 549*.

[*84] At the Hearing Arnowitz stated that he was carrying out Zimmerman's work in April 2004 while Zimmerman was on vacation. [72] As a preliminary matter it is difficult to see why Zimmerman or Arnowitz could not have simply requested a continuance from the court while Zimmerman was on vacation. Although not formally employed by Zimmerman, Arnowitz had effectively stepped into Zimmerman's shoes as receiver. Before hiring any attorney, a Receiver is required to ask permission of the court to hire an attorney pursuant to M.R.C.P. 66(d). The reason behind that rule is to prevent the unnecessary duplication of fees and to avoid any conflicts of interest that might arise. These are precisely the issues which arose in this case between Arnowitz and Zimmerman.

[*85] Nothing suggests that Zimmerman ever petitioned the court to have Arnowitz take over his duties as receiver in April 2004 when he was on vacation. Thus, Arnowitz was not authorized to carry out the work that he billed $ 7,072.50 during the week in April 2004 when he defended Moorshead's motions. Even if this court accepts, as Arnowitz claims, that he was acting in the interests of his client, Hilti, it is difficult to see why Hilti would not pay the bill rather than the receivership estate. Thus the actions of Arnowitz and Zimmerman in the improper request to pay Arnowitz's fee, when viewed in light of their close professional relationship, lend further support to the view that an attempt was being made to share the wealth of the HML receivership estate. No prior authorization of Arnowitz to act as attorney was applied for or approved by the court. He, therefore, acted as a volunteer and any fees paid to him should be returned to the receiver.

Conflicts of Interest: Arnowitz as Receiver

Although Xarras does not allege any conflicts of interest issues with regard to Arnowitz, it is apparent that these issues must be raised. Although Massachusetts has never addressed the issue of **[*86]** whether a ***Receiver*** hiring an ***attorney*** who also represents a creditor or conflicting creditor presents a ***conflict of interest***, a review of Massachusetts conflicts law and other jurisdictions provides us with some guidance.

Other jurisdictions have stated that ***HN14***[⬆] as a general rule that a court should not authorize the employment by the Receiver of an attorney who has been representing any of the parties, or whose interest is opposed to that of a party to the receivership. See *Cahall v. Lofland, 12 Del.Ch. 125, 107 A. 769, 769 (1919)* (Receiver and his counsel should be impartial between stockholder(s) and creditors, and therefore an attorney of creditor should not act as attorney of Receiver); *Liberty Folder Co. v. Anderson, 55 Ohio L. Abs. 268, 89 N.E.2d 500, 500 (1949)* (equity does not sanction the employment by a Receiver of the attorney of any of the parties or one whose interest is opposed to those of the parties in the receivership action, nor of an attorney for the debtor); *Bartelt v. Smith, 145 Wis. 31, 129 N.W. 782, 784 (1911)* (while as a rule Receivers should not employ the counsel of either of the parties, where such counsel's **[*87]** services to the Receiver do not conflict with his duties to the party, they may be employed and a reasonable counsel fee for their services may be allowed the Receiver); *Hozz v. Varga, 166 Cal. App. 2d 539, 543, 333 P.2d 113 (1959)* (it is improper for the Receiver to employ as attorney, without an order of the court, the attorney for the plaintiff in the action in which the Receiver was appointed); *Davis v. Bayless, 70 F.3d 367, 374 (5th Cir. 1995)* (law of one state apparently disfavors, but does not prohibit, reliance by a Receiver on counsel for one of the parties to a receivership proceeding to carry out certain functions assigned by court order to the Receiver); *Hyre v. Johnson, 107 W.Va. 524, 149 S.E. 385 (1929)*. However, some courts have carved out an exception to the general rule, when there is "a perfect identity of interests between the plaintiffs and the Receivers or where the parties have consented." *Lowder v. All Star*

showing the necessity of such employment. (Emphasis added.)

[72] Arnowitz: I filed an application with the court for the court to approve payment of a fee of twenty thousand dollars for the work that I did for the Receiver because Mr. Nickless wouldn't allow him to continue the case. Hearing Transcript, Page 81, 21-24.

Mills, Inc., 309 N.C. 695, 702-03, 309 S.E.2d 193 (1983).

The disfavoring of using a party's attorney to act as counsel for the Receiver is obvious. The duty of a creditor's counsel is to zealously guard his interests at all times. One could easily **[*88]** envision a situation where the attorney might discover that his duties as Receiver required action that his client creditor would disapprove of. This court shares the view of the majority of jurisdictions that counsel for a creditor should not act as Receiver or be employed by the Receiver in any capacity because of the potential for conflicts of interest.

It is a general rule of application in the United States that HN15[] an attorney may not simultaneously represent differing interests that are adverse to one another, unless both parties consent to the dual representation. Massachusetts follows this rule, on the ground that the undivided loyalty that a lawyer owes to his client forbids him, without the client's consent, from acting for the client in one action and at the same time against the client in another action, even if the lawsuits are unrelated in subject matter. McCourt Co., Inc. v. FPC Properties, Inc., 386 Mass. 145, 146, 434 N.E.2d 1234 (1982). In *McCourt* the SJC based its decision on the Canons of Ethics and Disciplinary Rules Regulating the Practice of Law, [S.J.C. Rule 3:07], in particular on the provisions of DR 5-105(B) which states **[*89]** that "[a] lawyer shall not continue multiple employment if it would be likely to involve him in representing differing interests." Id. at 146.

HN16[] Rule 1.7 of the Massachusetts Rules of Professional Conduct states that a lawyer shall not represent a client if the representation of that client will be directly adverse to another client unless 1) the lawyer reasonably believes the representation will not adversely affect the relationship with the other client, and 2) each client consents after consultation. MRPC 1.7(a). In addition a lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client, unless: 1) the lawyer reasonably believes the representation will not be adversely affected, and 2) the client consents after consultation. MRPC 1.7(b). When an attorney represents multiple clients in a single matter "the consultation shall include explanation of the implications of the common representation and the advantages and risks involved." MRPC 1.7(b)(2).

HN17[] With respect to MRPC 1.7(b) loyalty to a client is considered to be impaired when the lawyer "cannot consider, recommend or carry **[*90]** out an appropriate course of action for the client because of the lawyer's other responsibilities or interests." MRPC 1.7, Comment 4. Thus the crucial questions are: (1) the likelihood that a conflict would arise; (2) whether the conflict would materially limit the lawyer's independent professional judgment. MRPC 1.7, Comment 4. Although due consideration should be given to whether the client "wishes to accommodate the other interest involved." *Id.* However a lawyer may not ask for a client to consent to a conflict when "a disinterested lawyer would conclude that the client should not agree to the representation under the circumstances." MRPC 1.7, Comment 5. When a conflict exists before the representation of the client exists, the representation should be declined. MRPC 1.7, Comment 1. If the conflict arises after representation has begun, the lawyer should withdraw from the representation. MRPC 1.7, Comment 2. [73]

[*91] Arnowitz could not be considered an independent counsel because he was acting on behalf of one of HML's creditors. It is obvious that Arnowitz's duty to Hilti, as one of the creditors of HML, may have conflicted with his performance as Receiver because as counsel to Receiver it would be his duty to see that all creditors and parties are treated alike and with the utmost fairness. When asked by the court whether his simultaneous representation of both creditors, both Hilti and Suffolk, and the Receiver created a conflict of interest, Arnowitz stated that he was simply representing his client to protect its interest. [74]

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[73] It should be noted that the "appearance of impropriety standard" is not relevant to this analysis. Comment five (5) under Rule 1.9, dealing with the conflicts resulting from former clients states,

> The other rubric formerly used for dealing with disqualification is the appearance of impropriety proscribed in Canon 9 of the ABA Model Code of Professional Responsibility. This rubric has a twofold problem. First, the appearance of impropriety can be taken to include any new client-lawyer relationship that might make a former client feel anxious. If that meaning were adopted, disqualification would become little more than a question of subjective judgment by the former client. Second, since "impropriety" is undefined, the term "appearance of impropriety" is question begging. It therefore has to be recognized that the problem of disqualification cannot be properly resolved either by simple analogy to a lawyer practicing alone or by the very general concept of appearance of impropriety.

[74] Hearing transcript, Page 82, lines 7-14.

There is no evidence before this Court that HML consented to this arrangement, and it would not matter if it had because a Receiver could not fulfill his role as a fiduciary to HML and the creditors if he represented both simultaneously. This court therefore concludes that Arnowitz should not have been allowed to step into Zimmerman's shoes and **[*92]** act as Receiver paid for the work in April 2004.

As previously stated, with regard to the April 2004 fees there is no evidence that Zimmerman ever petitioned the court for permission to employ Arnowitz to fill in for him when he was on vacation as he was required to do. By failing to give the court the opportunity to rule on the desirability of Arnowitz acting as the Receiver, a conflicts problem was created. When viewed in context, it adds to the appearance that Zimmerman is more interested in spreading the wealth of the receivership estate, rather than acting in an economical and expedient manner. Thus, Arnowitz was nothing more than a volunteer and any fees paid to him should be returned to the receivership estate.

Arnowitz's Conflict of Interest: Hilti and Suffolk

The court also notes Arnowitz's simultaneous representation of HML's two unsecured creditors, Hilti and Suffolk, also presents a conflict of interest. Hilti and Suffolk were competing for limited funds in HML's receivership estate, and thus their positions are mutually antagonistic, rather than mutually aligned. In this case, there is a clear conflict of interest. Although there is not a direct conflict of interest, **[*93]** because Arnowitz is not acting as an advocate against a client that he represents in another matter, his simultaneous representation of Hilti and Suffolk materially affects his ability to zealously represent these respective clients in violation of MRPC 1.7(b).

This conflict is not cured by consent, because a disinterested lawyer would conclude that neither Hilti nor Suffolk nor HML should agree to the representation under the circumstances. When asked about this apparent conflict at the Hearing, Arnowitz stated that both of his clients had consented, although he offered no proof that this was the case. Assuming consent, the question then becomes whether "a disinterested lawyer would conclude that the client should not agree to the representation under the circumstances." MRPC 1.7, Comment 5.

As the attorney for a creditor it is Arnowitz's duty to maximize the monetary return for his creditor against HML. It would not be difficult to imagine a scenario where the interests of one creditor are antagonistic to that of another creditor, and this is where Arnowitz's simultaneous representation of Suffolk and Hilti, the only two remaining creditors, becomes problematic in both theory and **[*94]** practice. Indeed, Arnowitz's conflict of interest is perfectly illustrated by his supposedly *pro rata* distribution of payments to creditors Hilti and Suffolk. (See ***HN18***[↑] *G.L.c. 156B, § 106*, a Receiver is required to "distribute the funds ratably among the court approved creditors.") Arnowitz is a lawyer representing conflicting creditors, and not a creditor. The creditors are Hilti and Suffolk. Arnowitz stated at the Hearing that the payments from HML's estate were split *pro rata,* 95% to Suffolk and 5% to Hilti. Other than that representation, no other proof was presented to this Court. However the actual *pro rata* split of creditor payments between Suffolk and Hilti should have been 86% and 16% respectively. [75] If Hilti had had independent counsel there can be little doubt that they would have challenged Arnowitz's low distribution payment. With Arnowitz representing both Hilti and Suffolk there was nobody to fulfill and oversee the important function of protecting Hilti's rights. This perfectly illustrates why a disinterested lawyer would not recommend that a judgment creditor should be represented by an attorney who is also representing other judgment creditors of the same **[*95]** debtor corporation.

Zimmerman's Affidavit Against HML

In his Motion to Replace the Receiver, Xarras alleges that on June 21, 2005 Zimmerman signed and filed an affidavit advocating that the court assess treble damages against HML in the Suffolk case. [76] **[*96]** Xarras states that this is clearly against the interests of HML and constitutes a blatant breach of Zimmerman's fiduciary duty to HML. Zimmerman alleges in the affidavit that Xarras was negotiating on behalf of HML with the IRS without his authority. Subsequently, on December 21, 1999 the IRS, pursuant to a settlement agreement, adjusted HML's tax return(s) by adding $ 985,920.43 to its taxable income. Zimmerman stated that in settling the action with the IRS Xarras admitted that he had diverted $ 833,875 from HML in 1995 to the

[75] With HML owing $ 160,493.83 to Suffolk as of September 1999, and $ 26,139.99 to Hilti as of November 1997.

[76] Receiver's Affidavit in Support of the Plaintiff's Request for Separate Judgment and Treble Damages Against HML Development Corp. Attached as Exhibit "A" to Xarras's Motion to Replace Receiver.

detriment of creditors. [77]

It is perhaps noteworthy that Zimmerman states that he was "charged with the duty of collecting all HML Development Corp.'s assets for the benefit of its creditors," [78] and that he "owe[d] a duty" to the creditors of HML. [79] However it is clear that Zimmerman also owes a fiduciary duty to this court and HML, not just the creditors. This action adds weight to a finding that the Receiver should be removed as he is not acting in an impartial manner.

Xarras's Dilatory Motion to Remove the Receiver

HN19[⬆] Under *Mass.R.Civ.P. 5(b)*, service may be made by mailing the paper to the party or attorney at his last known address; if no address is known, the paper may be left with the clerk of court. Notice is complete upon depositing **[*97]** the correctly addressed, postage prepaid notice in the mailbox. See *Checkoway v. Cashman Bros. Co., 305 Mass. 470, 471, 26 N.E.2d 374 (1940)*. *Rule 5(d)* has been expanded to eliminate all formalities as to proof of service of papers upon other parties. If an adverse party challenges the adequacy of notice, the serving party will of course have to prove service. In order to minimize frivolous challenges, *Rule 5(d)* provides that a simple statement signed under the penalties of perjury will suffice to establish prima facie proof of service. The statement is designed to make explicit that the attorney's failure to supply proper proof of service does not invalidate the service if in fact it has been properly completed.

Xarras's Motion to Replace the Receiver must be viewed in light of the fact that Xarras waited seven years to contest any of the Receiver's actions. Zimmerman was appointed Receiver on March 19, 1999. Xarras did not file any oppositions to Zimmerman's Interim Expense Reports or Requests for Fees, and has not filed a Motion to Remove the Receiver until April 2006. Dombrowski filed a Motion to Intervene in the current action on April 20, 2006, which Hilti objected to because **[*98]** Dombrowski was allegedly already in the case and had been sent notices to everything filed in the case. [80] In the hearing Dombrowski stated that he had never seen a Motion to Reach and Apply Xarras and that he had first got into this case after Zimmerman filed a Complaint for Contempt against Xarras. [81] Dombrowski further stated that he was unaware that Xarras was an actual defendant in this case.

Notice to Dombrowski

The docket indicates Dombrowski as Xarras's attorney of record in this action since January 13, 2000. Indeed the first pleading bearing Dombrowski's signature in this case is the Assent of Parties Removal of Default, filed January 13, 2000. Each Interim Report and Request for Payment of Fees and Expenses has an attached signed affidavit of compliance from Zimmerman pursuant to *Superior Court Rule 9A(b)(2)*, in which he swears that service was made on Dombrowski **[*99]** at Dombrowski & Aveni, LLP, 6 Grove Avenue, Leominster, MA 01453. Each affidavit also states that "no response has been received from . . . Attorney Dombrowski, within three business days after the expiration of the time permitted for service of the response to the . . . Interim Report." In addition the docket reflects that notices were mailed to the attorneys of record after the court approved each report.

Zimmerman and Arnowitz have satisfied the notice requirements of *Rule 5(d) of the Massachusetts Rules of Civil Procedure.* Dombrowski has been the attorney of record since January 13, 2000 and cannot claim that he did not have notice of Zimmerman's activities. However, the delayed nature of HML's Motion to Remove the Receiver is heavily outweighed by the merit of the motion to Replace the Receiver.

CONCLUSION

The actions of Zimmerman and Arnowitz cannot be viewed in isolation, but must be viewed together, and in view of their undoubted close professional relationship. This court has no doubt, that Zimmerman's and Arnowitz's close professional relationship colored decisions that they have made with regard to the receivership estate. Zimmerman's failure **[*100]** to promptly foreclose on the Fitchburg and Westminster Properties is ample evidence that Zimmerman was more interested in extending the length of the receivership as a vehicle for generating fees for himself and his associates, rather than as a prompt and efficient mechanism for liquidating all of HML's assets and making rapid payments to creditors and then shareholders as the statute requires.

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[77] As noted these allegations against HML in the Suffolk case were found to be without merit.

[78] Affidavit, Page 2, Paragraph 3.

[79] Affidavit, Page 3, Paragraph 7.

[80] Hearing transcript, page 19, lines 1-3.

[81] The Complaint for Contempt was filed in November 1999.

Specifically this court finds that since his appointment as Receiver in this case in March 1999 Zimmerman has: (1) failed to properly carry out his statutory duty to expeditiously liquidate the assets of HML and make prompt payments to creditors; (2) failed to adequately scrutinize Arnowitz's highly questionable 2004 request for payment of fees and expenses from the HML estate; (3) failed to ask the court for permission to hire attorneys to assist him in the receivership, and then billing the receivership estate for their time; (4) failed to ask court permission to have Arnowitz act as Receiver when he was on vacation in April 2004; (5) breached his duty to HML by submitting an affidavit for Arnowitz advocating the imposition of treble damages against HML in the Suffolk case; (6) acted improperly **[*101]** by employing the Boston-based husband of an associate in his firm to act as property manager of the Fitchburg property, and then paying his fees from the receivership estate; (7) failed to provide the court with a detailed inventory of possessed property, or property as to which the Receiver has a right to possession within 30 days of his appointment, and failed to seek an extension of time from the court if required; and (8) failed to file any annual detailed report of the condition of the receivership by February 19 of each year pursuant to *Mass.R.Civ.P. 66(c)*; (9) failure to comply with orders of Murphy, J. and McCann, J. to deposit funds in an interest-bearing account.

As such, it is apparent to this court that it would be in the interest of all parties to replace Zimmerman as Receiver for HML. Zimmerman should be replaced with a Receiver that is entirely independent and unaffected by any relationship to the creditors in this case. In that way the court can ensure, as it is bound to do, that the Receiver is in the best possible position to properly fulfill the fiduciary duty that he owes to HML, HML's creditors and to this court.

ORDER

It is therefore **[*102]** *ORDERED* that the Motion to Replace the Receiver is *ALLOWED* and it is *ORDERED* as follows:

HML's Motion to Replace the Receiver is Allowed.

Zimmerman's Motion for Reconsideration of the Escrow of his Fees is Denied.

Arnowitz's Motion for Reconsideration of the Escrow of his Fees is Denied and his Cross Motion for Costs is Denied.

Arnowitz's Emergency Motion for Reconsideration Seeking a Stay of the Court's Sua Sponte Order Dated May 15, 2006 and the Court's Denial of Arnowitz's Motion for Reconsideration is denied.

The Court *VACATES* the Order of Peter L. Zimmerman as Receiver and Discharges him.

The Court appoints Roy A. Bourgeois as Receiver and he shall post the statutory bond as a condition of his appointment. All assets presently held by the Discharge Receiver Peter L. Zimmerman shall be transferred forthwith to Roy A. Bourgeois.

The Court takes no action at present on the Fifth Interim Account.

In addition to his normal duties as receiver, Roy A. Bourgeois is directed to review the entire receivership proceeding in light of this report and to make such recommendations to this Court as he sees fit.

John S. McCann

Justice of the Superior Court

Dated: February 5, 2007

End of Document

Exco Res. v. Milbank

United States District Court for the Southern District of New York

January 28, 2003, Decided ; February 3, 2003, Filed

02 Civ. 5638 (BSJ)

Reporter
2003 U.S. Dist. LEXIS 1442 *

In re ENRON CORP., et al., EXCO RESOURCES, INC., Appellant v. MILBANK, TWEED, HADLEY & MCCLOY LLP, et al., Appellees.

Disposition: [*1] Bankruptcy court's decision affirmed. Request to set aside bankruptcy court's decision and to disqualify counsel for Official Committee of Unsecured Creditors denied.

Core Terms

bankruptcy court, adverse interest, transactions, disclosures, alleges, investment banker, connections, conflicts, disinterested, structured, retention, matters, unsecured creditor, disqualify, asserts, argues, disqualification motion, supplemental, finance, agrees, bankruptcy proceedings, fail to disclose, representations, Remarketing, speculation, disclose, entities, bidders, parties, trading

Case Summary

Procedural Posture
Debtors filed voluntary petitions for relief under Chapter 11. The United States Bankruptcy Court approved appellee law firm as counsel for the committee of unsecured creditors. Appellant creditor later objected to the law firm's monthly fee statement and moved to disqualify the law firm as counsel for the committee. The bankruptcy court denied the motion. The creditor appealed the decision.

Overview

The creditor had standing to bring the appeal because as an unsecured creditor, it would have been directly and pecuniarily affected if the law firm's interests were adverse to the committee's interests and if the law firm had failed to disclose its relationships. The bankruptcy court's order denying the disqualification motion was a final, appealable order as a footnote related to the law firm's future involvement did not suggest that the bankruptcy court would have reconsidered its decision on the disqualification motion. Moreover, the creditor's failure to name the committee as an appellee did not warrant dismissal as it had named itself as required under *Fed. R. Bankr. P. 8001(a)*. On the merits, the law firm's disclosures complied with *Fed. R. Bankr. P. 2014* as they fully disclosed the relevant facts concerning its relationships and its relevant connections to potential parties. The law firm had not violated *11 U.S.C.S. § 1103(b)* as its alleged adverse interests relating to structured finance transactions pre-dated the firm's representation of the committee. The law firm also satisfied *11 U.S.C.S. § 101(14)* because it was disinterested and did not hold an adverse interest.

Outcome
The decision was affirmed.

LexisNexis® Headnotes

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

Civil Procedure > ... > Justiciability > Standing > Injury in Fact

Constitutional Law > The Judiciary > Case or Controversy > General Overview

Civil Procedure > Preliminary Considerations > Justiciability > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

HN1 **Procedural Matters, Judicial Review**

In every federal case, the threshold question in determining the power of the court to hear the case is whether a claimant has standing. The criteria for standing in a bankruptcy proceeding is more stringent than the injury in fact requirement under U.S. Const. art. III. In the Second Circuit, a party appealing a bankruptcy court ruling must be an aggrieved person. An aggrieved person is one that is directly and adversely affected pecuniarily by the challenged order of the bankruptcy court.

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

Civil Procedure > Appeals > Reviewability of Lower Court Decisions > Adverse Determinations

Civil Procedure > ... > Justiciability > Standing > General Overview

HN2 **Procedural Matters, Judicial Review**

Generally, a creditor has standing to appeal a bankruptcy order that disposes of the estate's property because such orders directly affect the funds available to meet a creditor's claims. However, an unsubstantiated, speculative, and indirect effect on the party's pecuniary interests is not enough to establish appellate standing.

Civil Procedure > ... > Justiciability > Standing > General Overview

Governments > Fiduciaries

Torts > Intentional Torts > Breach of Fiduciary Duty > General Overview

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

HN3 **Justiciability, Standing**

In the context of a bankruptcy proceeding, the standing requirement is not entirely inflexible. The United States Court of Appeals for the Second Circuit, for instance, finds that an unsuccessful bidder, who calls into question the intrinsic fairness of a bankruptcy sale transaction, has appellate standing.

Bankruptcy Law > Procedural Matters > Judicial Review > Jurisdiction

Civil Procedure > Attorneys > Disqualification of Counsel

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

Civil Procedure > Attorneys > General Overview

Civil Procedure > Appeals > Appellate Jurisdiction > Final Judgment Rule

HN4 **Judicial Review, Jurisdiction**

Pursuant to 28 U.S.C.S. § 158(a)(1), an appeal from a bankruptcy court order may be taken as of right if the order is final. In non-bankruptcy cases, an order denying a motion to disqualify counsel in a civil case is not an appealable, final order.

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

Civil Procedure > Appeals > Appellate Jurisdiction > Final Judgment Rule

HN5 **Procedural Matters, Judicial Review**

A more flexible standard of finality applies in a bankruptcy case. Within a bankruptcy context, orders may be immediately appealable if they finally dispose of discrete disputes within the larger case. The United States Court of Appeals for the Second Circuit holds in a line of cases that bankruptcy court orders granting or denying the retention of counsel dispose of such disputes and are, therefore, final and appealable.

Bankruptcy Law > Procedural Matters > General Overview

Civil Procedure > Appeals > Reviewability of Lower Court Decisions > Timing of Appeals

Bankruptcy Law > ... > Bankruptcy > Case Administration > Notice

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

Bankruptcy Law > Procedural Matters > Judicial Review > Bankruptcy Appeals Procedures

HN6 **Bankruptcy Law, Procedural Matters**

Under Fed. R. Bankr. P. 8001(a), a notice of appeal shall contain the names of all parties to the judgment, order, or decree appealed from. Rule 8001(a) also states that an appellant's failure to take any step other than timely filing a notice of appeal does not affect the validity of the appeal, but is ground only for such action as the district court deems appropriate, which may include dismissal of the appeal.

Bankruptcy Law > Procedural Matters > Judicial Review > Jurisdiction

Civil Procedure > Appeals > Reviewability of Lower Court Decisions > Timing of Appeals

Bankruptcy Law > ... > Bankruptcy > Case Administration > Notice

Bankruptcy Law > Procedural Matters > General Overview

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

HN7 **Judicial Review, Jurisdiction**

The time period for filing a notice of appeal is strictly enforced and failure to timely file deprives the district court of jurisdiction to review the bankruptcy court's order. Moreover, failure to name an appealing party may preclude that party's appeal. Because other defects are not jurisdictional, it is within the district court's discretion to take such action as it deems appropriate.

Bankruptcy Law > Procedural Matters > Judicial Review > Bankruptcy Appeals Procedures

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

HN8 **Judicial Review, Bankruptcy Appeals Procedures**

The standard by which the district court is to review an order of the bankruptcy court is set forth in Fed. R. Bankr. P. 8013.

Bankruptcy Law > Procedural Matters > Judicial Review > Bankruptcy Appeals Procedures

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

Bankruptcy Law > ... > Judicial Review > Standards of Review > Clear Error Review

HN9 **Judicial Review, Bankruptcy Appeals Procedures**

See Fed. R. Bankr. P. 8013.

Bankruptcy Law > ... > Judicial Review > Standards of Review > Clear Error Review

Civil Procedure > Appeals > Standards of Review > De Novo Review

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

Bankruptcy Law > ... > Judicial Review > Standards of Review > De Novo Standard of Review

Civil Procedure > Appeals > Standards of Review > Clearly Erroneous Review

HN10 **Standards of Review, Clear Error Review**

The district court will accept the bankruptcy court's findings of fact unless they are clearly erroneous. The district court will review the bankruptcy court's legal conclusions de novo.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

Civil Procedure > Attorneys > General Overview

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

HN11[] Professional Services, Retention of Professionals

A party's choice of counsel is entitled to great deference. Disqualification motions are viewed with disfavor because they interfere with a party's right to employ the counsel of its choice. Mere speculation will not suffice to establish sufficient grounds for disqualification.

Bankruptcy Law > Procedural Matters > Judicial Review > Bankruptcy Appeals Procedures

Bankruptcy Law > Procedural Matters > Judicial Review > General Overview

HN12[] Judicial Review, Bankruptcy Appeals Procedures

On appeal, the district court will only consider the record that was before the bankruptcy court. Fed. R. Bankr. P. 8006. The district court, therefore, will disregard any argument or document that appears for the first time on appeal.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > Debtors in Possession & Trustees

Bankruptcy Law > Case Administration > Examiners, Officers & Trustees > United States Trustee

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

HN13[] Retention of Professionals, Debtors in Possession & Trustees

Under Fed. R. Bankr. P. 2014(a), a professional seeking employment in a bankruptcy case is required to submit an application that states to the best of the applicant's knowledge, all of the person's connections with the debtor, creditors, and any other party in interest. Rule 2014(a) also requires the applicant to submit a verified statement setting forth these connections. The purpose of Rule 2014(a) is to provide the court and the United States trustee with information to determine whether the professional's employment is in the best interest of the estate. Fed. R. Bankr. P. 2014 disclosures are to be strictly construed and failure to disclose relevant connections is an independent basis for the bankruptcy court to disallow fees or to disqualify the professional from the case.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

HN14[] Professional Services, Retention of Professionals

Although Fed. R. Bankr. P. 2014(a) does not expressly require supplemental disclosures, they are necessary to preserve the integrity of the bankruptcy system.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

HN15[] Professional Services, Retention of Professionals

Under Fed. R. Bankr. P. 2014, an attorney seeking employment in a bankruptcy case must ensure that all relevant connections have been brought to light. The rule does not, however, require detailed description of those connections, such as every possible consequence resulting from the attorney's connections or a prediction as to the outcome of any possible litigation that may relate to the attorney's connections. The United States District Court for Southern District of New York finds that such disclosures are beyond the scope of Fed. R Bankr. P. 2014.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

HN16[] Professional Services, Retention of Professionals

See 11 U.S.C.S. § 1103(b).

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

HN17[] Professional Services, Retention of Professionals

An attorney violates 11 U.S.C.S. § 1103(b) if the attorney simultaneously represents both a committee of unsecured creditors and another party, with an interest adverse to the committee, in matters related to the bankruptcy proceeding. Section 1103(b) is not violated if the attorney represents an entity with an adverse interest in a matter unrelated to the bankruptcy case or in a matter that pre-dates the attorney's representation of the committee.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > Debtors in Possession & Trustees

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Bankruptcy Law > Case Administration > Examiners, Officers & Trustees > General Overview

Bankruptcy Law > Case Administration > Professional Services > General Overview

Bankruptcy Law > ... > Retention of Professionals > Compensation > Limitations on Compensation

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

Bankruptcy Law > ... > Professional Services > Retention of Professionals > Retention by Committees

HN18[] Retention of Professionals, Debtors in Possession & Trustees

The requirements of 11 U.S.C.S. § 327(a) concern solely the employment of professionals by a trustee or a debtor. Section 327(a) requires that the professional not hold an adverse interest to the estate and that the professional be disinterested under 11U.S.C.S. § 101(14). However, 11 U.S.C.S. § 328(c) of the Bankruptcy Code allows a bankruptcy court to deny compensation to a professional employed under either 11 U.S.C.S. §§ 327 or 1103 if that professional is not disinterested or holds an adverse interest. Consequently, at least one case has held that, notwithstanding the language of § 1103, the disinterested and adverse interest requirements of § 327(a) also apply to the initial retention of counsel for a committee under § 1103.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

HN19[] Professional Services, Retention of Professionals

Under 11 U.S.C.S. § 101(14), a disinterested person is defined, in part, as any person that (1) has not been, within three years before the date of the filing of the petition, an investment banker for a security of the debtor, or an attorney for such an investment banker in connection with the offer, sale, or issuance of a security of the debtor; and (2) does not have an interest materially adverse to the interest of the estate or of any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor or an investment banker or for any other reason. 11 U.S.C.S. § 101(14)(C), (E).

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

HN20[] Professional Services, Retention of Professionals

Merely hypothesizing that conflicts may arise is not sufficient to warrant the disqualification of an attorney in a bankruptcy proceeding.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

HN21[] Professional Services, Retention of Professionals

For purposes of determining whether an attorney's prior representations disqualifies that attorney in a bankruptcy proceeding, an adverse interest is defined as follows: (1) to possess or assert any economic interest that would tend to lessen the value of the bankruptcy estate or that would create either an actual or potential dispute in which the estate is a rival claimant; or (2) to possess a predisposition under circumstances that render such a bias against the estate.

Bankruptcy Law > Procedural Matters > Professional Responsibility

Legal Ethics > Client Relations > Appearance of Impropriety

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

Legal Ethics > Client Relations > Conflicts of Interest

HN22[] **Procedural Matters, Professional Responsibility**

Bankruptcy courts look to the Code of Professional Responsibility in analyzing attorney conflicts of interest.

Counsel: For Exco Resources, Inc, APPELLANT: Michael P Cooley, Gardere Wynne Sewell, LLP, Dallas, TX USA.

For Milbank Hadley Tweed & McCloy, LLP, APPELLEE: Luc A Despins, Milbank, Tweed, Hadley & McCloy, LLP, New York, NY USA.

For Enron Corp, DEBTOR: John C Nabors, Deirdre B Ruckman, Michael P Cooley, Gardere Wynne Sewell, LLP, Dallas, TX USA.

Carolyn S Schwartz, TRUSTEE.

Judges: BARBARA S. JONES, UNITED STATES DISTRICT JUDGE.

Opinion by: BARBARA S. JONES

Opinion

MEMORANDUM & ORDER

BARBARA S. JONES

UNITED STATES DISTRICT JUDGE

On December 2, 2001, and periodically thereafter, Enron Corporation and certain of its affiliated entities (collectively, the "Debtors") filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code. The U.S. Trustee formed the Official Committee of Unsecured Creditors ("Committee"), which sought to retain Appellee Milbank, Tweed, Hadley & McCloy LLP ("Milbank") as its counsel in the bankruptcy proceedings. On January 28, 2002, the **[*2]** bankruptcy court signed an order approving Milbank as the Committee's counsel. On March 19, 2002, Appellant Exco Resources, Inc. ("Exco"), a creditor of Enron North America, filed an objection to a monthly fee statement of Milbank and moved to disqualify Milbank as counsel for the Committee. Several creditors joined the motion. The bankruptcy court held a hearing on May 15, 2002 and, in a decision and order dated May 23, 2002, denied Exco's motion to disqualify Milbank. Exco now appeals the bankruptcy court's decision and order. In addition to Milbank, the Committee, the United States Trustee and the Debtors have all submitted briefs in opposition to Exco's motion. For the reasons set forth below, this Court affirms the decision of the bankruptcy court denying Exco's motion to disqualify Milbank as counsel for the Committee.

Jurisdiction

As a preliminary matter, this Court must address whether it has appellate jurisdiction in this case. Appellees Milbank and the Committee challenge this Court's jurisdiction on the following grounds: first, Exco lacks standing to appeal; second, the bankruptcy court's order was not final; and third, Exco failed to name the Committee as an **[*3]** appellee.

HN1[] In every federal case, the threshold question in determining the power of the court to hear the case is whether a claimant has standing. See *Warth v. Seldin, 422 U.S. 490, 498, 45 L. Ed. 2d 343, 95 S. Ct. 2197 (1975)*. The criteria for standing in a bankruptcy proceeding is more stringent than the "injury in fact" requirement under Article III. See *Kane v. Johns-Manville Corp., 843 F.2d 636, 642 n.2 (2d Cir. 1988)*. In the Second Circuit, a party appealing a bankruptcy court ruling must be an "aggrieved person." *Licensing by Paola, Inc. v. Sinatra, 126 F.3d. 380, 388 (2d Cir. 1997)*.

An aggrieved person is one that is "directly and adversely affected pecuniarily by the challenged order of the bankruptcy court." Id.

The Committee argues that Exco lacks standing because it is not an aggrieved person and because it is asserting the rights of the Committee, rather than its own rights. *HN2*[] Generally, a creditor has standing to appeal a bankruptcy order that disposes of the estate's property because such orders directly affect the funds available to meet a creditor's claims. Id.; *Kane, 843 F.2d at 642*. However, **[*4]** an "unsubstantiated, speculative, and indirect effect" on the party's pecuniary interests is not enough to establish appellate standing. See *In re Victory Markets, Inc., 195 B.R. 9, 15-16 (N.D.N.Y. 1996)* (rejecting appellant's claim that committee's inadequate representation resulted in pecuniary loss).

Exco alleges that the bankruptcy court should never have approved Milbank as counsel for the Committee because Milbank's disclosures of conflicts were inadequate. Exco also alleges that Milbank's interests in the Chapter 11 cases are adverse to the interests of the Committee and the unsecured creditors. While this Court is aware that granting appeals to any person affected by a bankruptcy court order "will sound the death knell of the orderly disposition of bankruptcy matters," *In re Gucci, 126 F.3d 380, 388 (2d Cir. 1997)*, Exco's appeal is not outside the limits of appellate standing. If Milbank's interests were indeed adverse to those of the Committee and if Milbank did fail to adequately disclose its relationships, Exco, as an unsecured creditor, would be directly, pecuniarily affected. In *In re Arochem Corp., 176 F.3d 610 (2d Cir. 1999)*, **[*5]** appellants, certain creditors, objected to the trustee's employment of counsel, arguing that counsel's retention conflicted with its representation of a certain unsecured creditor. See *Arochem 176 F.3d at 616*. When the bankruptcy court approved counsel's employment, the creditors appealed. See *id. at 618*. Both the district court and the Second Circuit heard the appeal and affirmed the bankruptcy court's retention order on the merits. See *id. at 620*.

Moreover, *HN3*[] the standing requirement is not entirely inflexible. The Second Circuit, for instance, has found an "unsuccessful bidder," who calls into question the "intrinsic fairness" of a bankruptcy sale transaction, also has appellate standing. See *In re Colony Hill Assocs., 111 F.3d 269, 274 (2d Cir. 1997)*. Exco alleges, among other things, that Milbank, to the detriment of the unsecured creditors, failed to disclose relationships with certain bidders. Exco alleges that the Committee consequently breached its fiduciary duty to ENA creditors such as Exco. Like the unsuccessful bidder, Exco questions the intrinsic fairness of this bankruptcy proceeding if Milbank is permitted **[*6]** to continue to represent the Committee. Accordingly, Exco has standing to appeal the bankruptcy court's denial of its motion to disqualify Milbank as counsel for the Committee.

Appellee Milbank further contends that the Court should dismiss Exco's appeal because the bankruptcy court's decision is not a final order. *HN4*[] Pursuant to *28 U.S.C. § 158(a)(1)*, an appeal from a bankruptcy court order may be taken as of right if the order is final. In non-bankruptcy cases, an order denying a motion to disqualify counsel in a civil case is not an appealable, final order. See *Firestone Tire & Rubber Co v. Risjord, 449 U.S. 368, 379, 66 L. Ed. 2d 571, 101 S. Ct. 669 (1981)*.

However, *HN5*[] "a more flexible standard of finality" applies in a bankruptcy case. *In re Johns Manville Corp., 920 F.2d 121, 126 (2d Cir. 1990)*. Within a bankruptcy context, orders "may be immediately appealable if they finally dispose of discrete disputes within the larger case." Id. The Second Circuit has held in a line of cases that bankruptcy court orders granting or denying the retention of counsel dispose of such disputes and are, therefore, final and appealable. **[*7]** See *Arochem, 176 F.3d at 620*; *In re Kurtzman, 194 F.3d 54, 57 (2d Cir. 1999)*; see also *In re Palm Coast, Matanza Shores Ltd. P'ship, 101 F.3d 253, 256 (2d Cir. 1996)* (order authorizing trustee to retain real estate consultant was a final order).

Milbank attempts to distinguish these cases by noting that they involved an order granting or denying counsel's employment *in the first instance,* rather than, as here, an order denying a *midstream* motion to disqualify counsel previously appointed without objection. Such distinction is without consequence. In both scenarios, the bankruptcy court is deciding a conflict issue. In AroChem, the Second Circuit made no such distinction. The court began its analysis of the order's finality with the Supreme Court's non-bankruptcy rule that "orders granting or denying motions to disqualify counsel are not considered final and are not immediately appealable." *Arochem, 176 F.3d at 619* (citing *Richardson-Merrell, Inc. v. Koller, 472 U.S. 424, 440, 86 L. Ed. 2d 340, 105 S. Ct. 2757 (1985)*; *Firestone, 449 U.S. at 379*)). Then the court held the **[*8]** order to be final and appealable because of the

more flexible standard of finality that applies in bankruptcy cases -- not because the order involved the initial retention of counsel. See Arochem, 176 F.3d at 620; see also In re Vebeliunas, 246 B.R. 172, 173 (S.D.N.Y. 2000) (noting that Arochem, Palm Coast and Kurtzman "affirm jurisdiction over appeals from orders granting or denying motions to disqualify counsel" in bankruptcy proceedings).

In Palm Coast, Arochem, and Kurtzman, the Second Circuit ultimately determined that the bankruptcy order was final because "nothing in the order of the bankruptcy court … indicates any anticipation that the decision will be reconsidered." Arochem, 176 F.3d at 620 (quoting Palm Coast, 101 F.3d at 256); Kurtzman, 194 F.3d at 57. In the instant appeal, Milbank contends that the bankruptcy court's order is not final because in a footnote the court stated that "the better course of action is to address these issues if and when the events were to occur." This statement, however, relates to Exco's speculation concerning Milbank's potential involvement **[*9]** in future litigation regarding Enron transactions. The court explained that "considering the limited scope of Milbank's retention concerning the transactions and the involvement of conflicts counsel in the investigation of the transactions, at this point, the speculation that Milbank may become a defendant or a witness is not sufficient to warrant a finding of adverse interest on Milbank's part." The court does not suggest that it will reconsider its decision relating to Exco's present motion. Moreover, in denying Exco's motion, the bankruptcy court also denied a request to hold the motion in abeyance. Accordingly, this Court finds that the bankruptcy court's order is a final, appealable order.

In its final argument challenging this Court's jurisdiction, Appellee Committee asserts that, by failing to name the Committee as an appellee, Exco did not comply with Bankruptcy Rule 8001(a). HN6[↑] Rule 8001(a) provides that "the notice of appeal shall … contain the names of all parties to the judgment, order, or decree appealed from …." Fed. R. Bankr. P. 8001(a). Rule 8001(a) also states that "an appellant's failure to take any step other than timely filing a notice of appeal does not affect **[*10]** the validity of the appeal, but is ground only for such action as the district court … deems appropriate, which may include dismissal of the appeal." Fed. R. Bankr. P. 8001(a).

HN7[↑] The time period for filing a notice of appeal is strictly enforced and failure to timely file deprives the district court of jurisdiction to review the bankruptcy court's order. See In re New York Hostel, Inc., 194 B.R. 313, 316 (S.D.N.Y. 1996). Moreover, failure to name an *appealing* party may preclude that party's appeal. See In re Pettibone Corp., 145 B.R. 570, 574 (N.D. Ill. 1992). Exco adequately named itself as the appellant in the notice of appeal. Because other defects are not jurisdictional, it is within the Court's discretion to take such action as it deems appropriate. See Medford Industries v. Lennar Partners, Inc., 205 B.R. 23 (E.D.N.Y. 1996). This Court finds that Exco's failure to name the Committee as an appellee does not warrant dismissal. [1] Accordingly, the Court will hear Exco's appeal.

[*11] Merits [2]

HN8[↑] The standard by which this Court is to review an **[*12]** order of the bankruptcy court is set forth in Rule 8013 of the Federal Rules of Bankruptcy Procedure:

> HN9[↑] On an appeal the district court or bankruptcy appellate panel may affirm, modify, or reverse a bankruptcy judge's judgment, order, or decree or remand with instructions for further proceedings. Findings of fact, whether based on oral or documentary evidence, shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the bankruptcy court to judge the credibility of witnesses.

Fed. R. Bankr. P. 8013.

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[1] Moreover, even if the Court decided that the deficiency warranted dismissal, its jurisdiction would be curtailed only with respect to the Committee, and not as to the parties that Exco properly named. See In re Novon Int'l Inc., No. 98cv0677E(F), 2000 U.S. Dist. LEXIS 5169, 2000 WL 432848, *1 (W.D.N.Y. March 31, 2000).

[2] In its decision, the bankruptcy court discussed Exco's delay in bringing this motion and concluded that such delay would provide a separate ground to deny the relief sought by Exco. The Committee's application to retain Milbank and Milbank's affidavit in support of that application were filed by January 16, 2002. Exco did not file any objections to the application. Nor did Exco appeal the bankruptcy court's January 28, 2002 order approving Milbank's retention. Exco did not file its motion seeking to disqualify Milbank until March 9, 2002, even though, as the bankruptcy court noted, the "underlying basis for the motion" was known to Exco no later than mid-January. This Court agrees with the bankruptcy court's finding that there was an unjustified delay on the part of Exco in bringing this motion. However, because of the seriousness of the allegations, the bankruptcy court addressed the merits and did not deny Exco's motion as untimely.

Thus, HN10[] the Court will accept the bankruptcy court's findings of fact unless they are clearly erroneous. See In re Manville Forest Products Corp., 896 F.2d 1384, 1388 (2d Cir. 1990). This Court will review the bankruptcy court's legal conclusions de novo. See id.

HN11[] A party's choice of counsel is entitled to great deference. See, e.g., Board of Educ. v. Nyquist, 590 F.2d 1241, 1246 (2d Cir. 1979). Disqualification motions are viewed with disfavor because they interfere with a party's right to employ the counsel of its choice. See A.V. By Versace, Inc. v. Gianni Versace, S.p.A., 160 F. Supp. 2d 657, 662-63 (S.D.N.Y. 2001); **[*13]** Universal City Studios, Inc. v. Reimerdes, 98 F. Supp. 2d 449, 455 (S.D.N.Y. 2000). Mere speculation will not suffice to establish sufficient grounds for disqualification. See A.V. By Versace, Inc., 160 F. Supp. 2d at 663.

Exco contends that three reasons exist to warrant Milbank's disqualification: first, during the retention application process, Milbank allegedly failed to disclose substantial conflicts and connections between itself and Debtors, creditors and Committee members; second, under Bankruptcy Code §§ 101, 327, 328 and 1103, Milbank allegedly fails to satisfy the "disinterested person" standard and violates the requirement that it not hold or represent an "adverse interest" and; and third, Milbank's retention allegedly violates the Canons of Professional Ethics and the Disciplinary Rules. [3]

[*14] *Disclosures*

HN13[] Bankruptcy Rule 2014(a) requires a professional seeking employment in a bankruptcy case to submit an application that states "to the best of the applicant's knowledge, all of the person's connections with the debtor, creditors, and any other party in interest …." Fed. R. Bankr. P. 2014(a). Rule 2014(a) also requires the applicant to submit a "verified statement" setting forth these connections. Id. The purpose of Rule 2014(a) is to provide the court and the United States trustee with information to determine whether the professional's employment is in the best interest of the estate. See In re The Leslie Fay Co., Inc., 175 B.R. 525, 532 (S.D.N.Y. 1994). Rule 2014 disclosures are to be strictly construed and failure to disclose relevant connections is an independent basis for the bankruptcy court to disallow fees or to disqualify the professional from the case. See id. 175 B.R. at 533.

Exco argues that Milbank failed to disclose numerous conflicts and connections. For instance, Exco alleges that Milbank failed to timely disclose its involvement in a transaction relating to Enron Wind Corporation ("Enron Wind"), an affiliated **[*15]** Enron debtor. On December 27, 2001, the bankruptcy court issued an order approving Enron's application to sell some assets of Enron Wind's non-debtor subsidiary, Enron Wind Development Corp. Exco asserts that Milbank did not completely disclose until its March 11, 2002 fee application that, during the transaction, it had represented both Enron Wind Development Corp. and the Committee and it simultaneously billed both the Enron estate and Enron Wind.

The bankruptcy court found, however, that Milbank's disclosures concerning the Enron Wind transaction complied with the requirements of Rule 2014 and that its disclosures "provided the court, the United States Trustee and any party in interest with adequate information to enable them to take whatever action, if any, deemed necessary regarding Milbank's retention." The bankruptcy court found that Milbank fully disclosed its relationships relating to the Enron Wind transaction in the January 15, 2002 affidavit in support of the application to retain Milbank as counsel for the Committee ("January 15th Affidavit"). The bankruptcy court also found that the relevant facts were fully disclosed in the pleadings filed by Weil, Gotshal & Manges **[*16]** LLP and that Milbank's dual representation was due to exigent circumstances. Moreover, American Electric Power Company, not Enron Wind, paid Milbank. Having reviewed Milbank's January 15th Affidavit and Milbank's several supplemental affidavits, this Court agrees with the bankruptcy court's findings.

Next, Exco alleges that Milbank allowed only its own clients to bid on the sale of Debtors' Trading Unit, which generated a $ 2 billion profit over a nine to twelve month period of time prior to the bankruptcy. The sale of the trading unit involved Citibank, JP Morgan Chase and UBS Warburg, as the three bidders, and The Blackstone Group L.P. as the investment banker conducting the

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[3] HN12[] On appeal, this Court will only consider the record that was before the bankruptcy court. See In re Davis, 169 B.R. 285, 293 (E.D.N.Y. 1994); Fed. R. Bankr. P. 8006. The Court, therefore, will disregard any argument or document that appears for the first time on this appeal, including but not limited to, the newspaper articles that appeared after the bankruptcy court's May 23, 2002 order.

auction. The bankruptcy court approved the sale of the trading unit to UBS Warburg on January 18, 2002. Exco alleges that Milbank failed to disclose its connections to the parties involved in the sale, namely Enron, Citibank, JP Morgan Chase, UBS Warburg and The Blackstone Group.

At the May 15, 2002 hearing before the bankruptcy court, however, counsel for Debtors argued that the Committee did not make any decisions regarding how the sale of Debtors' trading units would be conducted. As Debtors explained, their **[*17]** counsel -- not Milbank -- controlled the sale. Moreover, the bankruptcy court correctly found that Milbank disclosed in its January 15th Affidavit that it had represented the bidders in matters unrelated to the Enron trading unit transaction.

Exco also alleges that Milbank failed to adequately disclose its relationship with certain underwriters in structured finance transactions, such as Mahonia, Marlin I, Osprey I, Osprey II, and six credit-linked note transactions. Exco argues that Milbank should have specified the names of the underwriters and the amounts involved so that an interested party could determine whether there was a problem with Milbank's representation of the Committee. Exco also argues that Milbank failed to disclose the nature and magnitude of the Credit-Linked Note transactions.

The bankruptcy court found, however, that Milbank's disclosures of the Mahonia transaction in the January 15th Affidavit complied with *Rule 2014*. Milbank also disclosed in the January 15th Affidavit that it had represented the six investment bankers in the credit-linked note transactions. Moreover, Milbank disclosed in its "Engagement Limitations" that, because of prior representations of **[*18]** certain Enron companies, there were limitations on the scope of its representation of the Committee and that conflicts counsel would handle matters outside of Milbank's scope. As is evident from the "Engagement Limitations," Milbank is not representing the Committee in any matters that Exco has identified as situations in which Milbank has an adverse interest. This Court has reviewed Milbank's disclosures concerning the structured finance transactions and concludes that the bankruptcy court's findings are not clearly erroneous.

Milbank's January 15th Affidavit was twenty-nine pages long and contained four exhibits. In this affidavit and exhibits, Milbank extensively disclosed connections with potential parties of interest in the case. Milbank also disclosed its former representations of Enron entities and of other clients involved with Enron. In the January 15th Affidavit, Milbank agreed to provide regular supplements to the affidavit to provide additional disclosure of its relevant connections. To that end, Milbank has submitted six supplemental disclosures to continually reflect the nature of any relationship with new parties in interest and to expand upon prior disclosures. **[*19]** See *In re Granite Partners, L.P., 219 B.R. 22, 35* (noting that ***HN14***[⬆] although *Rule 2014(a)* does not expressly require supplemental disclosures, they are necessary to preserve the integrity of the bankruptcy system). While Exco maintains that the supplemental disclosures demonstrate that Milbank's disclosures are untimely and inadequate, this Court finds that the supplemental disclosures support the bankruptcy court's finding that Milbank's disclosures have been "meaningful, forthright, continuous and sufficiently detailed."

HN15[⬆] *Rule 2014* requires Milbank to ensure all relevant connections have been brought to light. See *In re Leslie Fay Co., Inc., 175 B.R. at 533*. The rule does not, however, require the detailed description of those connections that Exco proposes in this case. The bankruptcy court found that Exco would require Milbank to disclose information beyond the requirements of *Rule 2014*, such as every possible consequence resulting from Milbank's connections, as well as a prediction as to the outcome of any possible litigation that may relate to its connections. This Court agrees with the bankruptcy court that such disclosures are beyond the scope of **[*20]** *Rule 2014* and that Milbank's disclosures complied with *Rule 2014*. *Adverse Interests/ Disinterestedness*

Exco alleges that Milbank has adverse interests that require its disqualification under *11 U.S.C. §§ 1103*, *327*, and *328*. The bankruptcy court found Milbank does not hold or represent an adverse interest under any of these sections. *§ 1103(b)* states:

> ***HN16***[⬆] An attorney or accountant employed to represent a committee appointed under section 1102 of this title may not, while employed by such committee, represent any other entity having an adverse interest in connection with the case. Representation of one or more creditors of the same class as represented by the committee shall not per se constitute the representation of an adverse interest.

11 U.S.C. § 1103(b).

HN17[↑] Milbank violates § 1103(b) if it simultaneously represents both the Committee and another party, with an interest adverse to the committee, in matters related to the bankruptcy proceeding. See Daido Steel Co., Ltd., v. Official Comm. Of Unsecured Creditors, 178 B.R. 129, 132 (N.D. Ohio 1995). Section 1103(b) is not violated if Milbank represents **[*21]** an entity with an adverse interest in a matter *unrelated* to the bankruptcy case or in a matter that *pre-dates* Milbank's representation of the Committee. See Id.; In re Firstmark Corp., 132 F.3d 1179, 1182 (7th Cir. 1997) (emphasis added).

Exco's argument under § 1103 fails because Milbank's alleged adverse interests relating to the structured finance transactions pre-date Milbank's representation of the Committee. Moreover, Conflicts Counsel represents the Committee with respect to all matters in which Milbank was previously involved. Accordingly, the bankruptcy court was correct in finding that Milbank complies with the requirements of § 1103(b).

While Milbank asserts that § 1103(b) is the only statutory provision that applies to the Committee's right to select counsel, Exco argues Milbank must also satisfy the requirements of § 327(a). HN18[↑] Section 327(a) concerns solely the employment of professionals *by a trustee or a debtor* and requires that the professional not hold an adverse interest to the estate and that the professional be disinterested under § 101(14). However, § 328(c) of the bankruptcy code allows a bankruptcy court to deny compensation **[*22]** to a professional employed under either § 327 *or* § 1103 if that professional is not disinterested or holds an adverse interest. See 11 U.S.C. § 328(c) (emphasis added). Consequently, at least one case has held that, notwithstanding the language of § 1103, the disinterested and adverse interest requirements of 327(a) also apply to the initial retention of counsel for a committee under § 1103. See In re Caldor, 193 B.R. 165, 170-171 (Bankr. S.D.N.Y. 1996).

In the instant case, the bankruptcy court concluded that, even if the stricter requirements of § 327(a) are applied to Milbank's representation of the Committee, Milbank satisfies these requirements because it is disinterested under § 101(14) and because it does not hold an adverse interest. This Court agrees.

HN19[↑] § 101(14) defines a disinterested person, in pertinent part, as any person that:

> (C) has not been, within three years before the date of the filing of the petition, an investment banker for a security of the debtor, or an attorney for such an investment banker in connection with the offer, sale, or issuance of a security of the debtor; and …
>
> (E) does **[*23]** not have an interest materially adverse to the interest of the estate or of any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor or an investment banker … or for any other reason.

11 U.S.C. § 101(14).

Exco alleges that Milbank is not disinterested under 11 U.S.C. § 101(14) because it was counsel to investment bankers in connection with the offer, sale or issuance of a security of Debtors in the Marlin transactions, the Osprey I transactions and certain credit linked note transactions. Exco asserts that Milbank represented certain clients as arrangers of a structured finance offering in senior secured notes issued by the Marlin Water Trust II and by the Osprey Trust. Exco argues that as part of the Marlin and Osprey transactions, Enron issued preferred stock and entered into a Remarketing Agreement with Milbank's clients that, under certain provisions, required Milbank's clients to sell the preferred stock. Exco maintains, therefore, that Milbank's clients are underwriters or investment bankers in violation of 101(14).

Milbank, on the **[*24]** other hand, asserts that it represented certain investment bankers for securities issued by only non-Debtor entities prior to the petition date and disclosed these representations in its application. While Milbank acknowledges that some of its clients were parties to Remarketing Agreements with Enron, Milbank maintains that certain specified conditions would have to be met before the investment bankers would remarket Enron stock. Milbank asserts that the investment bankers never purchased, offered, sold or issued Enron securities.

Exco alleges, however, that the transactions are the Debtors' attempt to disguise the sale of Enron shares through trust vehicles and that Milbank's representation of investment bankers in connection with the secured notes is truly representation of those investment bankers in the sale of Enron stock.

The bankruptcy court found "absolutely no evidence … to prove, much less substantiate, Exco's allegations that the form of these vehicles was an artifice for a roundabout issuance of Enron securities." This Court

concurs with the bankruptcy court's finding that Exco's allegations are based on mere conjecture and speculation insufficient to support a motion **[*25]** for disqualification. See *A.V. by Versace, Inc., 160 F. Supp. 2d at 663*; *TWI Int'l, Inc. v. Vanguard Oil And Service Co., 162 B.R. 672, 675 (S.D.N.Y. 1994)* ***HN20***[] ("merely hypothesizing that conflicts may arise is not sufficient to warrant the disqualification of an attorney") (quoting *In re Stamford Color Photo, Inc., 98 B.R. 135, 138 (D. Conn. 1989)*.

The bankruptcy court relied on the Remarketing Agreements filed under seal in concluding that Milbank is disinterested pursuant to *§ 101(14)*. Having reviewed the Remarketing Agreements, this Court agrees with the bankruptcy court's findings that the conditions required for investment bankers to become underwriters of Enron stock have not been satisfied.

Exco argues that Milbank's prior representations, relating to the structured finance transactions, create an adverse interest. ***HN21***[] An adverse interest is defined as follows:

> (1) to possess or assert any economic interest that would tend to lessen the value of the bankruptcy estate or that would create either an actual or potential dispute in which the estate is a rival claimant; or (2) to possess a predisposition under circumstances that **[*26]** render such a bias against the estate.

In re Arochem Corp., 176 F.3d at 623 quoting *In re Roberts, 46 B.R. 815 (Bankr. D. Utah 1985)*.

The bankruptcy court found that the procedures Milbank has in place are satisfactory to handle its adverse representations in prior matters. This Court agrees.

Milbank's scope of employment is limited so that Milbank will not be handling any matter regarding Mahonia or any structured finance transaction that involved Milbank's representation. See N.Y. Bar Op. 2001-3 at 2-3 ("representation may be limited to eliminate adversity and avoid a conflict of interest"). Conflicts counsel reviews, on a daily basis, the docket and all pleadings to identify any matters from which Milbank should be excluded. Milbank has also created a "firewall" to prevent the transfer of information between Milbank employees who are representing the Committee and Milbank employees who previously represented parties with an adverse interest.

Moreover, conflicts counsel investigates the structured transactions relating to Milbank and the Examiner will investigate all of the structured transactions. The bankruptcy court explained that **[*27]** either Conflicts Counsel or the Examiner would discover any action by Milbank that would constitute a breach of Milbank's fiduciary duty in its own investigation of structured transactions. Accordingly, the bankruptcy court correctly concluded that there "is effectively no adverse interest in Milbank continuing these investigations."

The bankruptcy court also found that Milbank's receipt of alleged preferential transfers does not create an adverse interest between Milbank and the unsecured creditors. As the bankruptcy court explained, the Examiner will determine whether Milbank received an avoidable preference and Milbank, having waived its right to litigate the preference issue, will be bound by the Examiner's findings. The bankruptcy court found that Milbank's agreement to waive its rights to challenge the Examiner's findings has the same effect as the accepted practice of waiving a claim in order to comply with the disinterested person standard of *§ 101(14)(A)*. On appeal, Exco has not challenged the bankruptcy court's findings regarding Milbank's alleged preferential transfers. Because Milbank has agreed to be bound by the Examiner's determination, this Court agrees with the bankruptcy **[*28]** court that Milbank does not hold an adverse interest.

Ethical Violations

HN22[] Bankruptcy courts also look to the Code of Professional Responsibility in analyzing conflicts of interest. See *In re Caldor, 193 B.R. at 178*. Exco, therefore, alleges that Milbank should be disqualified under Canon 5 and Canon 9 of the Code of Professional Responsibility. This Court concurs with the bankruptcy court that, having found both that Milbank is not involved in any matter in which it has an adverse interest and that the use of conflicts counsel and ethical walls are appropriate, there is no basis for a violation of the Code of Professional Responsibility.

Conclusion

For the foregoing reasons, this Court affirms the Bankruptcy Court's Decision and Order dated May 23, 2002. Exco's request to set aside the bankruptcy court's decision and to have Milbank disqualified as counsel for the Official Committee of Unsecured Creditors is denied.

SO ORDERED:

BARBARA S. JONES

UNITED STATES DISTRICT JUDGE

Dated: January 28, 2003

End of Document

In re Townson

United States Bankruptcy Court for the Northern District of Alabama, Southern Division

March 7, 2013, Decided

Case No. 12-03027-TOM-7

Reporter
2013 Bankr. LEXIS 853 *

In Re: STEVEN REEVES TOWNSON and DEBRA D. TOWNSON, Debtors.

Core Terms

Disqualify, petitioning creditor, adverse interest, shares, counterclaim, defendant-creditor, adversary proceedings, potential conflict, actual conflict, probate estate, connections, deposition, represents, expenses, stock

Case Summary

Procedural Posture
This case came before the court for hearing on the Motion to Disqualify Professional filed by a defendant (hereafter "the defendant") in adversary proceeding 12-00160 ("AP") filed by the chapter 7 Trustee. The defendant sought to remove a certain law firm from representing the Trustee in the AP, alleging that the firm was disqualified due to its representation of another client.

Overview

There were different requirements for professionals employed pursuant to 11 U.S.C.S. § 327(a), which concerned hiring professionals to assist the trustee in carrying out his duties, and professionals employed pursuant to § 327(e) concerning the employment of special counsel with regard to a particular matter. However, both sections required that the attorney to be employed not hold or represent an interest adverse to the estate. This issue was of particular concern in this case. The court stated that the firm maintained a good reputation and the court did not conclude that it acted with the intent to deceive or intent to use its representation of both the Trustee and another individual to an impermissible advantage. Nonetheless, it was possible that the dual representation could ultimately lead to the firm acting in favor of one client to the detriment of the other. Even if somehow the firm could avoid doing so, there was still an appearance that the connections between debtor and the other individual created a conflict or could later give rise to a conflict. Removing the firm as counsel for the Trustee at this early stage in the adversary proceeding would prevent future problems.

Outcome
The Motion to Disqualify Counsel for the Trustee was granted. The Order approving the Application to Employ the law firm was set aside.

LexisNexis® Headnotes

Evidence > Judicial Notice > General Overview

HN1[] **Evidence, Judicial Notice**

Pursuant to Fed. R. Evid. 201, a court may take judicial notice of the contents of its own files.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

Legal Ethics > Client Relations > Conflicts of Interest

HN2[] Professional Services, Retention of Professionals

A trustee may employ professionals pursuant to 11 U.S.C.S. § 327. There are different requirements for professionals employed pursuant to § 327(a), which concerns hiring professionals to assist the trustee in carrying out his duties, and professionals employed pursuant to § 327(e) concerning the employment of special counsel with regard to a particular matter. However, both of these sections require that the attorney to be employed not hold or represent an interest adverse to the estate.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

Legal Ethics > Client Relations > Conflicts of Interest

HN3[] Professional Services, Retention of Professionals

In the context of 11 U.S.C.S. § 327, to "hold an interest adverse to the estate" means: (1) to possess or assert any economic interest that would tend to lessen the value of the bankruptcy estate or that would create either an actual or potential dispute in which the estate is a rival claimant; or (2) to possess a predisposition under circumstances that render such a bias against the estate. To "represent an adverse interest" means to serve as agent or attorney for any individual or entity holding such an adverse interest.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

Legal Ethics > Client Relations > Conflicts of Interest

HN4[] Professional Services, Retention of Professionals

It is sufficient to preclude counsel's employment by the estate under 11 U.S.C.S. § 327(a) or (e) if the record supports the existence of a single potential conflict.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

Legal Ethics > Client Relations > Conflicts of Interest

HN5[] Professional Services, Retention of Professionals

In the process of identification, potential conflicts on the subject dispute are just as disqualifying as actual, current ones. Regardless of whom a trustee has identified as an opponent, if a past or present client of proposed counsel was involved in any way with the events that gave rise to the dispute, or could otherwise be the subject of a claim based on those events, the client has an interest adverse to the estate and disqualification results.

Bankruptcy Law > ... > Professional Services > Retention of Professionals > General Overview

Legal Ethics > Client Relations > Conflicts of Interest

HN6[] Professional Services, Retention of Professionals

All facts that may be relevant to a determination of whether an attorney is disinterested or holds or represents an interest adverse to the debtor's estate must be disclosed. The purpose of such disclosure is to permit the court and parties in interest to determine whether the connection disqualifies the applicant from the employment sought, or whether further inquiry should be made before deciding whether to approve the employment. This decision should not be left to counsel, whose judgment may be clouded by the benefits of the

potential employment. Disclosure is required to ensure undivided loyalty and untainted advice from professionals.

Counsel: **[*1]** For Steven Reeves Townson, aka Steven Ralph Townson, aka Steve Townson, aka Steven R. Townson, Debtor: Andre' M. Toffel, Andre' M. Toffel, P.C., Birmingham, AL.

For Debra Decurtins Townson, aka Debra D. Townson, aka Debra D. Rice, Joint Debtor: Andre' M. Toffel, Andre' M. Toffel, P.C., Birmingham, AL.

For Thomas E Reynolds, Trustee: W. Lee Gresham, III, Heninger Garrison Davis, LLC, Birmingham, AL; Honza Jan Ferdinand Prchal, Heninger Garrison Davis, Birmingham, AL.

For Trustee: W. Lee Gresham, Heninger Garrison Davis, LLC, Birmingham, AL.

Judges: TAMARA O. MITCHELL, United States Bankruptcy Judge.

Opinion by: TAMARA O. MITCHELL

Opinion

MEMORANDUM OPINION AND ORDER

This case came before the Court for hearing on January 9, 2013, on the Motion to Disqualify Professional filed by William G. Bond. Appearing before the Court were Thomas E. Reynolds, Chapter 7 Trustee; W. Lee Gresham, III and Chris Hood, counsel for the Trustee; William Dennis Schilling, counsel for William G. Bond; David B. Anderson and Holly Chestnut, counsel for Frontier Bank; and Harry I. Brown, Jr., witness for Trustee. This Court has jurisdiction pursuant to *28 U.S.C. §§ 1334(b)*, *151*, and *157(a) (1994)* and the District Court's General Order Of Reference **[*2]** Dated July 16, 1984, As Amended July 17, 1984.[1] This is a core proceeding arising under Title 11 of the United States Code as defined in *28 U.S.C. § 157(b)(2)(A)*.[2] This Court has considered the pleadings, arguments of counsel, the testimony of Brown, the exhibits, and the law, and finds and concludes as follows:[3]

FINDINGS OF FACT[4]

William G. Bond ("Bond"), a defendant in adversary proceeding 12-00160 ("AP") filed by the chapter 7 trustee ("Trustee") on October 29, 2012, filed the Motion to Disqualify that is now before the Court. Bond seeks to remove the firm of Heninger Garrison Davis, LLC ("HGD") from representing the Trustee in the AP, alleging that the firm is disqualified due to its representation of another client. The Trustee filed the AP against Frontier National Corporation, Frontier Bank, and several directors and/or officers of one or both of those institutions.[5] Basically, the complaint alleges

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[1] The General Order of Reference Dated July 16, 1984, As Amended July 17, 1984 issued by the United States District Court for the Northern District of Alabama provides:

> The general order of reference entered July 16, 1984 is hereby amended to add that there be hereby referred to the Bankruptcy Judges for this district all cases, and matters and proceedings in cases, under the Bankruptcy Act.

[2] *28 U.S.C. §157(b)(2)(A)* and *(G)* provide as follows:

> (b)(2)Core proceedings include, but are not limited to—
>
> (A) matters concerning the administration of the estate[.]

[3] This Memorandum Opinion constitutes findings of fact and conclusions of law pursuant to *Federal Rule of Civil Procedure 52*, applicable to contested matters in bankruptcy pursuant to *Federal Rule of Bankruptcy Procedure 7052* and *Federal Rule of Bankruptcy Procedure 9014*.

[4] ***HN1***[↑] Pursuant to *Rule 201 of the Federal Rules of Evidence*, **[*3]** the Court may take judicial notice of the contents of its own files. *See ITT Rayonier, Inc. v. U.S., 651 F.2d 343 (5th Cir. Unit B July 1981)*; *Florida v. Charley Toppino & Sons, Inc., 514 F.2d 700, 704 (5th Cir. 1975)*.

[5] According to the complaint filed by the Trustee, Frontier National Corporation and Frontier Bank are separate entities. The relationship of each of these entities to the other is unclear, but it is apparent from testimony and pleadings that both are allegedly **[*5]** involved in the events that gave rise to

Frontier has not complied with its obligation as to debtor Steven Reeves Townson ("Townson"), a former officer and director of Frontier. According to the complaint Townson, in an effort to boost Frontier's financial position, agreed to reduce a monetary benefit he was otherwise entitled to each year. It is alleged that Frontier agreed in May 2010 to sell 15 shares of preferred stock, with a redemption **[*4]** value of $175,000.00 per share, to Townson for $1.00 per share in recognition of Townson's sacrifice, and that once Townson reached the age of 55 he would be able to redeem one share per year for 15 years at the agreed-upon redemption value. The complaint further alleges that the Board of Directors of Frontier ("Board") adopted on August 19, 2010, a Resolution approving the offer and issuance of the shares; however, the shares were never issued despite a verbal demand made by Townson's wife in December 2011. Shortly thereafter, Townson's employment with Frontier was terminated in January 2012. The Trustee seeks to have Frontier issue and redeem the shares in question, and to have a judgment entered in his favor for the value of the shares plus interest, fees, costs, and damages. An Application to Employ HGD[6] was filed August 20, 2012, and following a hearing on September 10, 2012, an Order was entered approving its employment.

The Trustee is not the only client of HGD currently involved in an action against Frontier. According to the Motion to Disqualify, Harry I. Brown, Jr. ("Brown"), who served with Townson on the Board, is represented by HGD in state court litigation filed by Frontier in the Circuit Court of Coosa County, Alabama.[7] Attached to the Motion to Disqualify is the answer and counterclaim filed by HGD for Brown against Frontier and others who were directors of Frontier at the time of the events described in the counterclaim. *See* First Amended Answer and Counter Claims, Exhibit B to the Motion to Disqualify, Doc. No. 79. One of the allegations in Brown's counterclaim is that he gave up certain monetary benefits to **[*6]** improve Frontier's capital situation, and that in recognition of Brown's action, Frontier agreed to offer to Brown 15 shares of preferred stock in Frontier at $1.00 per share. The counterclaim asserts that this agreement was memorialized in a Resolution passed by the Board at a special meeting on December 8, 2011. According to the answer and counterclaim, those shares were never issued to Brown.

Brown testified at the hearing on the Motion to Disqualify that he was represented by HGD in the Coosa County litigaton and that he was considering hiring HGD to also represent him as personal representative of his late father's probate estate. According to Brown's testimony, his father had also been on the Board, and Frontier has filed a claim in the estate relating to a guaranty signed by his father. Brown further claimed that the guaranty had been previously released by Townson on behalf of Frontier. Brown admitted that any or all of the directors on the Board, including Townson, are potential witnesses in the probate estate.

Brown's testimony also reflects **[*7]** that he was on the Board at the time the Resolution regarding the offer of shares to Townson was passed, but that he was not on the Compensation Committee and was not involved in the negotiations regarding the offer. He does not know why he was not included as a defendant in the Trustee's AP.[8] Brown also acknowledged that Townson was on the Board when the Resolution regarding the offer to Brown of 15 shares of stock was passed, and that Townson is not a defendant in the Coosa County litigation.

It was Brown's testimony that he and Townson are not friends and have not discussed the issues relating to the Trustee's AP. Brown acknowledged he recently contacted Townson, but not any of the other directors, to inform him of the probate issue. Furthermore, Brown testified that he and Townson had at least one meeting at the offices of HGD because Townson had information "important" to Brown's case.

At the hearing on the Motion to Disqualify, attorney W. Lee Gresham, III of HGD addressed the Court's questions as to how, if HGD continued to represent both the Trustee **[*8]** and Brown, expenses would be allocated between the two cases. Gresham stated that

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the Trustee's adversary proceeding and to the state court action filed by Harry I. Brown, Jr., that will be discussed herein. As to the issues currently before this Court the distinction between the two entities is not important. For the sake of convenience the entities will be collectively referred to as "Frontier."

[6] Prior to filing his bankruptcy petition Townson had hired HGD to represent him in pursuing his alleged claims against Frontier.

[7] HGD represents Brown as well as two companies (of which Brown is the only member) as defendants/counterclaimants in the state court action.

[8] In the Coosa County litigation and in the Trustee's AP, some, but not all, of the Board members of Frontier are named as defendants.

the expenses would not be split, but later acknowledged that the expense of a deposition helpful in both cases would be shared.[9]

Although HGD has argued that it did not and does not have a conflict, in its Amended Application to Employ it made the following disclosure:

> Said attorneys were employed by the Debtor prior to the filing of the Debtor's bankruptcy case.
> In addition, said attorneys currently represent Harry I. Brown, Jr., in an action pending in the Circuit Court of Coosa County, Alabama brought by Frontier Bank against Brown (the "Coosa County Litigation"). In connection with their defense of Brown in the Coosa County Litigation, said attorneys are also prosecuting a counterclaim on behalf of Brown against Frontier Bank and some of the Directors of Frontier Bank..
>
> Harry I. Brown, Jr., was a member of the Board of Directors of Frontier National Corporation at the time the **[*9]** compensation agreement was reached with the Debtor. However, Harry I. Brown, Jr., ceased to serve as a member of said board at the time the Debtor's employment was terminated, and also was not serving as a member of the board of directors at the time the Debtor became aware Frontier National Corporation and Frontier Bank did not intend to honor their agreement with the Debtor with respect to the issuance and ultimate redemption of the Preferred Stock. Said attorneys have been approached by Harry I. Brown, Jr., to represent his father's Probate Estate in connection with a matter related to the Coosa County litigation. As of the date of this amended application, the attorneys have not been retained to represent the Probate Estate.
> Furthermore, said attorneys recently have been notified that an insurer for Frontier Bank (Travelers) is investigating a claim of loss by the insured in connection with alleged dishonesty or theft by Steven Townson, Debtor. Said attorneys received notice of this investigation and claim on January 18, 2013. The notice was accompanied by a proof of loss submitted to the insurer by Frontier Bank. Said attorneys do not represent the Debtor in this matter.

These disclosures **[*10]** were not mentioned or referenced in the original Application to Employ and apparently might have gone undisclosed or with no notice having been given had the Motion to Disqualify not been filed by Bond.

CONCLUSIONS OF LAW

HN2[↑] A trustee may employ professionals pursuant to *Bankruptcy Code section 327*. There are different requirements for professionals employed pursuant to *§ 327(a)*, which concerns hiring professionals to assist the trustee in carrying out his duties, and professionals employed pursuant to *§ 327(e)* concerning the employment of special counsel with regard to a particular matter. However, both of these sections require that the attorney to be employed not hold or represent an interest adverse to the estate.[10] This issue is of particular concern in this case.

HGD represents the Trustee in his action against Frontier and certain directors. HGD also represents Brown in the state court action filed **[*11]** by Frontier and has filed counterclaims against Frontier and many of the same directors.[11] In his Addendum to the Motion to Disqualify Bond raises the issue that one or more of these defendants may not have sufficient assets to pay both judgments if the plaintiffs were successful in each of the these actions.

In *M & M Marketing, LLC, 426 B.R. 796 (8th Cir. B.A.P. 2010)*, an involuntary chapter 7 petition was filed against the debtor. After the order for relief was entered the chapter 7 trustee identified a potentially avoidable transfer and hired counsel to pursue a particular creditor. The counsel chosen by the trustee already represented the petitioning creditors. The particular creditor who was the target of the avoidance action sought to have counsel removed from representing the trustee, claiming in part that the petitioning creditors held an interest adverse to the estate because they too had received potentially avoidable transfers prior to the bankruptcy filing and that he potentially held state law

[9] No clear explanation was provided as to how expenses could be or would be shared between the two HGD clients (Brown and the Trustee). Further, the Amended Application provides no additional information as to how this might occur.

[10] There has been some question as to whether HGD's employment is pursuant to *§ 327(a)* or *§ 327(e)*; however, on January 22, 2013, after the hearing on the Motion to Disqualify, an Amended Application to Employ was filed that indicated HGD is to be employed pursuant to *11 U.S.C. § 327(e)*.

[11] HGD may also represent Brown as personal representative of his father's probate estate.

claims against the petitioning creditors as well. The court set out the definition of an "interest **[*12]** adverse" to the estate:

> HN3[] To "hold an interest adverse to the estate" means: "(1) to possess or assert any economic interest that would tend to lessen the value of the bankruptcy estate or that would create either an actual or potential dispute in which the estate is a rival claimant; or (2) to possess a predisposition under circumstances that render such a bias against the estate." To "represent an adverse interest" means to serve as agent or attorney for any individual or entity holding such an adverse interest.

Id. at 802-03 (citations omitted). The court agreed with the defendant-creditor that the petitioning creditors did hold an interest adverse to the estate, and furthermore, determined that an actual conflict existed:

> The final reason that [counsel] cannot be employed under § 327(e)—or § 327(a)—is that [counsel's] representation of the Trustee poses an actual conflict regardless of whether the scope of [counsel's] employment is limited to pursuing [the defendant-creditor]. As noted above, an individual's interest is considered adverse to an estate if that interest would tend to lessen the value of a bankruptcy estate or foster a predisposition against the estate. In this case, **[*13]** the interests of the Petitioning Creditors have the potential of doing both. The record (albeit sparse) suggests that [the defendant-creditor] might possess state-law claims against three of the Petitioning Creditors for the recovery of potentially fraudulent transfers. If [the defendant-creditor] pursues those claims, and the Trustee pursues the Petitioning Creditors for recovery of the same transfers, it is not difficult to conceive of several situations in which [counsel's] loyalties might be divided. If [the defendant-creditor] and the Petitioning Creditors seek to settle their dispute in a way that reduces the pool of assets available to the estate, then [counsel's] interests would be adverse to the estate. The zeal with which [counsel] pursues [the defendant-creditor] on behalf of the estate could be affected (negatively or positively) by litigation that might ensue between [the defendant-creditor] and the Petitioning Creditors. Or [counsel] might unearth incriminating information in his defense of the Petitioning Creditors which would interfere with his unbiased representation of the estate. Ultimately, it is unnecessary to fathom every possible conflict that might arise from **[*14]** [counsel's] concurrent representation of the Petitioning Creditors and the estate. HN4[] **It is sufficient to preclude [counsel's] employment by the estate under § 327(a) or (e) if the record supports the existence of a single potential conflict. And here it does**.

Id. at 804 (emphasis added).

While the facts of *M & M Marketing* may not be exactly on point with the issues here, that court's analysis squarely addresses many of this Court's concerns regarding the employment of HGD. The Trustee's AP and Brown's state court action admittedly share some overlapping issues. Both Townson and Brown were on the Board at the time the relevant events in each action took place. For the most part the same people were involved in those events. It is conceivable that during the course of investigating the claims in each of these actions HGD could discover information that could help one client while harming the other. Furthermore, it is conceivable that a win for both clients could mean there are not enough assets to go around. Counsel for the Trustee will be obliged to get the maximum recovery available for the estate but it will be impossible to do so if counsel has the same obligation to another client and **[*15]** the common defendants cannot completely satisfy both awards. Further, as noted at the hearing on the Motion to Disqualify, if all parties to the AP and the Coosa County litigation were ordered to participate in "global mediation," and if there were limited funds available, how would HGD get the maximum for two clients competing for money from the same "pot?" Although this is not certain to happen, the record supports the existence of more than one potential conflict which is enough to prevent HGD from representing the Trustee in the AP.

For whatever reasons, Brown is not a defendant in the Trustee's AP, and Townson is not a defendant in Brown's state court counterclaim. If either was a defendant in the other action there would be an actual conflict that would keep HGD from representing the estate. However, whether or not an actual conflict exists, the appearance that HGD represents an interest possibly adverse to the estate, and thus has a potential conflict, is a problem. In *Buckley v. Transamerica Investment Corp. (In re Southern Kitchens, Inc.)*, the court opined:

> HN5[] In the process of identification, however, potential conflicts on the subject dispute are just as

> disqualifying as actual, **[*16]** current ones. . . . Regardless of whom a trustee has identified as an opponent, if a past or present client of proposed counsel was involved in any way with the events that gave rise to the dispute, or could otherwise be the subject of a claim based on those events, the client has an interest adverse to the estate and disqualification results.

Buckley v. Transamerica Investment Corp. (In re Southern Kitchens, Inc.), 216 B.R. 819, 827 (Bankr. D. Minn. 1998).

Here, Townson and Brown were unquestionably involved in the events giving rise to each action. Brown served on the Board at the time it passed the Resolution to offer Townson 15 shares of stock. Likewise, Townson was on the Board when a similar Resolution was passed with regard to Brown. Brown in fact testified that he and Townson attended a meeting at HGD's offices because Townson had "important" information regarding Brown's case. Thus, Townson and Brown are each potential witnesses in the other's action and HGD could be in a position of examining its own client as a witness, whether it be on direct examination or as an adverse witness called by the defense. Furthermore, Brown testified that any of the directors on the Board, including **[*17]** Townson, could be a witness with regard to the claim filed by Frontier in Brown's father's probate estate. At the very least these connections create an appearance that HGD represents an interest adverse to the estate.

Another area of concern involves common expenses, such as the cost of discovery, between HGD's two clients. There are two choices - either the clients will "share" the expenses or HGD will keep the expenses separate. Either way is problematic. Sharing the cost of a deposition, for example, will in effect result in the estate (and the unsecured creditors) shouldering an expense that is not entirely beneficial to the estate. Brown's state court action against Frontier and the directors includes claims that are irrelevant to the Trustee's adversary proceeding. While some of the testimony elicited in the deposition could be important to the estate, there will be time spent questioning the deponent about the issues not relevant to the Trustee's AP. If the cost of the deposition is split down the middle the estate will in effect pay for discovery that only benefits Brown. The only way to get around this problem is for HGD to depose the same person twice, asking only the questions **[*18]** relevant to the client paying for the particular deposition. Obviously this would be impractical and a waste of resources. If separate attorneys represented Brown and the Trustee the problem would be avoided altogether.

Even if HGD continued to represent the estate this will not necessarily be the end of the subject. If new or additional information surfaces regarding an actual or a potential conflict, HGD could still be removed from representing the Trustee. It would not matter if HGD were in the middle or at the end of its representation. Depending on the facts it is possible HGD's fees could be reduced or denied altogether regardless of how much time it had invested in the case. The adversary proceeding is right now in the beginning stages. The complaint has only recently been filed and a motion to dismiss is still pending. No significant harm will have been done by ending HGD's representation now. The Court recognizes that HGD is already familiar with the facts and circumstances that gave rise to the adversary proceeding but that familiarity may be as much of a disadvantage as an advantage. Birmingham is a very large legal community and there are other well-qualified attorneys who **[*19]** could represent the Trustee, have no ties or connections to any parties or witnesses, and could quickly "get up to speed" in the AP. The benefits of retaining HGD as counsel are outweighed by the possible fight over a limited pot, the appearance of conflicts, the expense-splitting dilemma, and the potential for an actual conflict.

HGD claims it did not disclose that it represented Brown because it did not see a need to do so. This assertion in and of itself is troubling. As one court has said:

> ***HN6***[⬆] All facts that may be relevant to a determination of whether an attorney is disinterested or holds or represents an interest adverse to the debtor's estate must be disclosed. See, e.g., *Diamond Lumber v. Unsecured Creditors' Committee, 88 B.R. 773, 777 (N.D. Tex. 1988)*; *In re Roberts, 75 B.R. 402, 411 (D. Utah 1987)*. The purpose of such disclosure is to permit the Court and parties in interest to determine whether the connection disqualifies the applicant from the employment sought, or whether further inquiry should be made before deciding whether to approve the employment. *This decision should not be left to counsel, whose judgment may be clouded by the benefits of the potential employment*.

In re Lee, 94 B.R. 172, 176 (Bankr. C.D. Cal. 1988) **[*20]** (emphasis added); *see also In re Biddle, No. 12-05171, 2012 Bankr. LEXIS 5766, 2012 WL 6093926, at*

*4 (Bankr. D.S.C. Dec. 6, 2012) (disclosure is required "to ensure undivided loyalty and untainted advice from professionals") (citation omitted). HGD should not have unilaterally made the decision that its representation of Brown has no bearing on its representation of the Trustee. There is no question that Brown and Townson have connections. If HGD believed it would have no conflicts representing both clients, it is difficult to see how HGD would not disclose these connections so that the Court and other interested parties could examine the relationships and conclude for themselves that the representation of both is no cause for concern. HGD has now amended its Application for Employment to disclose its representation of Brown but it did not do so until Bond brought the issue to the Court's attention and the Court indicated at the hearing its view that the information should have been disclosed.

CONCLUSION

Heninger Garrison Davis LLC maintains a good reputation in the Birmingham community and this Court does not conclude that it acted with the intent to deceive or intent to use its representation of both the **[*21]** Trustee and Brown to an impermissible advantage. Nonetheless, it is possible that the dual representation could ultimately lead to HGD acting in favor of one client to the detriment of the other. Even if somehow HGD could avoid doing so, there is still an appearance that the connections between Townson and Brown create a conflict or could later give rise to a conflict. Removing HGD as counsel for the Trustee at this early stage in the adversary proceeding will prevent future problems and the possibility that HGD could ultimately be denied fees. Therefore, it is hereby

ORDERED, ADJUDGED, and **DECREED** that the Motion to Disqualify Counsel for the Trustee is **GRANTED**.

It is further **ORDERED, ADJUDGED**, and **DECREED** that the Order approving the Application to Employ HGD is set aside.

Dated: March 7, 2013

/s/ Tamara O. Mitchell

TAMARA O. MITCHELL

United States Bankruptcy Judge

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Positive
As of: June 11, 2021 4:31 PM Z

Jo Ann Howard & Assocs., P.C. v. Cassity

United States District Court for the Eastern District of Missouri, Eastern Division

April 13, 2012, Decided; April 13, 2012, Filed

Case No. 4:09CV01252 ERW

Reporter
2012 U.S. Dist. LEXIS 52178 *; 2012 WL 1247271

JO ANN HOWARD & ASSOCIATES, P.C., et al., Plaintiffs, vs. J. DOUGLAS CASSITY, et al., Defendants.

Subsequent History: Motion denied by *Jo Ann Howard & Assocs., P.C. v. Cassity, 2012 U.S. Dist. LEXIS 66391 (E.D. Mo., May 11, 2012)*

Prior History: *Jo Ann Howard & Assocs., P.C. v. Cassity, 2012 U.S. Dist. LEXIS 17423 (E.D. Mo., Feb. 13, 2012)*

Core Terms

Entities, Receivership, attorney-client, protective order, disqualified, matters, Receiver, disqualification motion, parties, waive, communications, former client, discovery, courts, instant case, documents, powers, former representation, opposing counsel, confidential, appointed, confer, Amend

Case Summary

Overview
Pursuant to Mo. Sup. Ct. R. 4-1.9(a), a receiver's motion to disqualify legal counsel from representing a law firm and attorney in an action alleging, inter alia, legal malpractice was granted where counsel had personally represented the receivership entities in prior proceedings, the receiver was a former client by virtue of its status as special deputy receiver of the receivership entities, and the representation was substantially related to counsel's current representation of the law firm and attorney.

Outcome
Motion granted.

LexisNexis® Headnotes

Civil Procedure > Attorneys > Disqualification of Counsel

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > Erie Doctrine

HN1[] **Attorneys, Disqualification of Counsel**

Motions to disqualify opposing counsel are subject to the discretion of the district court. Because motions to disqualify counsel in federal proceedings are substantive motions affecting the rights of the parties, they are decided by applying standards developed under federal law. Under federal law, a party seeking to disqualify opposing counsel bears a heavy burden. A party's right to select its own counsel is an important public right and a vital freedom that should be preserved. In addition, motions to disqualify may be abused by opposing counsel in pursuit of a tactical advantage. As a result, courts subject motions to disqualify to particularly strict scrutiny, and the extreme measure of disqualifying a party's counsel of choice should be imposed only when absolutely necessary. Even so, any doubt is to be resolved in favor of disqualification.

Legal Ethics > Client Relations > Conflicts of Interest

HN2[] **Client Relations, Conflicts of Interest**

See Mo. Sup. Ct. R. 4-1.9(a).

Legal Ethics > Client Relations > Conflicts of

Interest

HN3[] **Client Relations, Conflicts of Interest**

Mo. Sup. Ct. R. 4-1.9(a) prevents an attorney from representing a person, when that person has adverse interests to one of the attorney's former clients.

Bankruptcy Law > ... > Examiners, Officers & Trustees > Duties & Functions > General Overview

Evidence > Privileges > Attorney-Client Privilege > Waiver

HN4[] **Examiners, Officers & Trustees, Duties & Functions**

The trustee of a corporation in bankruptcy has the power to waive the corporation's attorney-client privilege with respect to pre-bankruptcy communications.

Bankruptcy Law > ... > Examiners, Officers & Trustees > Duties & Functions > General Overview

Civil Procedure > Attorneys > Disqualification of Counsel

Evidence > Privileges > Attorney-Client Privilege > Waiver

Legal Ethics > Client Relations > Conflicts of Interest

HN5[] **Examiners, Officers & Trustees, Duties & Functions**

Lower courts state that judicial precedent reflects a continuity of the attorney-client relationship without regard to a corporation's bankruptcy status. As a result, when an attorney has represented a corporation before it entered bankruptcy, the courts disqualify that attorney from representing defendants adverse to the corporation in its bankruptcy proceedings. Courts disqualify an attorney under the applicable equivalent to Mo. Sup. Ct. R. 4-1.9(a), even though the party moving for disqualification was the bankruptcy trustee or a similarly interested party, rather than the corporation itself.

Evidence > Privileges > Attorney-Client Privilege > General Overview

Legal Ethics > Client Relations > Conflicts of Interest

HN6[] **Privileges, Attorney-Client Privilege**

Courts employ the practical consequences test when evaluating whether a particular transaction between a predecessor corporate entity and its successor operates to transfer control over the former's attorney-client privilege. For instance, a mere transfer of some assets or a single patent from one corporation to the other does not transfer the attorney-client privilege. However, if the practical consequences of the transaction result in the transfer of control of the business and the continuation of the business under new management, the authority to assert or waive the attorney-client privilege will follow as well. Thus, the practical consequences test is used where corporate control transfers as the result of some transaction, such as the purchase and sale of assets or patents.

Legal Ethics > Client Relations > Conflicts of Interest

HN7[] **Client Relations, Conflicts of Interest**

Matters are substantially related' for purposes of Mo. Sup. Ct. R. 4-1.9 if they involve the same transaction or legal dispute or if there otherwise is a substantial risk that confidential factual information as would normally have been obtained in the prior representation would materially advance the client's position in the subsequent matter. Mo. Sup. Ct. R. 4-1.9(a) cmt., para. 3.

Legal Ethics > Client Relations > Conflicts of Interest

HN8[] **Client Relations, Conflicts of Interest**

The Missouri Supreme Court listed factors the courts consider when determining whether two matters are substantially related for purposes of Mo. Sup. Ct. R. 4-1.9(a). Among these factors are: whether the matters involve the same clients or a series of matters or transactions that reveal a client's pattern of conduct; whether the lawyer interviewed witnesses key to both cases; whether the matters share a commonality of

witnesses, legal theories, and client business practices; and whether the matters share common subject matter issues, and causes of action. However, when determining whether a substantial relationship between a former and current representation exists, the underlying question is whether the lawyer was so involved in the matter that the subsequent representation can be justly regarded as a changing of sides in the matter in question. Put another way, the inquiry is whether it is reasonable to infer that confidential information would have been given to the lawyer during the prior representation and, if so, whether that information is relevant to issues raised in the current litigation.

Legal Ethics > Client Relations > Conflicts of Interest

HN9[] **Client Relations, Conflicts of Interest**

The mere existence of an attorney-client relationship raises an irrefutable presumption that confidences were disclosed.

Evidence > Privileges > Attorney-Client Privilege > Waiver

Legal Ethics > Client Relations > Conflicts of Interest

HN10[] **Attorney-Client Privilege, Waiver**

It is true that when a client challenges his attorney's competence, the client puts the substance of attorney-client communications into issue. As a result, such a challenge waives the attorney-client privilege, thereby enabling the attorney to defend himself against the client's allegations. However, such a challenge does not result in blanket waiver, but instead in a waiver limited to only those documents and communications that are at-issue. More importantly, a waiver of the privilege does not bar a plaintiff from invoking Mo. Sup. Ct. R. 4-1.9(a), because the Rule protects a client's interest in both confidences and loyalty. Accordingly, if an attorney is burdened by a conflict of interest, then Rule 4-1.9(a) requires that attorney to secure informed consent, confirmed in writing, to continue a representation.

Civil Procedure > Attorneys > Disqualification of Counsel

HN11[] **Attorneys, Disqualification of Counsel**

In ruling on a motion to disqualify an attorney, the court must resolve all doubts in favor of disqualification.

Civil Procedure > Discovery & Disclosure > Discovery > Protective Orders

HN12[] **Discovery, Protective Orders**

See *Fed. R. Civ. P. 26(c)(1)*.

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Judges: E. RICHARD WEBBER, SENIOR UNITED STATES DISTRICT JUDGE.

Opinion by: E. RICHARD WEBBER

Opinion

MEMORANDUM AND ORDER

This matter comes before the Court on: (1) Plaintiff Jo Ann Howard & Associates, P.C.'s Motion to Disqualify Jack Spooner as Counsel for the Wittner Defendants, [ECF No. 842]; and (2) Defendant Brown Smith **[*7]** Wallace's Motion for a Protective Order, or, in the Alternative, to Amend the July 22, 2011 Consent Protective Order, [ECF No. 821]. The Court held a hearing on these Motions on March 28, 2012.

I. PLAINTIFF JO ANN HOWARD & ASSOCIATES, P.C.'S MOTION TO DISQUALIFY JACK SPOONER AS COUNSEL FOR THE WITTNER DEFENDANTS. [ECF No. 842].

Plaintiff Jo Ann Howard & Associates, P.C. (Plaintiff) has been appointed to serve as the Special Deputy Receiver (SDR) of three companies: National Prearranged Services, Inc. (NPS); Lincoln Memorial Life Insurance Co. (Lincoln); and Memorial Service Life Insurance Co. (Memorial) (collectively, the Receivership Entities). In the instant case, Plaintiff, in its capacity as the SDR of the Receivership Entities, has asserted claims such as breach of fiduciary duty, legal malpractice, gross negligence, and others, against Defendant Wittner, Spewak & Maylack, P.C. and/or Howard A. Wittner (collectively, the Wittner Defendants). Pls.' Second. Amended Compl. ¶¶ 229-45, 302-06, 353-64, 365-71, 372-78, 420-29, 430-36, [ECF No. 594]. On February 21, 2012, Jack Spooner entered his appearance as counsel for the Wittner Defendants. [ECF No. 828]. Approximately one week later, **[*8]** all other counsel of record for the Wittner Defendants moved to withdraw from the representation. [ECF No. 836; ECF No. 837]. The Court granted these Motions, with the result that Spooner alone was counsel of record for the Wittner Defendants. [ECF No. 838]. Plaintiff now moves to disqualify Spooner as counsel for the Wittner Defendants. Pls.' Mot. to Disqualify Spooner, [ECF No. 842].

HN1[↑] Motions to disqualify opposing counsel are subject to the discretion of the district court. *Petrovic v. Amoco Oil Co., 200 F.3d 1140, 1154 (8th Cir. 2000)*. "[B]ecause motions to disqualify counsel in federal proceedings are substantive motions affecting the rights of the parties, they are decided by applying standards developed under federal law." *Dalton v. Painters Dist. Council No. 2, no. 4:10CV01090 AGF, 2011 U.S. Dist. LEXIS 38403, 2011 WL 1344120, at *4 (E.D. Mo. April 8, 2011)*. Under federal law, a party seeking to disqualify opposing counsel bears a heavy burden. *Macheca Transp. Co. v. Phila. Indem. Co. 463 F.3d 827, 833 (8th Cir. 2006)*. "A party's right to select its own counsel is an important public right and a vital freedom that should be preserved[.]" *Id.* In addition, motions to disqualify may be abused by opposing counsel **[*9]** in pursuit of a tactical advantage. *Id.* As a result, courts subject motions to disqualify to "particularly strict scrutiny," and "the extreme measure of disqualifying a party's counsel of choice should be imposed only when absolutely necessary." *Id.* Even so, "any doubt is to be resolved in favor of disqualification." *Coffelt v. Shell, 577 F.2d 30, 32 (8th Cir. 1978)*; *see also Dalton, no. 4:10CV01090 AGF, 2011 U.S. Dist. LEXIS 38403, 2011 WL 1344120, at *4*.

Plaintiff argues that because Spooner has previously represented the Receivership Entities in various matters, he is barred under the Court's Rules of Professional Conduct from representing the Wittner Defendants in the instant case. Plaintiffs rely upon Rule 4-1.9(a) of the Missouri Rules of Professional Conduct:

> HN2[] A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing.

Mo Sup. Ct. R. 4-1.9(a); *see also* E.D. Mo. L.R. 12.02 (adopting the Missouri Rules of Professional Conduct). This Rule "protects the client's **[*10]** interest in both loyalty and confidentiality." Griffen by Freeland v. E. Prairie, Mo. Reorganized Sch. Dist. No. 2, 945 F. Supp. 1251, 1253 (E.D. Mo. 1996) (citing In re American Airlines, Inc., 972 F.2d 605, 618 (5th Cir. 1992)). In addition, it promotes fundamental fairness by barring an attorney from using an informational advantage gained in the course of a former representation, and it serves the important policies of encouraging client disclosure of all pertinent information and fostering confidence in the integrity of the judicial system. Dalton, no. 4:10CV01090 AGF, 2011 U.S. Dist. LEXIS 38403, 2011 WL 1344120, at *5.

There is no dispute here that Spooner has previously represented at least some of the Receivership Entities, that the interests of the Receivership Entities and the Wittner Defendants are materially adverse, and that the Receivership Entities have not consented in writing to Spooner's representation. Thus, the parties dispute three points: (1) whether Spooner personally represented the Receivership Entities; (2) whether Plaintiff is a "former client" within the meaning of Rule 4-1.9(a); and (3) whether Spooner's former representation of the Receivership Entities and current representation **[*11]** of the Wittner Defendants are substantially related.

1. Whether Spooner personally represented the Receivership Entities

Plaintiffs argue that Spooner has personally represented the Receivership Entities in numerous cases over many years. Plaintiffs' primarily rely upon Spooner's appearance as counsel of record for NPS in Hannover Life Reassurance Co. of Am. v. Sutton, et. al, no. 4:07-cv-01434 JCH, 2008 U.S. Dist. LEXIS 45421 (E.D. Mo.) and a related arbitration action. A review of those matters shows that Spooner appeared on the docket and in filings as counsel for NPS. Pl.'s Mot. to Disqualify Spooner Ex. 1, [ECF No. 842-1]. Plaintiff has also submitted billing records showing that Spooner's representation of NPS was substantial and involved a wide variety of legal work. Pl.'s Reply Ex. 1-A, [ECF No. 850-2]. Various records also show that for those matters, Spooner both attended depositions and personally deposed witnesses. Pl.'s Reply Ex. 1-B, [ECF No. 850-3]. Plaintiffs have also presented evidence that Spooner served as counsel for Lincoln and NPS in several other matters. Pls.' Mot. to Disqualify Spooner Ex. 1. Based on this evidence, the Court finds that Spooner has personally represented the Receivership **[*12]** Entities. [1]

2. Whether Plaintiff is a "former client" within the meaning of Rule 4-1.9(a)

HN3[] Rule 4-1.9(a) prevents an attorney from representing a person, when that person has adverse interests to one of the attorney's former clients. Here, Spooner has not previously represented Plaintiff, but instead has previously represented NPS and Memorial. As a result, the Court must decide whether Plaintiff, based on its status as SDR, may seek to disqualify Spooner's representation of the Wittner Defendants as a violation of Rule 4-1.9(a). Neither party presented the Court with any authority that squarely resolves this issue, and the Court found no **[*13]** such authority after conducting independent research. Nevertheless, a review of the relevant case law makes clear that Plaintiff may seek to disqualify Spooner.

The Court's analysis of Plaintiff's Motion to Disqualify begins with the United States Supreme Court decision of Commodity Futures Trading Comm'n v. Weintraub, 471 U.S. 343, 105 S. Ct. 1986, 85 L. Ed. 2d 372 (1985).

[1] Because the Court finds that Spooner personally represented the Receivership Entities, the Court rejects the Wittner Defendants' contention that the Plaintiff's Motion be analyzed under Mo. Sup. Ct. R. 4-1.9(b). Rule 4-1.9(b) bars a lawyer from representing a person as a result of that lawyer's prior affiliation with a firm who represented clients with adverse interests to that person. This Rule is inapplicable here, because it was not merely Spooner's former law firm, but instead Spooner himself who previously represented the Receivership Entities.

In that case, the issue presented was "whether the trustee of a corporation in bankruptcy has the power to waive the debtor corporation's attorney-client privilege with respect to communications that took place before the filing of the petition in bankruptcy." *Id. at 345*. The Court noted that "for solvent corporations, the power to waive the corporate attorney-client privilege rests with the corporation's management," so that "when control of a corporation passes to new management, the authority to assert and waive the corporation's attorney-client privilege passes as well." *Id. at 348*. Because a corporation's management controls its privilege outside of the bankruptcy context, the Court concluded that the actor who held duties most analogous to management should also control its privilege during bankruptcy. *Id. at 351-52*. The Court then noted that **[*14]** when a corporation enters bankruptcy, its trustee acquires wide-ranging powers, including the power to manage its property, to manage its financial affairs, to pursue its legal claims, and to operate its business. *Id. at 352* (citing and discussing provisions of the Bankruptcy Code). Based in large part upon these powers, the Court held "that ***HN4***[⬆] the trustee of a corporation in bankruptcy has the power to waive the corporation's attorney-client privilege with respect to prebankruptcy communications." *Id. at 358*.

HN5[⬆] Lower courts have stated that *Weintraub* "reflects a continuity of the attorney-client relationship" without regard to a corporation's bankruptcy status. *In re Peck Foods, 196 B.R. 434, 438 (Bankr. E.D. Wis. 1996)*; *see also In re Successor I Corp., 321 B.R. 640, 652 (Bankr. S.D.N.Y. 2005)* ("that the attorney-client privilege of a corporation continued after the process of liquidation has begun is a necessary predicate for" *Weintraub*). As a result, when an attorney has represented a corporation before it entered bankruptcy, the courts have disqualified that attorney from representing defendants adverse to the corporation in its bankruptcy proceedings. *In re Successor I Corp., 321 B.R. 640, 654, 663*; **[*15]** *In re Jaeger, 213 B.R. 578, 594 (Bankr. C.D. Cal. 1997)*; *In re Marks v. Goergens, Inc., 199 B.R. 922, 929 (Bankr. E.D. Mich. 1996)*; *see also In re Peck Foods, 196 B.R. 434, 440* (court denied approval of attorney's representation of defendant, when that attorney previously represented corporation); *In re Rodriguez, no. 10-05835 BKT, 2012 Bankr. LEXIS 195, 2012 WL 112971, at *4 (Bankr. D. P.R. Jan. 12, 2012)* ("... if the trustee is pursuing claims of the debtor under to *Section 541* [of the Bankruptcy Code], the trustee stands in the shoes of the debtor."); *In re Estates of Dublin Sec., Inc., 214 B.R. 310, 314 (Bankr. S.D. Ohio 1997)* (attorney who had previously represented corporation disqualified under a distinct Rule from representing defendant with adverse interests). Courts have disqualified an attorney under the applicable equivalent to *Rule 4-1.9(a)*, even though the party moving for disqualification was the bankruptcy trustee or a similarly interested party, rather than the corporation itself. *In re Successor I Corp., 321 B.R. 640, 654, 663*; *In re Jaeger, 213 B.R. 578, 594*; *In re Marks & Goergens, Inc., 199 B.R. 922, 929*.

In the instant case, Plaintiff's duties and obligations as the Receivership Entities' **[*16]** SDR place it in a position similar to that of the bankruptcy trustees described above. For instance, Plaintiff's authority arises from the Texas Insurer Receivership Act, and that Act gives SDRs broad powers to manage the property, business operations, and legal claims of entities placed under receivership. *Tex. Ins. Code § 443.001 et seq.*; *id. § 443.154*. Furthermore, it is clear that Plaintiff may exercise those broad powers in pursuit of its duties here. Pls' Second Amended Compl. Ex. 3, [ECF No. 594-3]; *Speaks Family Legacy Chapels, Inc. v. Nat'l Heritage Enters., Inc., no. 2:08-cv-04148-NKL, 2009 U.S. Dist. LEXIS 107483, 2009 WL 3855685, at *1 (W.D. Mo. Nov. 18, 2009)* (describing authority and powers granted to SDR of NPS, Lincoln, and Memorial). Plaintiff is therefore "functioning in the same manner as a bankruptcy trustee, marshaling and preserving assets as circumstances allow." *SEC v. Bravata, no. 09-12950, 2011 U.S. Dist. LEXIS 13856, 2011 WL 606745, at *2 (E.D. Mich. Feb. 11, 2011)*; *id.* ("The appointing order provides the Receiver with broad authority to act on behalf of the receivership entities.").

The Court is also guided by decisions addressing whether a receiver may assert the attorney-client privilege on behalf of an entity **[*17]** in receivership. Several courts have held such authority is within the powers granted to a receiver. *United States v. Plache, 913 F.2d 1375, 1381 (9th Cir. 1990)* ("Prior to the instant action, the corporation was placed in receivership. Because the privilege was held by the corporation, any right to assert the attorney-client privilege on behalf of the corporation passed when the receiver of ELMAS/ROBL and its affiliates and subsidiaries, was appointed by the court."); *Bravata, no. 09-12950, 2011 U.S. Dist. LEXIS 13856, 2011 WL 606745, at *2* ("The appointing order provides the Receiver with broad authority to act on behalf of the receivership entities. That authority includes the right to waive the attorney-client privilege, if the Receiver in his judgment deems that course prudent."); *United States v. Shapiro, 2007 U.S. Dist. LEXIS 74725, 2007 WL 2914218, at *5*

(S.D.N.Y. Oct. 2, 2007) (holding that receiver had authority to waive corporate entity's attorney-client privilege, and collecting cases in support); *see also* SEC v. Ryan, 747 F. Supp. 2d 355, 362 (N.D.N.Y. 2010) ("Now that the Court has determined that Prime Rate is an independent entity, our next inquiry is to ascertain if the Receiver steps into the proverbial shoes of Prime Rate, **[*18]** becoming a client of Bosman & Associates, who may have the right to seek its own files. Again, both the facts and law compel only one observation: Levine, as Receiver and successor to the management of Prime Rate, is indeed a client."). Though these cases address only whether a receiver exercises control over a corporation's privilege, the same legal principles determine whether opposing counsel should be disqualified under Rule 4-1.9(a). Parus Holdings, Inc. v. Banner & Witcoff, Ltd., 585 F. Supp. 2d 995, 1001-02 (N.D. Ill. 2008).

The Wittner Defendants raise several arguments against Plaintiff's authority to seek Spooner's disqualification, but each is without merit. First, the Wittner Defendants' argue that the Court must distinguish between the Receivership Entities's attorney-client privilege and their attorney-client relationships. There is no basis in the law for making such a distinction. *Id.*

Next, the Wittner Defendants argue the Court should determine whether the Receivership Entities' attorney-client relationships transfer to Plaintiff by examining the "practical consequences" of the receivership. However, ***HN6***[⬆] courts employ the practical consequences test when evaluating whether **[*19]** a particular transaction between a predecessor corporate entity and its successor operates to transfer control over the former's attorney-client privilege. *See, e.g.*, id. at 1002-03; Soverain Software LLC v. Gap, Inc., 340 F. Supp. 2d 760, 763 (E.D. Tex. 2004). For instance, "a mere transfer of some assets or a single patent from one corporation to the other does not transfer the attorney-client privilege." Soverain Software LLC, 340 F. Supp. 2d 760, 763. However, "[i]f the practical consequences of the transaction result in the transfer of control of the business and the continuation of the business under new management, the authority to assert or waive the attorney-client privilege will follow as well." *Id.* Thus, the practical consequences test is used where corporate control transfers as the result of some transaction, such as the purchase and sale of assets or patents. *Id.*; In re Successor I Corp., 321 B.R. 640, 653-54. It is therefore inapplicable here, because Plaintiff acquired control over the Receivership Entities by virtue of its appointment as their SDR. For the same reasons, the Wittner Defendants' reliance on *FDIC v. Amundson* is misplaced. *See* 682 F. Supp. 981, 983-84 (D. Minn. 1988) **[*20]** (the court denied the FDIC's motion to disqualify opposing counsel, where the FDIC was acting "in its corporate capacity as purchaser of certain assets" of an insolvent bank rather than as receiver of that bank).

After reviewing the legal principles discussed above, the Court finds that Plaintiff qualifies as a "former client" by virtue of its status as the SDR of the Receivership Entities. As a result, Plaintiff may seek to disqualify Spooner on the grounds that his representation of the Wittner Defendants violates Rule 4-1.9(a).

3.Whether Spooner's Former Representation of the Receivership Entities and Current Representation of the Wittner Defendants are Substantially Related

Finally, Plaintiff argues that Spooner's former representation of the Receivership Entities is substantially related to his representation of the Wittner Defendants in the instant case. ***HN7***[⬆] "Matters are 'substantially related' for purposes of this Rule 4-1.9 if they involve the same transaction or legal dispute or if there otherwise is a substantial risk that confidential factual information as would normally have been obtained in the prior representation would materially advance the client's position in the subsequent **[*21]** matter." Rule 4-1.9(a) cmt. ¶ 3; *see also* In re IH 1, Inc., 441 B.R. 742, 746 (Bankr. D. Del. 2011).

HN8[⬆] In *In re Carey*, the Missouri Supreme Court listed factors the courts consider when determining whether two matters are substantially related. 89 S.W.3d 477, 494 (Mo. 2002). Among these factors are: whether the matters involve the same clients or a series of matters or transactions that reveal a client's pattern of conduct; whether the lawyer interviewed witnesses key to both cases; whether the matters share a commonality of witnesses, legal theories, and client business practices; and whether the matters share common subject matter issues, and causes of action. *Id.* However, when determining whether a substantial relationship between a former and current representation exists, "[t]he underlying question is whether the lawyer was so involved in the matter that the subsequent representation can be justly regarded as a changing of sides in the matter in question." Dalton, no. 4:10CV01090 AGF, 2011 WL 1344120, at *6 (quoting Rule 4-1.9(a) cmt. ¶ 1.). Put another way, "[t]he

inquiry is whether it is reasonable to infer that confidential information would have been given to the lawyer during **[*22]** the prior representation and, if so, whether that information is relevant to issues raised in the current litigation." *Dalton, no. 4:10CV01090 AGF, 2011 WL 1344120, at *6* (citation omitted).

Plaintiff argues Spooner's former representations are substantially related to the instant case by focusing on the *Hannover Reassurance Life Co. of Am. v. Lincoln Memorial Life Ins. Co.* arbitration and litigation. In these matters, Hannover named Lincoln as a defendant and alleged it had breached its contractual duties and committed fraud. Some of the factual allegations against Lincoln were that NPS financial advisor David Wulf was not independent, that NPS officers and directors improperly surrendered whole value life insurance policies and replaced them with term life insurance policies, and that NPS failed to make timely payments to Lincoln. Similarly, here, Lincoln and NPS are Receivership Entities, and Plaintiff alleges these Receivership Entities suffered damages resulting from Defendants' breach of their duties and fraud. These causes of action are built, in part, upon the factual allegations discussed above.

During his representation of Lincoln, Spooner also had extensive interactions with **[*23]** witnesses and parties that are relevant here. For instance, Plaintiff produced evidence showing that Spooner regularly communicated with Lincoln's corporate officers and attorneys, including Howard A. Wittner and Katherine Scannell. Both of these individuals are defendants here. Records show that Spooner also communicated with Howard A. Wittner, Randall Sutton, David Wulf, and J. Douglas Cassity. All of these individuals are Defendants here. Finally, Spooner also attended the depositions of Tony Lumpkin, Randall Sutton, and J. Douglas Cassity. Each of these individuals is a Defendant here. [2]

Even if the Court were **[*24]** to put aside the evidence of the extent of Spooner's representation in the *Hannover* matters, ***HN9***[↑] the mere existence of an "attorney-client relationship raises an irrefutable presumption that confidences were disclosed." *Fred Weber, Inc. v. Shell Oil Co., 566 F.2d 602, 608 (8th Cir. 1977)*. The Court has already concluded that Spooner personally represented Lincoln and NPS, in part based upon Spooner's billing records indicating he discussed confidential matters regarding those entities. Accordingly, there is an irrebuttable presumption that NPS and Lincoln disclosed confidential communications to Spooner. *Dalton, no. 4:10CV01090 AGF, 2011 U.S. Dist. LEXIS 38403, 2011 WL 1344120, at *6*; *Griffen by Freeland, 945 F. Supp. 1251, 1254*. Accordingly, Plaintiff need not prove the Receivership Entities in fact disclosed confidences to Spooner to prevail on their disqualification motion.

The Wittner Defendants argue that Plaintiff has waived the attorney-client privilege by alleging the attorneys for the Receivership Entities committed malpractice and breached their fiduciary duties. This argument is misplaced. ***HN10***[↑] It is true that when a client challenges his attorney's competence, the client puts the substance of attorney-client **[*25]** communications into issue. *Tasby v. United States, 504 F.2d 332, 336 (8th Cir. 1974)*. As a result, such a challenge waives the attorney-client privilege, thereby enabling the attorney to defend himself against the client's allegations. *United States v. Glass, 761 F.2d 479, 480 (8th Cir. 1985)*. However, such a challenge does not result in blanket waiver, but instead in a waiver limited to only those documents and communications that are at-issue. *Jones v. United States, no. 4:11CV00702 ERW, 2012 U.S. Dist. LEXIS 18028, 2012 WL 484663, at *1 (E.D. Mo. Feb. 14, 2012)*. More importantly, a waiver of the privilege does not bar Plaintiff from invoking *Rule 4-1.9(a)*, because the Rule protects a client's interest in both confidences and loyalty. *In re Jaeger, 213 B.R. 578, 589 (Bankr. C.D. Cal. 1997)* ("A waiver of the attorney-client privilege does not affect the duty of loyalty for conflict of interest purposes."); *Griffen by Freeland, 945 F. Supp. 1251, 1253*. Accordingly, if an attorney is burdened by a conflict of interest, then *Rule 4-1.9(a)* requires that attorney to secure informed consent, confirmed in writing, to continue a representation. Regardless of any issues of privilege and waiver, it is undisputed here that **[*26]** Spooner has not obtained Plaintiff's consent to represent the Wittner Defendants.

HN11[↑] In ruling on this matter, the Court must resolve all doubts in favor of disqualification. *Coffelt. 577 F.2d 30, 32*; *see also* *Dalton, no. 4:10CV01090 AGF, 2011*

[2] Plaintiff also argues that Spooner may be called as a witness in the instant case, given his extensive history and knowledge of the Receivership Entities and the allegations pending against his former law firm. Plaintiff does not claim Spooner's status as a possible witness warrants his disqualification under *Rule 4-3.7*, but rather argues that this status is further evidence of the necessity of his disqualification under *Rule 4-1.9(a)*. The Court bears this possibility in mind, but does not base its decision upon this consideration. *Macheca Transp. Co., 463 F.3d 827, 833-34*.

U.S. Dist. LEXIS 38403, 2011 WL 1344120, at *4. Upon review of the facts and the law, the Court finds that Spooner has personally represented the Receivership Entities. The Court also finds that this representation was substantially related to his current representation of the Wittner Defendants in the instant case, and that Plaintiff qualifies as a "former client" of Spooner based on its status as SDR of the Receivership Entities. As a result, Plaintiff has shown that Spooner's representation of the Wittner Defendants violates Rule 4-1.9(a). The Court will therefore grant Plaintiff's Motion to Disqualify Spooner.

II. DEFENDANT BROWN SMITH WALLACE'S MOTION FOR A PROTECTIVE ORDER, OR, IN THE ALTERNATIVE, TO AMEND THE JULY 22, 2011 CONSENT PROTECTIVE ORDER. [ECF No. 821].

In their Second Amended Complaint, Plaintiffs allege Defendant Brown Smith Wallance (BSW), an accounting firm, is liable for one count of professional negligence in auditing. BSW states that although this allegation **[*27]** is only a small aspect of Plaintiffs' wide-ranging Complaint, Plaintiffs have produced or identified a tremendous number of documents. BSW argues it is unclear which of these documents, if any, pertain to the single negligence allegation it faces, and that sifting through this mass of documents presents an undue burden. BSW therefore asks the Court to enter a Protective Order requiring Plaintiffs to identify with specificity the documents supporting their negligence allegation. In the alternative, BSW asks the Court to amend the Consent Protective Order dated July 22, 2011. [ECF No. 742]. In this Order, the Court permitted certain parties to exchange fact-based interrogatories without regard to the stay of under-oath discovery previously issued by the Court in this case. BSW asks the Court to Amend this Order to include BSW, so that it too may engage in discovery by fact-based interrogatories.

Fed. R. Civ. P. 26(c)(1) states, in part, as follows:

> HN12[] A party or any person from whom discovery is sought may move for a protective order in the court where the action is pending—or as an alternative on matters relating to a deposition, in the court for the district where the deposition will be **[*28]** taken. The motion must include a certification that the movant has in good faith conferred or attempted to confer with other affected parties in an effort to resolve the dispute without court action. The court may, for good cause, issue an order to protect a party or person from annoyance, embarrassment, oppression, or undue burden or expense,....

BSW's request does not fit well within the text of this Rule. First, BSW seeks an Order requiring Plaintiffs to identify documents supporting their allegation. Thus, BSW is not protected from the burden of *producing* discovery to Plaintiffs; instead, it seeks protection from the burden of *reviewing* the discovery Plaintiffs produced for their *Rule 26* initial disclosures. *Fed. R. Civ. P. 26(a)(1)*. BSW is therefore not a "party or person from whom discovery is sought[.]" John Wiley & Sons, Inc. v. Does Nos. 1-27, no. 11 Civ. 7627(WHP), 2012 U.S. Dist. LEXIS 13667, 2012 WL 364048, at *2 (S.D.N.Y. Feb. 3, 2012). Next, there was some discussion that the parties had talked prior to filing this Motion, but the Motion contained no certification confirming the parties had conferred in good faith. BSW's Motion therefore violated both *Rule 26*, as well as Local Rule 3.04. *Fed. R. Civ. P. 26(c)(1)*; **[*29]** E.D Mo. L.R. 3.04(A). In addition, it was immediately apparent at the hearing held on this Motion that the failure of the parties to communicate materially impeded their resolution of this matter. Finally, BSW must show "good cause" to be entitled to a protective order. Donovan v. Shaw, 668 F.2d 985, 991 (8th Cir. 1982). Given the present stage of the discovery process and BSW's failure to take simple measures to resolve this dispute without Court intervention, BSW has failed to make this showing. BSW's request for a Protective Order will therefore be denied.

As for BSW's alternative request, Plaintiffs state that they take no position with regard to BSW's request that the Consent Protective Order be amended so that BSW may also engage in fact-based interrogatories. Because Plaintiffs do not object to BSW's request, the Court believes that this issue can best be resolved through discussions between the parties. For this reason, the Court will deny BSW's request at the present time. However, the Court invites BSW and Plaintiffs to confer and develop a mutually agreeable Consent Protective Order to submit for the Court's consideration.

Accordingly,

IT IS HEREBY ORDERED that Plaintiff Jo **[*30]** Ann Howard & Associates, P.C.'s Motion to Disqualify Jack Spooner as Counsel for the Wittner Defendants, [ECF No. 842], is **GRANTED.** Spooner is disqualified from further representation of the Wittner Defendants in this

case. The Clerk's Office shall terminate Spooner's entry immediately. Witter Defendants shall employ new counsel within twenty (20) days of this Order.

IT IS FURTHER ORDERED that Defendant Brown Smith Wallace's Motion for a Protective Order, or, in the Alternative, to Amend the July 22, 2011 Consent Protective Order, [ECF No. 821] is **DENIED.** However, the Court invites the parties to confer and develop a mutually agreeable Consent Protective Order to submit for the Court's consideration.

So Ordered this 13th day of April, 2012.

/s/ E. Richard Webber

E. RICHARD WEBBER

SENIOR UNITED STATES DISTRICT JUDGE

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Pressman-Gutman Co. v. First Union Nat'l Bank

United States District Court for the Eastern District of Pennsylvania

November 30, 2004 ; November 30, 2004, Filed, November 30, 2004, Entered

CIVIL ACTION No. 02-8442

Reporter
2004 U.S. Dist. LEXIS 23991 *; 34 Employee Benefits Cas. (BNA) 1915

PRESSMAN-GUTMAN CO., INC., EMPLOYER/SPONSOR OF THE PRESSMAN-GUTMAN CO., INC. PROFIT SHARING PLAN, Plaintiff, v. FIRST UNION NATIONAL BANK and FOREFRONT CAPITAL ADVISORS, LLC, Defendants, FIRST UNION NATIONAL BANK, Third-Party Plaintiff, v. ALVIN GUTMAN and JAMES GUTMAN, Third-Party Defendants.

Subsequent History: Motion denied by *Pressman-Gutman Co. v. First Union Nat'l Bank, 2004 U.S. Dist. LEXIS 25608 (E.D. Pa., Dec. 22, 2004)*

Reconsideration denied by *Pressman-Gutman Co. v. First Union Nat'l Bank, 2004 U.S. Dist. LEXIS 25607 (E.D. Pa., Dec. 22, 2004)*

Appeal dismissed by, Writ of mandamus denied *Pressman-Gutman Co. v. First Union Nat'l Bank (In re Pressman-Gutman Co.), 459 F.3d 383, 2006 U.S. App. LEXIS 21219 (3d Cir. Pa., Aug. 18, 2006)*

Prior History: *Pressman-Gutman Co. v. First Union Nat'l Bank, 2004 U.S. Dist. LEXIS 17720 (E.D. Pa., Aug. 30, 2004)*

Disposition: Defendants' motions for reconsideration or clarification of court's August 30, 2004 order granted. Court's order of August 30, 2004 vacated. Hamburg and Golden, P.C. was completely disqualified from this case.

Core Terms

disqualified, profit-sharing, third-party, appoint, joint representation, fiduciary, conflicting interest, losses, motions, disqualification motion, reconsideration motion, investment decision, adversely affect, disqualification, consented, preliminary injunction, professional conduct, deny a motion, ad litem, defendants', loyalty

Case Summary

Procedural Posture
Plaintiff employer, on behalf of its employee profit-sharing plan, brought an action against defendants, plan trustee and plan advisor. Defendants counterclaimed against officers of the plan. After the court disqualified the plan's law firm from representing the officers, defendants sought to have the firm completely disqualified from the case. The advisor also moved for the appointment of an independent party to act on behalf of the plan.

Overview
The employer claimed that defendants failed to utilize proper research and analysis in the management of the plan's assets, causing substantial losses, and that defendants misrepresented that they were skilled, professional, and conscientious in the management of the plan's assets. Defendants filed a third-party complaint against the officers, individually and as officers of the employer and the plan, arguing that the officers breached their fiduciary duties and were negligent by breaching their duties to issue instructions to defendants which would not injure, jeopardize, or impair the plan's assets. The court disqualified the firm from representing the officers due to a conflict of interest. Upon reconsideration, the court held that the firm should be disqualified altogether because the firm's duty of loyalty to the officers precluded it from recommending to the plan that it seek recovery from the officers. The court also removed the officers as administrators of the plan because of their potential liability.

Outcome
The court granted the motions, completely disqualifying counsel from the case. The court also ordered that a guardian ad litem, who would be appointed in a separate order to serve as administrator of the plan for the limited purpose of the instant action, would have 30 days to appoint new counsel for the plan.

LexisNexis® Headnotes

Civil Procedure > Attorneys > General Overview

Governments > Courts > Rule Application & Interpretation

Legal Ethics > Law Firms

HN1 **Civil Procedure, Attorneys**

A court's power to disqualify an attorney is based on its inherent authority to supervise the professional conduct of attorneys appearing before it. In considering a motion to disqualify, the court should determine if disqualification is an appropriate means of enforcing the applicable disciplinary rule. The court should consider the ends that the disciplinary rule is designed to serve and any countervailing policies, such as permitting a litigant to retain the counsel of his choice and enabling attorneys to practice without excessive restrictions. The party seeking to disqualify opposing counsel must clearly demonstrate that continued representation would be impermissible, but doubts as to the existence of a conflict of interest should be resolved in favor of disqualification.

Legal Ethics > Professional Conduct > General Overview

HN2 **Legal Ethics, Professional Conduct**

The Rules of Professional Conduct adopted by the Supreme Court of Pennsylvania serve as the standards for professional conduct that attorneys appearing before the U.S. District Court for the Eastern District of Pennsylvania must comply with. U.S. Dist. Ct., E.D. Pa., R. 83.6(IV)(B).

Legal Ethics > Client Relations > Conflicts of Interest

HN3 **Client Relations, Conflicts of Interest**

See Pa. R. Prof. Conduct 1.7(a).

Legal Ethics > Client Relations > Conflicts of Interest

HN4 **Client Relations, Conflicts of Interest**

Pa. R. Prof. Conduct 1.7(a) precludes representation of opposing parties in litigation. Simultaneous representation of parties whose interests in litigation may conflict, such as co-plaintiffs or co-defendants, is governed by Pa. R. Prof. Conduct 1.7(b).

Legal Ethics > Client Relations > Representation > Acceptance

Legal Ethics > Client Relations > Conflicts of Interest

HN5 **Representation, Acceptance**

Loyalty is an essential part of a lawyer's relationship with a client. If an impermissible conflict of interest arises after representation has been undertaken, the lawyer should withdraw from the representation. Loyalty to a client is impaired when a lawyer cannot consider, recommend or carry out an appropriate course of action for the client because of the lawyer's other responsibilities or interests. The conflict in effect forecloses alternatives that would otherwise be available to the client. A possible conflict does not itself preclude the representation. The critical questions are the likelihood that a conflict will eventuate and, if it does, whether it will materially interfere with the lawyer's independent professional judgment in considering alternatives or foreclose courses of action that reasonably should be pursued on behalf of the client. Consideration should be given to whether the client wishes to accommodate the other interest involved.

Legal Ethics > Client Relations > Conflicts of Interest

HN6 **Client Relations, Conflicts of Interest**

An impermissible conflict may exist by reason of substantial discrepancy in the parties' testimony, incompatibility in positions in relation to an opposing party or the fact that there are substantially different possibilities of settlement of the claims or liabilities in question. A client may consent to representation regardless of a conflict. However, when a disinterested

lawyer would decide that the client should not agree to the representation, the lawyer involved cannot properly provide representation on the basis of the client's consent. When there is more than one client involved, the question of a conflict must be decided as to each client.

Civil Procedure > Remedies > Injunctions > Preliminary & Temporary Injunctions

HN7 **Injunctions, Preliminary & Temporary Injunctions**

A preliminary injunction is proper when a party will suffer immediate irreparable injury which cannot be redressed by a legal or an equitable remedy following a trial. A party seeking a preliminary injunction must demonstrate: (1) a likelihood of success on the merits; (2) that it will suffer irreparable harm if the injunction is denied; (3) that granting preliminary relief will not result in even greater harm to the nonmoving party; and (4) that the public interest favors such relief.

Governments > Fiduciaries

Pensions & Benefits Law > ... > Fiduciaries > Fiduciary Responsibilities > General Overview

Pensions & Benefits Law > ERISA > Fiduciaries > General Overview

HN8 **Governments, Fiduciaries**

Primary responsibility of a benefit plan administrator is to administer the plan for the exclusive benefit of the participants and their beneficiaries. Furthermore, as fiduciaries of the plan, the administrator must function solely in the interest of the beneficiaries of the plan and with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.

Civil Procedure > Parties > Capacity of Parties > General Overview

HN9 **Parties, Capacity of Parties**

Courts have the power to order the appointment of a representative for a party whose interests may not be adequately represented.

Civil Procedure > Parties > Capacity of Parties > General Overview

HN10 **Parties, Capacity of Parties**

See *Fed. R. Civ. P. 17(c)*.

Counsel: **[*1]** For Plaintiff PRESSMAN-GUTMAN CO., INC.: Christopher M. Tretta, Yost and Tretta, Philadelphia, PA.

For Defendant FIRST UNION NATIONAL BANK: Erin Elizabeth Floyd and Joseph G. Derespino, Derespino & Dougher, PC, Philadelphia, PA.

For Defendant/Cross Claimant FOREFRONT CAPITAL ADVISORS, LLC: Zachary L. Grayson, Philadelphia, PA.

For Third Party Defendants ALVIN P. GUTMAN and JAMES C. GUTMAN: Alvin P. Gutman, Pro se, CMS Companies, Philadelphia, PA, James C. Gutman, Pro se, Pressman-Gutman Co., Inc., New York, NY, and Christopher M. Tretta, Yost and Tretta, Philadelphia, PA.

For Cross Defendant/Third Party Plaintiff FIRST UNION NATIONAL BANK: Joseph G. Derespino, Derespino & Dougher, PC, Philadelphia, PA.

Judges: LAWRENCE F. STENGEL, J.

Opinion by: LAWRENCE F. STENGEL

Opinion

Stengel, J.

Stengel, J. November 30, 2004

Pressman-Gutman Co., Inc. ("Pressman-Gutman"), plaintiff, brought this ERISA action on behalf of its employee profit-sharing plan, claiming that First Union National Bank ("First Union") and Forefront Capital Advisors, LLC ("Forefront"), defendants, mismanaged its investments. First Union filed a third-party complaint against Alvin and James Gutman ("the Gutmans"), **[*2]**

individually and as officers of Pressman-Gutman and its profit-sharing plan. On August 30, 2004, I found that Hamburg and Golden, P.C.'s ("Hamburg and Golden") representation of both the profit-sharing plan and the Gutmans presented a conflict of interest and I disqualified Hamburg and Golden from representing the Gutmans. On September 8, 2004, Forefront and First Union each filed a motion for reconsideration of the August 30, 2004 order, requesting that Hamburg and Golden be completely disqualified from this case. Forefront also filed a separate motion, requesting that an independent party be appointed to replace the Gutmans as a representative of the profit-sharing plan. I will grant all three motions.

I. BACKGROUND

Plaintiff brought this ERISA action on behalf of its profit-sharing plan and all of its participants and beneficiaries against First Union and Forefront to recover losses sustained by the plan. Plaintiff first presents a breach of fiduciary duty claim against First Union, the trustee of the plan, and Forefront, First Union's "sub-advisor." According to plaintiff, First Union and Forefront failed to utilize proper research and analysis in the management of **[*3]** the plan's assets, causing substantial losses. Plaintiff also presents an equitable estoppel claim, claiming reliance on First Union and Forefront's "misrepresentations" that they were skilled, knowledgeable, professional, and conscientious in the management of the plan's assets. Plaintiff alleges that its reliance on First Union and Forefront's misrepresentations resulted in substantial losses.

On April 22, 2003, First Union filed a third-party complaint against Alvin and James Gutman, individually and as officers of Pressman-Gutman and its profit-sharing plan. First Union argues that to the extent its management of the plan was imprudent, the Gutmans breached their fiduciary duties and were negligent by breaching their duties to issue instructions to First Union and Forefront which would not injure, jeopardize, or impair the plan's assets. First Union demands judgment in its favor and against the Gutmans for contribution and/or indemnity in the event that it is found liable to plaintiff.

On August 1, 2003, First Union filed a motion to disqualify Hamburg and Golden from representing both the profit-sharing plan and the Gutmans, alleging that the joint representation presented a **[*4]** conflict of interest. On September 11, 2003, the Honorable J. Curtis Joyner of the United States District Court for the Eastern District of Pennsylvania denied the motion, indicating that there was insufficient evidence to disqualify counsel at that time. *Pressman-Gutman Co. v. First Union Nat'l Bank, No. 02-8442, n.1, 2003 U.S. Dist. LEXIS 26096, at *2 (E.D. Pa. Sept. 11, 2003)*.

On April 6, 2004, the Gutmans filed a motion for summary judgment on the third-party complaint, arguing that First Union is substantially more at fault than they are and thus contribution should not be permitted in this case. The Gutmans also contended that they were not fiduciaries with respect to the investment decisions. On May 13, 2004, Judge Joyner denied the motion, stating:

> Pressman-Gutman Co., Inc. is a named fiduciary of the Plan, who acted at all relevant times by and through Alvin and James Gutman in their capacities as officers and directors. Plf.'s Complaint PP 2-3. It is true that the trust and plan documents give the trustees, or an appointed investment manager, sole responsibility for management of the assets. See Document No. 56, Exs. 1, 2. However, to the extent that the Gutmans may have used **[*5]** their positions to cause First Union and/or Forefront to relinquish their independent discretion with respect to management of the assets and exercised actual control over the assets, the Gutmans may be liable as fiduciaries for investment decisions. *See Sommers Drug Stores Co. Employee Profit Sharing Trust v. Corrigan Enterprises, Inc., 793 F.2d 1456, 1459-60 (5th Cir. 1986)*. We find that First Union has established triable issues with respect to the Gutmans['] actual control over plan assets and investment decisions. Genuine issues of material fact still exist on this record, most importantly, identification of the alleged inappropriate stock. In addition, the Gutmans, as agents of the Employer, had the responsibility to appoint and remove the trustee and to periodically review the performance of any fiduciary. To the extent that the Gutmans were aware of, approved, or authorized investment goals or objectives that were imprudent, they may be found to have breached fiduciary duties of the Employer under the plan. We believe that it would be premature for us to decide at this juncture whether one fiduciary is substantially more at fault than the other. We therefore **[*6]** DENY Third Party Defendants' Motion for Summary Judgment as to these claims.

Pressman-Gutman Co., Inc. v. First Union Nat'l Bank, 2004 U.S. Dist. LEXIS 8955, No. 02-8442, slip. op. at 2

n.1 (E.D. Pa. May 13, 2004).

These findings by Judge Joyner, i.e., that there are genuine issues in this case concerning the Gutmans' control over the plan assets and investment decisions, are significant to the disqualification issue. When Judge Joyner first considered the defendants' motion to disqualify, he had not yet considered this case in the summary judgment posture. After the first disqualification motion was decided, the Gutmans' *Rule 56* motion was filed and briefed. With the benefit of the *Rule 56* papers, Judge Joyner identified substantive issues regarding the actions of the Gutmans in managing the plan. These issues give new and important support to the defendants' disqualification argument.

Forefront then filed a second motion to disqualify Hamburg and Golden from its joint representation of the profit-sharing plan and the Gutmans, indicating that there was sufficient evidence of the Gutmans' liability for this court to find a conflict of interest. On August 30, 2004, I granted Forefront's motion and **[*7]** disqualified Hamburg and Golden from representing the Gutmans as third-party defendants. In granting the motion, I stated:

> This court finds that plaintiff's potential claims against third-party defendants present directly adverse interests. Plaintiff's settlement opportunities may well be adversely affected by joint representation. Plaintiff's avenues of obtaining recovery are adversely affected by Hamburg and Golden's joint representation of plaintiff and third-party defendants because third-party defendants may, in fact, be responsible for the plaintiff plan's losses.
>
> This court finds it unreasonable for Hamburg and Golden to believe it can adequately represent both plaintiff and third-party defendants. Plaintiff is an employee profit-sharing plan, comprised of a group of employees and former employees. This group has in excess of a hundred members and includes Alvin and James Gutman, the principals of the company. There is no question that the Gutmans worked with defendants on the plan's investments. Defendant First Union has introduced the claim that the Gutmans' investment choices, not defendants' investment choices, are responsible for the plan's alleged losses. The court's **[*8]** review of the record reveals that plaintiff has not consented to Hamburg and Golden's joint representation of plaintiff and third-party defendants. Therefore, Hamburg and Golden is disqualified from representing third-party defendants in this action.

Pressman-Gutman Co. v. First Union Nat'l Bank, 2004 U.S. Dist. LEXIS 17720, No. 02-8442, slip. op. at 4 (E.D. Pa. Aug. 30, 2004).

On September 8, 2004, Forefront and First Union each filed a motion for reconsideration of the August 30, 2004 order, requesting that Hamburg and Golden be completely disqualified from this action. They contend that the Rules of Professional Conduct required Hamburg and Golden's complete disqualification because the firm's duty to protect confidential information obtained during the course of its representation of the Gutmans would be at odds with the firm's duty to disclose such information for the benefit of the plan. Forefront also filed a motion for the appointment of an independent party to act on behalf of the profit-sharing plan because the Gutmans can not adequately represent the plan.

II. DISCUSSION

A. Defendants' Motions for Reconsideration

HN1[] A court's power to disqualify an attorney is based on **[*9]** its inherent authority to supervise the professional conduct of attorneys appearing before it. U.S. v. Miller, 624 F.2d 1198, 1201 (3d Cir. 1980) (citations omitted). In considering a motion to disqualify, the court should determine if disqualification "is an appropriate means of enforcing the applicable disciplinary rule." *Id.* The court "should consider the ends that the disciplinary rule is designed to serve and any countervailing policies, such as permitting a litigant to retain the counsel of his choice and enabling attorneys to practice without excessive restrictions." *Id.* (citations omitted). The party seeking to disqualify opposing counsel must clearly demonstrate that continued representation would be impermissible, Cohen v. Oasin, 844 F. Supp. 1065, 1067 (E.D. Pa. 1994) (citation omitted), but doubts as to the existence of a conflict of interest should be resolved in favor of disqualification. *See* Int'l Bus. Mach. Corp. v. Levin, 579 F.2d 271, 283 (3d Cir. 1978) (citations omitted).

HN2[] The Rules of Professional Conduct adopted by the Supreme Court of Pennsylvania serve as the standards for professional conduct that attorneys **[*10]** appearing before this court must comply with.

Commonwealth Ins. Co. v. Graphix Hot Line, Inc., 808 F. Supp. 1200, 1203 (E.D. Pa. 1992); *E.D.Pa.R. 83.6(IV)(B)*. Rule 1.7 of the Pennsylvania Rules of Professional Conduct, entitled Conflict of Interest: General Rule, states:

> *HN3*[] (a) A lawyer shall not represent a client if the representation of that client will be directly adverse to another client, unless:
>
> (1) the lawyer reasonably believes the representation will not adversely affect the relationship with the other client; and
>
> (2) each client consents after consultation.
>
> (b) A lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client or to a third person, or by the lawyer's own interests, unless:
>
> (1) the lawyer reasonably believes the representation will not be adversely affected; and
>
> (2) the client consents after full disclosure and consultation. When representation of multiple clients in a single matter is undertaken, the consultation shall include explanation of the implications of the common representation and the advantages and risks involved. **[*11]**

Pa.R.P.C. 1.7. *HN4*[] Paragraph (a) precludes representation of opposing parties in litigation. *Id.*, Comment. Simultaneous representation of parties whose interests in litigation may conflict, such as co-plaintiffs or co-defendants, is governed by paragraph (b). *Id.*

HN5[] Loyalty is an essential part of a lawyer's relationship with a client. *Id.* If an impermissible conflict of interest arises after representation has been undertaken, "the lawyer should withdraw from the representation." *Id.* (citing *Pa.R.P.C. 1.16*).

> Loyalty to a client is impaired when a lawyer cannot consider, recommend or carry out an appropriate course of action for the client because of the lawyer's other responsibilities or interests. The conflict in effect forecloses alternatives that would otherwise be available to the client. . . A possible conflict does not itself preclude the representation. The critical questions are the likelihood that a conflict will eventuate and, if it does, whether it will materially interfere with the lawyer's independent professional judgment in considering alternatives or foreclose courses of action that reasonably should be pursued on behalf of the client. Consideration **[*12]** should be given to whether the client wishes to accommodate the other interest involved.

Id. *HN6*[] "An impermissible conflict may exist by reason of substantial discrepancy in the parties' testimony, incompatibility in positions in relation to an opposing party or the fact that there are substantially different possibilities of settlement of the claims or liabilities in question." *Id.*

A client may consent to representation regardless of a conflict. *Id*. However, when a disinterested lawyer would decide that the client should not agree to the representation, the lawyer involved cannot properly provide representation on the basis of the client's consent. *Id.* When there is more than one client involved, the question of a conflict must be decided as to each client. *Id.*

In this case, Judge Joyner previously found that the Gutmans may be liable as fiduciaries for investment decisions to the extent that they may have used their positions to cause First Union and/or Forefront to relinquish their independent discretion with respect to management of the assets and exercised actual control over the assets.*Pressman-Gutman Co., Inc. v. First Union Nat'l Bank, 2004 U.S. Dist. LEXIS 8955, No. 02-8442, slip. **[*13]** op. at 2 n.1 (E.D. Pa. May 13, 2004)*. Judge Joyner found that there are triable issues regarding the Gutmans' actual control over plan assets and investment decisions. *Id.* According to Judge Joyner, genuine issues of material fact exist in this case, such as identification of the alleged inappropriate stock. *Id.* Moreover, the Gutmans, as agents of the plan, had the responsibility to appoint and remove the trustee and to periodically review the performance of any fiduciary. *Id.* To the extent that the Gutmans were aware of, approved, or authorized investment goals or objectives that were imprudent, they may be found to have breached fiduciary duties to the plan. *Id.*

Based on Judge Joyner's findings and my independent review of the facts and the arguments advanced by counsel, I concluded on August 30, 2004 that Hamburg and Golden's joint representation of plaintiff and third-party defendants presented a conflict of interest.

Pressman-Gutman Co., Inc. v. First Union Nat'l Bank, 2004 U.S. Dist. LEXIS 17720, No. 02-8442, slip. op. at 4 (E.D. Pa. Aug. 30, 2004). Specifically, I concluded that the profit-sharing plan's avenues of obtaining recovery were adversely affected by Hamburg and Golden's joint **[*14]** representation of the plan and the Gutmans because the Gutmans may, in fact, be responsible for the plan's losses. *Id.* I found that it was unreasonable for Hamburg and Golden to believe that it could adequately represent both the plan and the Gutmans. *Id.* Furthermore, I found that the plan had not consented to Hamburg and Golden's joint representation of the plan and the Gutmans. *Id.* After further consideration of this issue, I conclude that the decision to disqualify counsel for third-party defendants was correct, but did not go far enough. I had hoped to achieve some efficiency by removing the conflict in a technical sense and allowing plaintiff to proceed with counsel of its choice, who are also very familiar with the case. Yet after an opportunity to review the record again, it appears to me that plaintiff's counsel may well be counsel of the Gutmans' choice, not necessarily of the plan's choice. It further appears to me that removing the conflict of interest in a technical sense, by removing Hamburg and Golden firm from one half of the representation, i.e., third-party defendants, the conflict still remains in a practical sense. It is clear that the Gutmans hired plaintiff's **[*15]** counsel and that plaintiff's counsel are taking their direction from the Gutmans. In fact there is no indication from plaintiff's counsel that they are taking direction or even communicating with the remaining hundred or so members of the plan, the named plaintiff in the case.

Upon further review of the record as it existed on August 30, 2004, I conclude that Hamburg and Golden must also be disqualified from representing the profit-sharing plan as plaintiff. Because of Hamburg and Golden's duty of loyalty to the Gutmans, who it represented on August 30, 2004, Hamburg and Golden could not recommend to the plan that it act against the Gutmans, as well as, or instead of, First Union and Forefront. Hamburg and Golden could only recommend to the plan that it proceed only against First Union and Forefront. Based on Hamburg and Golden's duty of loyalty to the Gutmans, who may well be liable for the plan's losses, I conclude that it was unreasonable for Hamburg and Golden to believe that it could adequately represent the plan. Moreover, since only the Gutmans represented the plan in this action, I find that any consent given by the plan to Hamburg and Golden for Hamburg and Golden's continued **[*16]** representation of the plan was invalid.

Hamburg and Golden argues that the purpose of Forefront and First Union's motions for reconsideration is to delay this case from proceeding to trial and that the court should deny the motion on that basis alone. The record, however, reveals that First Union requested that Hamburg and Golden consider disqualifying itself, without this court's involvement, in October 2003, when a conflict of interest became apparent. [1] The record also reveals that Forefront twice requested that Hamburg and Golden consider disqualifying itself, without the court's involvement, in February 2004, after the conflict further developed. [2] Since the present motions were only filed several months after Forefront and First Union requested that Hamburg and Golden disqualify itself, without the court's involvement, I find that these motions were not filed to delay this case from proceeding to trial.

[*17] Hamburg and Golden also argues that the present motions are actually requests for a preliminary injunction, and defendants cannot carry the burden of proof for a preliminary injunction. ***HN7***[⬆] A preliminary injunction is proper when a party will suffer immediate irreparable injury "which cannot be redressed by a legal or an equitable remedy following a trial." *Acierno v. New Castle County, 40 F.3d 645, 653 (3d Cir. 1994)* (quotation omitted). A party seeking a preliminary injunction must demonstrate: "(1) a likelihood of success on the merits; (2) that it will suffer irreparable harm if the injunction is denied; (3) that granting preliminary relief will not result in even greater harm to the nonmoving party; and (4) that the public interest favors such relief." *Kos Pharms., Inc. v. Andrx Corp., 369 F.3d 700, 708 (3d Cir. 2004)* (citation omitted).

In this case, Forefront and First Union do not argue that they will suffer immediate irreparable harm if Hamburg and Golden remains in this case. Instead, defendants contend that the Gutmans may be liable for the profit-sharing plan's losses, and Hamburg and Golden's duty of loyalty to the Gutmans precludes **[*18]** it from recommending to the plan that it seek recovery from the Gutmans. This is not a request for a preliminary injunction. This is a motion for disqualification based upon the Rules of Professional Conduct.

Citing *Hamilton v. Merrill Lynch, 645 F. Supp. 60 (E.D. Pa. 1986)*, and *Altschul v. Paine Webber, Inc., 488 F. Supp. 858 (S.D.N.Y. 1980)*, Hamburg and Golden also

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[1] First Union's Memorandum of Law in Support of the Motion for Reconsideration, 9/8/04, Exhibit D.

[2] Forefront's Memorandum of Law in Support of the Renewed Motion for Disqualification, 3/4/04, Exhibits 14-15.

notes that courts have previously allowed counsel to continue representation of multiple clients in cases where the joint representation presented an alleged conflict of interest. In *Hamilton*, plaintiffs, represented by a single attorney, claimed that defendants engaged in fraudulent activities in connection with the sale of securities in drilling operations. One of the defendants later filed a counterclaim against one of the plaintiffs, alleging that the plaintiff was responsible for the injuries to the other plaintiffs. Before discovery was complete, defendants moved to disqualify plaintiffs' counsel because of an alleged conflict of interest in the joint representation. The court, however, denied the motion, noting that plaintiffs were family members and that each plaintiff "consented **[*19]** to joint representation after full disclosure of the possible effect of such representation, and after obtaining the advice of independent counsel." *Hamilton, 645 F. Supp. at 62*.

In *Altschul*, plaintiffs filed a lawsuit against defendants, stating that defendants wrongfully depleted their securities account. One of the defendants later brought a third-party claim against plaintiff's son, who was employed by the defendant as a registered representative to service his parents' account. The defendant claimed that it was entitled to indemnification from plaintiff's son in the event that it was held liable to plaintiffs. Before discovery was complete, the defendant moved to disqualify counsel, who represented plaintiffs as well as their son, because of an alleged conflict of interest. However, the court denied the motion, noting that counsel's clients were family members and that they all consented to counsel's joint representation. *Altschul, 488 F. Supp. at 859, 861*.

I find that this case is distinguishable from *Hamilton* and *Altschul*. Unlike *Hamilton* and *Altschul*, the present motions regarding counsel's disqualification were filed **[*20]** after extensive discovery established that there was a conflict of interest. [3] Moreover, the record in this case does not reveal that the Gutmans and the plan participants are all members of the same family. There certainly is no record of disclosure and waiver of a conflict in this case. Despite all the informal and formal requests to have plaintiff's counsel removed, it is noteworthy to this court that plaintiff's counsel has never once produced any evidence that the members of the plan have any idea about a possible conflict, let alone a full disclosure and waiver which might, under certain circumstances, remove the conflict. Thus, this court is not confronted by a unique situation, such as the one presented in *Hamilton* and *Altschul*, which might persuade it to allow such joint representation. Finally, since only the Gutmans represent the plan in this action, any consent given by the plan to Hamburg and Golden for Hamburg and Golden's continued representation of the plan was invalid. Accordingly, since the circumstances presented in *Hamilton* and *Altschul* are not present here, I will not allow Hamburg and Golden to continue representing the plan.

[*21] Based on the foregoing, I find that Hamburg and Golden must be disqualified from representing the plan and that new counsel must be appointed to replace Hamburg and Golden.

B. Forefront's Motion for the Appointment of an Independent Party

As administrators of the profit-sharing plan, the Gutmans' ***HN8***[⬆] primary responsibility is to administer the plan for the exclusive benefit of the participants and their beneficiaries. [4]

Furthermore, as fiduciaries of the plan, [5] the Gutmans must function

> solely in the interest of the beneficiaries of the plan and "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims."

Ream v. Frey, 107 F.3d 147, 153 (3d Cir. 1997) (citation omitted); *29 U.S.C. § 1104(a)(1)(B)*.

[*22] This court finds that the Gutmans may well not be able to fulfill their duties as administrators and fiduciaries of the plan because of their potential liability. The Gutmans' duty to the plan includes seeking full compensation for the plan's losses. Because the Gutmans may be liable to the plan, the duty to the plan may include presenting claims against the Gutmans. However, because the Gutmans have an interest in protecting themselves from liability, the Gutmans are not

[3] Discovery in this case was ordered to be complete by March 23, 2004. *Pressman-Gutman Co., Inc. v. First Union Nat'l Bank*, No. 02-8442 (E.D. Pa. Nov. 21, 2003).

[4] The Gutmans' Memorandum of Law in Support of the Motion for Summary Judgment, 4/6/04, Exhibit 1.

[5] *Id.*

likely to act against themselves for the benefit of the plan, and the plan's avenues of obtaining recovery may be adversely affected. Accordingly, I will appoint a guardian ad litem who will replace the Gutmans and serve as administrator of the plan for the limited purpose of this lawsuit. [6] The guardian ad litem will, in turn, appoint new counsel for the plan.

[*23] III. CONCLUSION

Based on the foregoing, I grant First Union and Forefront's motions for reconsideration and find that Hamburg and Golden must be completely disqualified from this case. I also grant Forefront's motion for the appointment of an independent party. An order granting the motions for reconsideration follows. The appointment of a guardian ad litem will be made in a separate order.

ORDER

AND NOW, this 30th day of November, 2004, upon consideration of First Union National Bank and Forefront Capital Advisors, LLC's motions for reconsideration or clarification of the court's August 30, 2004 order, and replies thereto, it is hereby ORDERED that said motions are GRANTED and that this court's order of August 30, 2004 is VACATED. Hamburg and Golden, P.C. is completely disqualified from this case. A guardian ad litem, who will be appointed in a separate order, will have thirty (30) days to appoint new counsel. New counsel shall be paid by the Pressman-Gutman Co., Inc. Profit-Sharing Plan's trust fund. All pending motions shall be STAYED until thirty (30) days after the filing of the order appointing the guardian ad litem. No further motions, briefs, or memoranda **[*24]** shall be filed during that period.

/s/

LAWRENCE F. STENGEL, J.

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[6] I note that *HN9*[↑] courts have the power to order the appointment of a representative for a party whose interests may not be adequately represented. *See* ***F.R.C.P. 17(c)***(stating that *HN10*[↑] "the court shall appoint a guardian ad litem for an infant or incompetent person not otherwise represented in an action").

Scholes v. Tomlinson

United States District Court for the Northern District of Illinois, Eastern Division

July 26, 1991, Decided ; July 29, 1991, Docketed

Case Nos. 90 C 1350, 90 C 6615, 90 C 7201, (Related to No. 89 C 8407)

Reporter
1991 U.S. Dist. LEXIS 10486 *; 1991 WL 152062

STEVEN S. SCHOLES, not individually, but solely as Receiver for Michael S. Douglas, D & S Trading Group, Ltd., Analytic Trading Service, Inc., Analytic Service, Inc., and on behalf of a class and HARRIS and DIANE DEJONG, both individually and on behalf of those similarly situated, Plaintiffs, v. ROBERT G. TOMLINSON, DARLENE TOMLINSON, GEORGE EDGAR TOMLINSON, JR., and TOMLINSON ENTERPRISES, LTD., Defendants. STEVEN S. SCHOLES, not individually, but solely as Receiver for Michael S. Douglas, D & S Trading Group, Ltd., Analytic Trading Systems, Inc., Analytic Trading Service, Inc., and Market Systems, Inc. and JOHN LaVINKA and PAMELA LaVINKA, individually and on behalf of those similarly situated, Plaintiffs, v. MICHAEL P. MOORE, Defendant. STEVEN S. SCHOLES, not individually, but solely as Receiver for D & S Trading Group, Ltd., Analytic Trading Systems, Inc., Analytic Trading Service Inc., and Market Systems, Inc. and on behalf of a class, and JOHN LaVINKA and PAMELA LaVINKA, individually and on behalf of all persons similarly situated, Plaintiffs, v. STONE, McGUIRE & BENJAMIN, HOWARD L. STONE, and MICHAEL L. SIEGEL, Defendants

Core Terms

holders, receivership, disqualify, entities, ethical, belonging, disqualification, dual, investors, appointed, injunction, wrongdoing, permanent, purports

Case Summary

Procedural Posture

In these three cases, defendant individuals and corporations sought to disqualify plaintiff receiver from acting as class representative and to disqualify the receiver's law firm from representing the account holder class. The individuals and corporations also sought to remove the receiver and to disqualify his law firm from representing the receiver.

Overview

The receiver was appointed to operate the receivership entities in a securities fraud case. Purporting to act on authority of the court's orders, the receiver also filed three class action lawsuits, naming himself as the class representative. The receiver was also a partner in the law firm representing the receiver. The individuals and corporations objected to this apparent conflict of interest and the court agreed. The court held that other courts had refused to permit class attorneys, their relatives, or business associates from acting as the class representative. The court noted that the receiver's duty as receiver was to preserve the assets of the receivership entities for the benefit of all creditors. On the other hand, the receiver's duty as class representative was to secure the most favorable distribution possible of those same assets on behalf of the account holder class. The court concluded that the receiver could not simultaneously exercise independent judgment as to both. The court refused, however, to disqualify the receiver from acting as receiver or to disqualify his law firm because the same potential for conflict of interest did not exist.

Outcome

The court granted in part and denied in part the individuals' and corporations' motion to disqualify the receiver and his law firm. The motion was granted as to disqualification as class representative but denied as to removal of the receiver and his law firm.

LexisNexis® Headnotes

Legal Ethics > Professional Conduct > Illegal Conduct

HN1[] **Professional Conduct, Illegal Conduct**

United States District Court for the Northern District of Illinois Rule 3.54(B) establishes the Model Code of Professional Responsibility of the American Bar Association as the guiding force in evaluating ethical conduct and motions for disqualification which present ethical conflicts.

Civil Procedure > Remedies > Receiverships > General Overview

Civil Procedure > Remedies > Injunctions > Permanent Injunctions

HN2[] **Remedies, Receiverships**

A receiver or like surrogate cannot pursue claims that belong, not to the receivership estate as such, but rather to those who may have an ultimate derivative interest in the estate.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

HN3[] **Class Actions, Prerequisites for Class Action**

A majority of courts have refused to permit class attorneys, their relatives, or business associates from acting as the class representative.

Civil Procedure > ... > Class Actions > Class Attorneys > General Overview

Legal Ethics > Client Relations > Conflicts of Interest

HN4[] **Class Actions, Class Attorneys**

DR 5-101 and 5-102 of the Model Code of Professional Responsibility of the American Bar Association (ABA) prohibit a law firm from representing a client if a lawyer from the same firm may be called as a witness. ABA Model Code of Professional Responsibility, DR 5-101 and 5-102 (1980); ABA Model Rules of Professional Conduct Rule 3.7 (1984); Ill. R. Prof. Conduct 3.7 (1990).

Legal Ethics > Client Relations > Conflicts of Interest

HN5[] **Client Relations, Conflicts of Interest**

DR 5-105 of the Model Code of Professional Responsibility of the American Bar Association (ABA), which emanates from Canon 5's directive that a lawyer should exercise independent judgment, addresses the issue of dual representation. ABA Model Code of Professional Responsibility, Canon 5 (1980). DR 5-105 (A) and (B) prohibit dual representation of clients if the exercise of an attorney's independent professional judgment in behalf of a client will be or is likely to be adversely affected by his representation of another client, or if it would be likely to involve him in representing differing interests. ABA Model Code of Professional Responsibility DR 5-105(A) and (B) (1980). DR 5-105(C) creates an exception to these rules where it is obvious that an attorney can adequately represent the interest of each client and if each consents to the representation after full disclosure of the possible effect of such representation on the exercise of his independent professional judgment on behalf of each. ABA Model Code of Professional Responsibility Dr 5-105(C)(1980). ABA Model Code of Professional Conduct Rule 1.7 (1984); Ill. R. Prof. Conduct 1.7 (1990) (adopting ABA Model Rules of Professional Conduct Rule 1.7 with minor modification). These disciplinary rules are mandatory in character and represent the minimum level of conduct below which no lawyer should

fall.

Judges: **[*1]** James H. Alesia, United States District Judge.

Opinion by: ALESIA

Opinion

MEMORANDUM OPINION AND ORDER

In all three of these related cases, the defendants have filed separate motions to ***disqualify*** Steven S. Scholes ("Scholes") as ***Receiver*** and McDermott, Will & Emery ("MWE") as ***counsel***. For the reasons outlined below, the Court disqualifies Scholes from acting as class representative and ***attorney*** for the class in each case and disqualifies MWE from representing the account holder class in each case, but declines to remove Scholes as ***Receiver***, to ***disqualify*** MWE from continuing to represent Scholes, or to require MWE to forfeit any fees earned in pursuing these cases.

I. Background

All three of these cases arise out of a securities fraud action brought by the Securities and Exchange Commission ("SEC") against Michael S. Douglas ("Douglas"), D & S Trading Group, Ltd., Analytic Trading Systems, and Analytic Trading Service, Inc. under Docket No. 89 C 8407 ("the underlying SEC action"). Douglas devised a massive securities fraud scam in the form of a classic Ponzi scheme, bilking millions of dollars from numerous investors ("account holders"). Douglas has since been convicted for his role in the fraud.

[*2] On November 30, 1989, with Douglas' consent, this Court entered a rather lengthy order of permanent injunction drafted by the SEC. Among other things, Article XI of this order provided for appointment of a receiver to operate the receivership entities and vested the receiver with certain powers, including the authority to "institute such actions as said receiver deems necessary against those individuals, entities, corporations, partnerships, associations or incorporated organizations which the receiver may claim to have wrongfully, illegally or otherwise improperly misappropriated monies or other proceeds *from investors or clients of the Defendants* [the receivership entities]. . . ." (*SEC v. Douglas,* No. 89 C 8407, Order of November 30, 1989 at 10).

On the same day the Court issued the order of permanent injunction, we appointed Scholes, an attorney with the law firm of MWE, as the equitable receiver for *Douglas, D & S Trading Group, Ltd., Analytic Trading Systems, Inc., and Analytic Trading Service, Inc. (SEC v. Douglas, 89 C 8407*, Minute Order of November 30, 1989). Sometime later, on July 5, 1990, the Court also appointed Scholes as equitable receiver for Market Systems, **[*3]** Inc. and vested him with the same powers previously enumerated in Article XI of the November 30, 1989 order. [1] (*SEC v. Douglas*, No. 89 C 8407, Order of July 5, 1990). Scholes retained his law firm, MWE, to represent him in his capacity as Receiver.

In September of 1990, the Court directed the SEC to send all account holders a ballot in order to solicit their input on the direction of the receivership. The SEC tallied the votes and presented the results to the Court. Despite tabulation problems, we determined that the majority of the account holders voted in favor of allowing the Receiver to pursue existing and new litigation in some fashion. For reasons more fully set forth in our previous order, the Court specifically concluded that is was "in the best interests of the account holders to allow the Receiver to wind up existing litigation on an hourly fee basis **[*4]** and, to the extent that the Receiver may have standing to bring certain claims that the individual account holders may not have standing to bring, to allow the Receiver to pursue new litigation on a contingent fee basis." (*SEC v. Douglas,* No. 89 C 8407, Order of October 26, 1990 at 6-7) (emphasis supplied). The Court expressed no opinion as to whether the Receiver did, in fact, have standing to bring any particular claims. Indeed, during the hearing which preceded the entry of this order, the Court expressed its concerns regarding the standing issue.

Purporting to act on the authority of this Court's orders, the Receiver thereafter filed the three related cases

[1] For ease of reference, when necessary, the Court will collectively refer to Douglas and all of his affiliated entities as "the receivership entities."

before us now, as well as other litigation. In each of the three cases, Scholes, a partner with MWE, purports to bring the action in his capacity as Receiver for Douglas and the receivership entities and as a putative class representative of a group of account holders whom Douglas and the receivership entities allegedly defrauded. In each of the three cases, MWE simultaneously purports to act as counsel for Scholes as Receiver and as counsel for the account holder class. Perceiving this dual representation to create an **[*5]** impermissible conflict, the defendants in each of the three cases have moved to ***disqualify*** Scholes as ***Receiver*** and MWE as ***counsel***.

II. Standards for Evaluating Disqualification

HN1[↑] Rule 3.54(B) of the Rules of the United States District Court for the Northern District of Illinois ("Local 3.54(B)") establishes the *Model Code of Professional Responsibility of the American Bar Association* ("the ABA Model Code") as the guiding force in evaluating ethical conduct and motions for disqualification which present ethical conflicts. *See* *Ransburg Corp. v. Champion Spark Plug Co., 648 F.Supp. 1040, 1041 (N.D.Ill 1986)*; *Clay v. Doherty, 608 F.Supp. 295, 301 & n.3 (N.D.Ill. 1985)* (noting that although the local rule, as drafted, appears to establish the ABA Model Code as the standard applicable to attorney discipline, the rule has also been used by the courts to guide them in evaluating motions for disqualification). [2] Accordingly, we refer to the applicable provisions of the ABA Model Code in evaluating defendants' various arguments that Scholes and MWE should be disqualified.

[*6] III. Discussion

The defendants' motions for disqualification raise a variety of issues. Although not all of these issues relate to preceived ethical conflicts, they nonetheless require clarification. We address each of these issues in turn. [3]

A. Scope of Receiver's Authority to Institute Actions

[*7] First, the defendants question the Receiver's standing to bring actions belonging to the account holders. The defendants challenge the breadth of the powers conferred upon the Receiver in Paragraph C of Article XI of the order of permanent injunction entered on November 30, 1989. Citing Judge Shadur's recent opinion in *Scholes v. Schroeder, 744 F.Supp 1419 (N.D. Ill. 1990)*, the defendants argue that Scholes, as designated Receiver for Douglas and the receivership entities, can only bring actions belonging to Douglas and the receivership entities, not actions belonging to the account holders whom Douglas allegedly defrauded. According to the defendants, to the extent that the order of permanent injunction prepared by the SEC and entered by this Court on November 30, 1989 vests the Receiver with more expansive authority, it is unduly broad.

Although Judge Shadur raised the standing issue in the *Schroeder* case and so alerted this Court, this is the first time that the parties have formally raised the issue before us. Now that we have had the opportunity to review and consider the *Schroeder* decision and the authorities it cites, we agree that the language in **[*8]** the order of permanent injunction which purports to confer upon the Receiver the authority to bring actions belonging to the "investors or clients" of the receivership entities exceeds that permitted by law. As Judge Shadur correctly pointed out, "***HN2***[↑] a receiver or like surrogate cannot pursue claims that belong, not to the receivership estate as such, but rather to those who may have an ultimate derivative interest in the estate." *Schroeder, 744 F.Supp. at 1422* (citing *Caplin v. Marine*

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[2] The Court notes that Local Rule 3.54(B) has very recently been supplanted by new Local Rule 3.52(B). The new rule establishes the *Rules of Professional Conduct for the Northern District of Illinois* (a code of conduct essentially comprised of selected portions of the *American Bar Association Model Rules of Professional Conduct* ("the ABA Model Rules") and discipline and, presumably, attorney disqualification. Because the full court has not yet formally adopted the *Rules of Professional Conduct for the Northern District of Illinois* (they are still labeled "proposed" rules and have been only tentatively approved), however, implementation of new Local Rule 3.52(B) has been delayed pending the full court's adoption these rules. Accordingly, the Court continues to use Local Rule 3.54(B) and the ABA Model Code as its benchmark, though we note that the result would be the same under the ABA Model Rules and the Illinois Rules.

[3] At the outset, MWE and Scholes challenge certain defendants' standing to seek disqualification. Because we believe that it is the ethical responsibility of all attorneys to alert the Court to possible ethical conflicts, we reject this argument summarily. *See ABA Model Code of Responsibility* DR 103(A) & EC 1-4 (1980); *Coleman v. Smith, 814 F.2d 1142, 1147 (7th Cir. 1987)* ("Because of the dire consequences that joint representation may bring, a trial judge must be ever sensitive to that possibility and act accordingly, even absent an objection.") (emphasis supplied); *United States v. White,* 743 F.2d 488, 498 (7th Cir. 1984) (Flaum, J., concurring) (citing other cases).

Midland Grace Trust Co. of New York, 406 U.S. 416, 92 S.Ct. 1678, 1685-88 (1972); *see also Fleming v. Lind-Waldock & Co., 922 F.2d 20, 25 (1st Cir. 1990)*. Accordingly, we modify the order of permanent injunction entered November 30, 1989 to omit the words "investors or clients of" in Paragraph D of Article XI and to omit any other language in the order which purports to confer authority upon the Receiver to institute actions belonging to the investors, clients, or account holders of the receivership entities. As modified, the order authorizes the Receiver to institute only actions belonging to Douglas and the receivership entities. **[*9]** This modification should eliminate any further confusion as to the scope of the Receiver's authority to institute litigation. [4]

B. Scholes' Authority to Act as Putative Class Representative

Scholes is the court-appointed Receiver, a putative class representative, and a partner at MWE. At the same time, MWE is acting as counsel for the Receiver and counsel for the class. According to the defendants, Scholes cannot act as a putative class representative for two reasons. First, Scholes lacks standing to do so. Second, even if Scholes had standing, ethical conflicts prevent him from doing so because his respective duties as Receiver and putative class representative conflict and because an attorney representing a class (or associated **[*10]** with the law firm representing the class) should not simultaneously act as a class representative. Scholes disagrees, claiming that prior orders entered in this and related litigation, as well as case law, permit him to act as class representative while his law firm acts as class counsel. We disagree with Scholes on both counts.

1. Prior Court Orders

MWE and Scholes appear to labor under the misconception that certain orders entered in this and related litigation implicitly conferred upon them the authority to bring a class action on behalf of the account holders. While we understand Scholes' stated desire to protect the account holders from having their claims lapse because of statute of limitations problems, we vehemently disagree. First, this Court's order of October 26, 1990 contained no language which authorized MWE or Scholes to bring a class action on behalf of the account holders. Instead, the order of October 26, 1990 merely permitted Scholes, to the extent that he might have standing to bring certain claims that the individual account holders might not have standing to bring, to pursue such litigation on a contingent fee basis. The order further advised the account holders **[*11]** that if they wished to pursue other claims through litigation, they should immediately contact an attorney of their choice. Finally, the order directed the SEC to advise the account holders that certain claims would be time-barred if not filed before November 13, 1990, and that the account holders should consult an attorney of their choice if they wished to pursue such litigation. *(SEC v. Douglas,* No. 89 C 8407, Order of October 26, 1990 at 6-7). Thus, contrary to Scholes' claims, this Court's order of October 26, 1990 contemplated that Scholes might not have standing to assert certain claims belonging to the investors and that MWE might have a conflict; the order in no way authorized Scholes or MWE to bring this litigation.

Similarly, this Court's previous entry of orders granting Scholes leave to file amended complaints in actions containing class allegations substantially similar to those asserted in these cases did not operate to vest Scholes or MWE with authority to bring a class action on behalf of the account holders. By granting a litigant leave to file an amended complaint, the Court does not lend its imprimatur to the allegations contained in that complaint. The **[*12]** Court does not act as an adversary; any objections to the complaint are properly raised by opposing counsel. Moreover, within the emergency motions seeking leave to file these amended complaints, Scholes himself acknowledged that although certain defendants "had raised issues relating to the Receiver's standing to bring securities claims" on behalf of account holders, Scholes was filing these complaints to protect these account holders' claims from being time-barred. *(Scholes v. Douglas,* No. 90 C 1292, Emergency Motion for Leave to File First Amended Complaint at para. 5; *Scholes v. Tomlinson,* No. 90 C 1350, Emergency Motion for Leave to File Second Amended Complaint Instanter at para. 5).

Likewise, the Court assigns little, if any, weight to Judge Lindberg's order granting Scholes general leave to file class actions in his capacity as class representative. Significantly, Judge Lindberg entered this order in his capacity as emergency judge. The order, which consists of a single sentence and appears to be a draft prepared by Scholes or MWE, merely granted Scholes "leave to

[4] Because this modification affects the original order of permanent injunction entered on November 30, 1989 in *SEC v. Douglas, 89 C 8407*, and will apply to all litigation initiated by the Receiver, we enter a separate order in the underlying SEC litigation noting the modification.

file complaints in the capacity of a class representative in those instances where the Receiver deems it **[*13]** prudent to do so." *(SEC v. Douglas,* No. 89 C 8407, Order of December 12, 1990) (Lindberg, J.). Unfamiliar with this litigation and its many procedural nuances, Judge Lindberg never had occasion to address or question Scholes' authority or standing to file complaints in the capacity of a class representative. Accordingly, to the extent that Judge Lindberg's order granted Scholes authority to file complaints in the capacity of a class representative for the account holders, we vacate it, and to the extent that MWE and Scholes believe that they have been acting under the authority of prior orders entered in this and related litigation, we dispel that misconception once and for all.

2. Standing and Ethical Considerations

Our review of applicable case law also lends little support to Scholes' argument that no conflict exists in the present context. As this circuit observed in *Susman v. Lincoln American Corp., 561 F.2d 86 (7th Cir. 1977)*, ***HN3***[⬆] "a majority of courts . . . have refused to permit class attorneys, their relatives, or business associates from acting as the class representative." *Susman, 561 F.2d at 90*. According to the court in *Susman,* **[*14]** the rationale for disallowing this practice is rooted in both standing and ethical considerations. *Susman, 561 F.2d at 91*; *see also Barliant v. Follett Corp., 74 Ill.2d 226, 236-37, 384 N.E.2d 316, 321 (1979)*.

Both of those concerns apply with equal force here. First, as made clear in the Court's preceding discussion, Scholes cannot assert claims belonging to the account holders. As a consequence, he has no standing to act as a putative class representative because he is not "similarly situated" to the account holders. *See Susman, 561 F.2d at 92*. Scholes' lack of standing therefore renders him an inadequate class representative. That Scholes has aligned himself with the account holder class in litigation as "an additional class representative" does not persuade us otherwise.

Second, ethical considerations militate against allowing Scholes to serve as class representative while acting as Receiver, as well as allowing Scholes to act as class representative while his law firm represents both him and the class. Obviously, Scholes' duty as Receiver is to preserve the assets of the receivership entities for the benefit **[*15]** of all creditors. On the other hand, Scholes' duty as class representative is to secure the most favorable distribution possible of those same assets on behalf of the account holder class. Scholes cannot simultaneously exercise independent judgment as to both. *See ABA Model Code of Professional Responsibility* Canon 5 & DR 5-105 (1980).

Ethical considerations similarly counsel against allowing Scholes to serve as class representative while his law firm represents both him and the class. For example, a conflict certainly would arise if Scholes, as named putative class representative, were to be called to testify as a witness in the class action litigation, while his law firm is employed as counsel to the class. *See Susman, 561 F.2d at 91*. ***HN4***[⬆] DR 5-101 and 5-102 of the ABA Model Code prohibit a law firm from representing a client if a lawyer from the same firm may be called as a witness. *See ABA Model Code of Professional Responsibility,* DR 5-101, 5-102 (1980); *see also ABA Model Rules of Professional Conduct* Rule 3.7 (1984); *Illinois Rules of Professional Conduct* Rule 3.7 (1990). Given the defendants' claims that the other putative class representatives **[*16]** in these cases have scant knowledge of the factual underpinnings of the class claims, we view this as a likelihood, rather than a mere possibility. Even if Scholes attempted to eliminate this conflict by agreeing not to act as a witness, his inability to testify certainly would render him an inadequate representative of the class.

Finally, because Scholes is a partner with MWE, both he and his law firm have a financial stake in the outcome of this litigation as long as MWE continues to represent the class. At a minimum, allowing Scholes to act as a class representative under these circumstances creates the appearance of impropriety. *See ABA Model Code of Professional Responsibility* Canon 9 (1980). Aside from that, a conflict is likely to develop if the account holder class (for whatever reason) wishes to settle this litigation on financial terms less favorable than Scholes and MWE would like. Although Scholes claims that he and the class have a common interest in recovering as much as possible and that MWE has accepted the matter on a fixed, contingent fee basis, these facts do not eliminate the potential for conflict. It is not beyond the realm of possibility (especially given **[*17]** the strained financial status of the majority of the account holders) that the account holders might be willing to accept a more modest settlement offer in order to cut their losses early, while Scholes might want to resist such an offer and hold out for a larger settlement precisely because his law firm stands to receive one-third of the settlement proceeds. Indeed, this Court seriously questions the wisdom of ever allowing an attorney to act as a class representative when his law firm represents the class and both have a

financial stake in the outcome of the litigation. That especially holds true where, as here, the attorney who purports to act as class representative is serving in a fiduciary capacity and his law firm is representing and counseling him in his fiduciary capacity. Under these circumstances, this Court concludes that both standing problems and ethical conflicts warrant disqualification of Scholes as class representative and attorney for the class. [5]

[*18] Scholes' reliance on *Dirks v. Clayton Brokerage Co., 105 F.R.D. 125 (D. Minn. 1985)* to support a contrary conclusion is misplaced. Although Scholes characterizes *Dirks* as "dispositive," we find it inapposite for several reasons. First, *Dirks* may be persuasive authority, but it certainly is not binding on this Court. Furthermore, even the court in *Dirks* acknowledged that a receiver cannot pursue claims belonging to individual investors. *Dirks, 105 F.R.D. at 135*. Finally, *Dirks* is procedurally and factually distinguishable from the cases before us now. In *Dirks,* the only motion before the court was a motion for class certification and the only issue before the court was whether the receiver was an adequate representative of the investor class. In contrast, in this litigation, the motion before us is a motion for disqualification and the issue before us is not just whether the Receiver is a suitable class representative, but also whether ethical conflicts preclude the Receiver, who is a lawyer and whose law firm also represents the class, from acting as a class representative. Contrary to Scholes' representation, there is no **[*19]** evidence suggesting that the Receiver's law firm in *Dirks* also represented the class. Thus, *Dirks* neither involved nor addressed some of the ethical questions presented by this litigation and, for those reasons, we decline to follow it. [6]

C. MWE's Ability to Simultaneously Act as Counsel for Receiver and as Counsel for Class

The defendants contend that MWE's dual representation of the account holder class and Scholes--who is the receiver, a partner at MWE, and a putative class representative--also creates an impermissible conflict for MWE. According to the defendants, the account holders are merely one group of creditors whom Scholes has a duty to protect. Thus, to the extent that the interests of other creditors (including fellow account holders who are not included in the **[*20]** class or who are being sued by the Receiver) may diverge from the interests of the account holder class, and MWE represents some of the account holders (but not others), MWE's representation of the account holder class effectively impairs MWE's ability to impartially advise both the Receiver and the account holder class.

For their part, Scholes and MWE contend that no conflict exists because Scholes and the account holders "have a common interest in recovering monies from defendants." (Memorandum in Opposition at 4). Indeed, Scholes and MWE even go so far as to characterize Scholes' interests and the account holders' interests as "identical." (Surreply at 3). Dismissing defendants' arguments as specious, MWE and Scholes argue that Scholes, as Receiver, has admitted Douglas' liability, does not seek to defend Douglas' conduct and, consequently, neither MWE nor Scholes will have to take a position adverse to that of the account holders and MWE's independent professional judgment will not be compromised by its dual representation of Scholes and the account holder class.

HN5[↑] DR 5-105 of the ABA Model Code, which emanates from Canon 5's directive that "a lawyer should exercise independent **[*21]** judgment," addresses the issue of dual representation. *ABA Model Code of Professional Responsibility,* Canon 5 (1980). DR 5-105 (A) and (B) prohibit dual representation of clients "if the exercise of [an attorney's] independent professional judgment in behalf of a client will be or is likely to be adversely affected by his representation of another client, or if it would be likely to involve him in representing differing interests . . . ." *ABA Model Code of Professional Responsibility* DR 5-105(A), (B) (1980). DR 5-105(C) creates an exception to these rules where "it is obvious that [an attorney] can adequately represent the interest of each [client] and if each consents to the representation after full disclosure of the possible effect of such representation on the exercise of his independent professional judgment on behalf of each." *ABA Model Code of Professional Responsibility* Dr 5-105(C)(1980). *See also ABA Model Code of Professional Conduct* Rule 1.7 (1984); *Illinois Rules of Professional Conduct* Rule 1.7 (1990)(adopting *ABA*

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[5] The defendants also argue that the other account holders named as putative class representatives (the DeJongs in the *Tomlinson* litigation and the LaVinkas in the *Moore* and *Stone, McGuire & Benjamin* litigation) cannot adequately represent the class. This issue is more properly raised in response to a motion for class certification; therefore, we decline to address it now.

[6] The remaining authorities cited by Scholes, which stand for the proposition that no wrongdoing is imputed to a receiver (or other fiduciary), while correct, add nothing to the Court's analysis of the ethical conflicts posed here.

Model Rules of Professional Conduct Rule 1.7 with minor modification). [7] These disciplinary rules "are mandatory in character and represent **[*22]** the minimum level of conduct below which no lawyer should fall." *Ransburg, 648 F.Supp. at 1045*.

Applying these rules to this litigation, the Court concludes that the conflict presented by MWE's dual representation of Scholes and the account holder class not only is obvious, but also is not subject to waiver by consent under the peculiar circumstances of this litigation. [8] That Receiver and the account holder class may share a common interest in recovering money does not eliminate the ethical problems posed by MWE's dual representation of the Receiver and the account holder class. MWE's and Scholes' argument to the contrary overlooks the fact that the Receiver's duty extends to all creditors of the receivership entities and, that as Receiver, Scholes undoubtedly will play some role in the SEC's plan of distribution. At the very **[*23]** least, the SEC would solicit Scholes' advice and input; to suggest otherwise, as Scholes does, is naive. MWE's dual representation of the account holder class and Scholes, as well as Scholes' representation of the class while suing some members of the class, creates the unseemly appearance of partiality toward some of the creditors of the receivership entities. Indeed, if Scholes were confronted with a dilemma which required weighing the interests of the account holders against other creditors of the receivership entities and he sought the advice of MWE, MWE could not exercise independent judgment on behalf of both Scholes and the account holder class. These circumstances create a likelihood that both the independent professional judgment of MWE, as counsel for the Receiver, and of Scholes, as Receiver, may be adversely affected if they continue to simultaneously represent the account holder class. It is of utmost importance that both Scholes and MWE make decisions with freedom from any influences which might cause them, consciously or unconsciously, to be partial. We therefore disqualify Scholes and MWE from representing the account holder class.

[*24] Scholes' and MWE's argument that their disqualification will result in undue injury to both the receivership estates and the account holder class is without merit. We note that the plaintiff account holders have three options: they may retain counsel to substitute for MWE and continue pursuing this lawsuit as a class action; they may pursue their claims individually; or, to the extent that their claims overlap with those asserted in other pending class actions, they may join in those actions. *See, e.g., Marchuk v. Schroeder, et al.,* No. 90 C 6509 (N.D.Ill. 1990)(Zagel, J.). In light of these alternatives, Scholes' and MWE's claims of irreparable harm here ring hollow. In spite of their protests to the contrary, MWE must be disqualified from representing the account holder class and Scholes must be disqualified from acting as putative class representative or ***attorney*** for the class.

D. Removal of ***Receiver*** and Disqualification of MWE as ***Receiver***'s ***Counsel***

The defendants also urge the Court to remove Scholes as ***Receiver*** and to ***disqualify*** MWE from continuing to represent Scholes. In support of their request for this drastic relief, the defendants raise two arguments, each of **[*25]** which are equally unavailing. First, the defendants point out that by filing suit against certain account holders and creditors of the receivership entities based on their alleged collusion with Douglas, Scholes already has begun to discriminate against some account holders and creditors in favor of others. According to the defendants, this "discriminatory" treatment demonstrates that the Receiver cannot exercise impartial and independent judgment vis-a-vis all creditors of the receivership estates, warranting removal of the Receiver. We disagree.

Realistically, any receiver appointed by the Court, whether Scholes or someone else, would be obligated to file suit against any individuals implicated in Douglas' wrongdoing. That holds true whether the alleged wrongdoer or collaborator is an account holder, a creditor, or anyone else. The Receiver is not required to turn a blind eye to allegations of wrongdoing and to treat all account holders or creditors on an equal footing when confronted with evidence suggesting that some of those individuals aided and abetted Douglas in his scheme; indeed, if the Receiver ignored such evidence, he would be remiss in his obligations. Thus, to the extent **[*26]** that the Receiver has filed suit against alleged wrongdoers, he has merely fulfilled the obligations of his appointment and this causes the Court no concern. As explained previously, however, what causes the Court concern and creates a conflict is that the Receiver is not only discriminating among some of

[7] We note that the same results would obtain under these rules as well. Thus, the dispute as to whether federal or state law controls is really a non-issue in this case.

[8] Because Scholes is both a client of MWE (in his capacity as Receiver) and a partner at MWE, he could not objectively or meaningfully waive the conflict.

the account holders by suing them, but at the same time, is representing other account holders in a class action. Though we conclude that this situation creates a conflict, by disqualifying Scholes as attorney for the class and putative class representative and disqualifying MWE as counsel for the class, even the unconscious temptation to act partially toward certain account holders because of conflicting duties is removed. [9]

[*27] Nevertheless, the defendants also argue that if Scholes remains as Receiver and MWE continues to act as Scholes' counsel, then the interests of both will be adverse to the interests of their former clients, namely, the account holders. Although the defendants' arguments might have a certain surface appeal if the traditional concerns of adversity or antagonism between differing interests were present, that is simply not the case here because of the unique nature of receivership litigation. Scholes has neither attempted to exonerate nor to defend Douglas' actions. On the contrary, Scholes has admitted Douglas' wrongdoing. Notably, the defendants have identified no actual adversity that will befall the account holders, and under these particular circumstances, we can foresee none. The record does not suggest that the relationships created by MWE's representation of the Receiver and the account holder class have detrimentally affected either MWE's ability to advise the Receiver or the Receiver's ability to continue to faithfully execute his duties. Nor does the record suggest that Scholes and MWE have gained additional weapons in their arsenal as a result of those relationships. Even **[*28]** the defendants claim that the other putative class representatives (who are account holders) have scant knowledge of the factual underpinnings of this litigation. The Receiver undoubtedly was privy to any information regarding these (and other) defendants' alleged wrongdoing before these cases were ever filed. Moreover, even if the account holder class had been represented by other counsel at the outset, such counsel undoubtedly would have alerted the Receiver to alleged wrongdoing.

In any event, as previously explained, our concern with Scholes serving as putative class representative and MWE representing both Scholes and the account holder class stemmed not from our perception of actual adversity between Scholes' interests and the account holders' interests, but from our perception that the conflicting duties of Scholes, as Receiver, and MWE, as his counsel, could impair their independent judgment. Disqualifying Scholes as putative class representative and as attorney for the account holder class and disqualifying MWE as counsel for the class has eliminated the ethical conflicts otherwise presented. Thus, we believe that allowing Scholes to continue to act as Receiver and allowing **[*29]** MWE to remain as his counsel does not run afoul of ethical rules. The defendants' naked allegations of adversity are not sufficient to persuade us otherwise.

Finally and most importantly, the benefits of allowing Scholes to continue to act as Receiver and MWE to remain as counsel for Scholes appreciably outweigh any benefits to be obtained from removing Scholes as Receiver and disqualifying MWE from continuing to represent him. At this juncture, both Scholes and MWE are intimately familiar with the details of the underlying SEC action and all of the related litigation, have invested a substantial amount of time and effort in marshalling the assets of the receivership entities, and have done so very capably. We do not believe that their brief involvement in this litigation has in any way tainted or otherwise adversely affected their ability to continue to act in their respective capacities. On the other hand, to entirely remove Scholes and MWE from this litigation at this stage of the proceedings would wreak havoc. To appoint a new receiver and new counsel in the underlying SEC action and all related litigation would effectively grind all proceedings to a halt and further delay collection **[*30]** and distribution of the assets recovered. The professional fees and costs already incurred will reduce the assets available for distribution to the account holders and other creditors by a sizeable sum. Appointing a new receiver and new counsel who undoubtedly would have to familiarize themselves with all of this litigation would only cause professional costs to escalate and further dissipate the assets available for distribution. This, in turn, would impose tremendous financial and emotional hardship upon the account holders, many of whom have been financially ruined by Douglas' scam and, at this point, do not enjoy the luxury of time. The account holders have suffered enough and the Court declines to pour salt into their already festering wounds. For these reasons, the Court declines to remove Scholes as Receiver or to disqualify MWE

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[9] Contrary to certain defendants' claims, allowing Scholes to continue to serve as Receiver will not run afoul of Rule 1.10 of the Illinois Rules because Scholes in his capacity as Receiver will be representing only the receivership entities, not the account holders. *See* Ill. Rev. Stat. ch. 110A, RPC 1.10 (1990). The same result obtains under DR 5-105(D) of the ABA Model Code and DR 1.10 of the ABA Model Rules. *See ABA Model Code of Professional Responsibility* DR 5-105(D)(1980); *ABA Model Rules of Professional Conduct* Rule 1.10 (1984).

from continuing to represent Scholes.

E. Fee Forfeiture

We likewise decline to order MWE to forfeit whatever fees it has earned as a result of this litigation. In urging the Court to grant such relief, the defendants merely state that the account holders should not have to pay twice for legal services which will not benefit the receivership estates. **[*31]** Yet, the defendants cite no authority supporting this draconian request. Indeed, in *Lowder v. All Star Mills, Inc., 309 S.E.2d 193, 202-03 (N.C. 1983)*, the only case cited by the defendants, the court soundly rejected the idea of a fee forfeiture. For obvious reasons, so do we. While Scholes and MWE may have committed an error of judgment, that does not reduce the value of the services performed by them nor does it render their services unbeneficial. Similarly, our decision to disqualify Scholes from acting as attorney and putative class representative and to disqualify MWE from representing the account holder class should not be construed as imputing any personal or professional wrongdoing to Scholes or to MWE. Both have performed capably, and the Court is confident that both will continue to perform capably absent the conflicts posed by their dual representation.

IV Conclusion

For the reasons outlined, the defendants' motions for disqualification are granted in part and denied in part. The motions are granted to the extent that the Court disqualifies Steven S. Scholes from acting as attorney and putative class representative for the account holders and disqualifies **[*32]** McDermott, Will & Emery from representing the account holder class. The motions are denied to the extent that the defendants seek to remove Scholes as Receiver, to disqualify McDermott, Will & Emery from continuing to represent Scholes as Receiver, and to require McDermott, Will & Emery to forfeit whatever fees it has earned in pursuing this litigation.

End of Document

West's Nevada Revised Statutes Annotated
Title 57. Insurance (Chapters 679a-697)
Chapter 695I. Silver State Health Insurance Exchange
Organization; Powers and Duties

N.R.S. 695I.200

695I.200. Creation; purpose

Effective: July 1, 2011

Currentness

The Silver State Health Insurance Exchange is hereby established to:

1. Facilitate the purchase and sale of qualified health plans in the individual market in Nevada;

2. Assist qualified small employers in Nevada in facilitating the enrollment and purchase of coverage and the application for subsidies for small business enrollees;

3. Reduce the number of uninsured persons in Nevada;

4. Provide a transparent marketplace for health insurance and consumer education on matters relating to health insurance; and

5. Assist residents of Nevada with access to programs, premium assistance tax credits and cost-sharing reductions.

Credits

Added by Laws 2011, c. 439, § 13, eff. July 1, 2011.

Notes of Decisions (1)

695I.200. Creation; purpose, NV ST 695I.200

N. R. S. 695I.200, NV ST 695I.200
Current through legislation of the 81st Regular Session (2021) effective as of May 26, 2021. Some sections effective July 1, 2021 are also available; see effective date in individual sections. Text subject to revision and classification by the Legislative Counsel Bureau

End of Document

West’s Nevada Revised Statutes Annotated
Title 57. Insurance (Chapters 679a-697)
Chapter 696B. Delinquent Insurers: Conservation, Rehabilitation and Liquidation

N.R.S. 696B.060

696B.060. “Delinquency proceeding” defined

Currentness

“Delinquency proceeding” means:

1. Any proceeding commenced against an insurer pursuant to this chapter for the purpose of conserving, rehabilitating, reorganizing or liquidating the insurer; or

2. The summary proceedings authorized by NRS 696B.500 to 696B.565, inclusive.

Credits

Added by Laws 1971, p. 1884.

N. R. S. 696B.060, NV ST 696B.060
Current through legislation of the 81st Regular Session (2021) effective as of May 26, 2021. Some sections effective July 1, 2021 are also available; see effective date in individual sections. Text subject to revision and classification by the Legislative Counsel Bureau

End of Document

West's Nevada Revised Statutes Annotated
Title 57. Insurance (Chapters 679a-697)
Chapter 696B. Delinquent Insurers: Conservation, Rehabilitation and Liquidation

N.R.S. 696B.190

696B.190. Jurisdiction of delinquency proceedings; venue; exclusiveness of remedy; appeal

Effective: January 1, 2015

Currentness

1. The district court has original jurisdiction of delinquency proceedings under NRS 696B.010 to 696B.565, inclusive, and any court with jurisdiction may make all necessary or proper orders to carry out the purposes of those sections.

2. The venue of delinquency proceedings against a domestic insurer must be in the county in this state of the insurer's principal place of business or, if the principal place of business is located in another state, in any county in this state selected by the Commissioner for the purpose. The venue of proceedings against foreign insurers must be in any county in this state selected by the Commissioner for the purpose.

3. At any time after commencement of a proceeding, the Commissioner or any other party may apply to the court for an order changing the venue of, and removing, the proceeding to any other county of this state in which the proceeding may most conveniently, economically and efficiently be conducted.

4. No court has jurisdiction to entertain, hear or determine any petition or complaint praying for the dissolution, liquidation, rehabilitation, sequestration, conservation or receivership of any insurer, or for an injunction or restraining order or other relief preliminary, incidental or relating to such proceedings, other than in accordance with NRS 696B.010 to 696B.565, inclusive.

5. An appeal to the appellate court of competent jurisdiction pursuant to the rules fixed by the Supreme Court pursuant to Section 4 of Article 6 of the Nevada Constitution may be taken from any court granting or refusing rehabilitation, liquidation, conservation or receivership, and from every order in delinquency proceedings having the character of a final order as to the particular portion of the proceedings embraced therein.

Credits

Added by Laws 1971, p. 1886. Amended by Laws 1995, p. 1635; Laws 1997, c. 603, § 31; Laws 2013, c. 343, § 191, eff. Jan. 1, 2015.

N. R. S. 696B.190, NV ST 696B.190
Current through legislation of the 81st Regular Session (2021) effective as of May 26, 2021. Some sections effective July 1, 2021 are also available; see effective date in individual sections. Text subject to revision and classification by the Legislative Counsel Bureau

End of Document

West's Nevada Revised Statutes Annotated
Title 57. Insurance (Chapters 679a-697)
Chapter 696B. Delinquent Insurers: Conservation, Rehabilitation and Liquidation

N.R.S. 696B.255

696B.255. Commissioner as receiver, rehabilitator or liquidator authorized to appoint special deputies and advisory committee

Currentness

1. The Commissioner, as receiver, rehabilitator or liquidator, may appoint one or more special deputies who have all the powers and responsibilities of a receiver, rehabilitator or liquidator, and the Commissioner may employ such counsels, clerks and assistants as the Commissioner considers necessary. The compensation of such special deputies, counsels, clerks and assistants and all expenses of taking possession of the insurer and of conducting the proceedings must be fixed by the Commissioner with the approval of the court, and paid out of the money or other assets of the insurer. The persons appointed pursuant to this section serve at the pleasure of the Commissioner. The Commissioner, as receiver, rehabilitator or liquidator, may, with the approval of the court, appoint an advisory committee of policyholders, claimants or other creditors, including guaranty associations, if the Commissioner considers such a committee necessary. The committee serves at the pleasure of the Commissioner and serves without compensation other than reimbursement for reasonable travel and other expenses. No other committee of any nature may be appointed by the Commissioner or the court in proceedings for receivership, rehabilitation or liquidation conducted pursuant to this chapter.

2. If the property of the insurer does not contain sufficient cash or liquid assets to defray the costs incurred, the Commissioner may advance the costs so incurred out of any appropriation for the maintenance of the Division. Any amounts so advanced for expenses of administration must be repaid to the Commissioner out of the first available money of the insurer.

Credits

Added by Laws 1995, p. 1634.

N. R. S. 696B.255, NV ST 696B.255
Current through legislation of the 81st Regular Session (2021) effective as of May 26, 2021. Some sections effective July 1, 2021 are also available; see effective date in individual sections. Text subject to revision and classification by the Legislative Counsel Bureau

End of Document

West's Nevada Revised Statutes Annotated
Title 57. Insurance (Chapters 679a-697)
Chapter 696B. Delinquent Insurers: Conservation, Rehabilitation and Liquidation

N.R.S. 696B.270

696B.270. Injunctions

Currentness

1. Upon application by the Commissioner for such an order to show cause, or at any time thereafter, the court may without notice issue an injunction restraining the insurer, its officers, directors, stockholders, members, subscribers, agents and all other persons from the transaction of its business or the waste or disposition of its property until the further order of the court, but the court shall so frame its injunction as not to prevent the Nevada Life and Health Insurance Guaranty Association and the Nevada Insurance Guaranty Association from exercising their respective powers under this title.

2. The court may at any time during a proceeding under NRS 696B.010 to 696B.565, inclusive, issue such other injunctions or orders as may be deemed necessary to prevent interference with the Commissioner or the proceeding, or waste of the assets of the insurer, or the commencement or prosecution of any actions, or the obtaining of preferences, judgments, attachments or other liens, or the making of any levy against the insurer or against its assets or any part thereof.

3. No bond may be required of the Commissioner as a prerequisite for the issuance of any injunction or restraining order pursuant to this section.

Credits

Added by Laws 1971, p. 1890. Amended by Laws 1991, p. 883.

Notes of Decisions (1)

N. R. S. 696B.270, NV ST 696B.270
Current through legislation of the 81st Regular Session (2021) effective as of May 26, 2021. Some sections effective July 1, 2021 are also available; see effective date in individual sections. Text subject to revision and classification by the Legislative Counsel Bureau

West's Nevada Revised Statutes Annotated
Title 57. Insurance (Chapters 679a-697)
Chapter 696B. Delinquent Insurers: Conservation, Rehabilitation and Liquidation

N.R.S. 696B.420

696B.420. Order of distribution of claims from estate of insurer on liquidation

Currentness

1. The order of distribution of claims from the estate of the insurer on liquidation of the insurer must be as set forth in this section. Each claim in each class must be paid in full or adequate money retained for the payment before the members of the next class receive any payment. No subclasses may be established within any class. Except as otherwise provided in subsection 2, the order of distribution and of priority must be as follows:

(a) Administration costs and expenses, including, but not limited to, the following:

(1) The actual and necessary costs of preserving or recovering the assets of the insurer;

(2) Compensation for any services rendered in the liquidation;

(3) Any necessary filing fees;

(4) The fees and mileage payable to witnesses; and

(5) Reasonable attorney's fees.

(b) All claims under policies, any claims against an insured for liability for bodily injury or for injury to or destruction of tangible property which are covered claims under policies, including any such claims of the Federal Government or any state or local government, and any claims of the Nevada Insurance Guaranty Association, the Nevada Life and Health Insurance Guaranty Association and other similar statutory

organizations in other jurisdictions. Any claims under life insurance and annuity policies, whether for death proceeds, annuity proceeds or investment values, must be treated as loss claims. That portion of any loss for which indemnification is provided by other benefits or advantages recovered or recoverable by the claimant may not be included in this class, other than benefits or advantages recovered or recoverable in discharge of familial obligations of support or because of succession at death or as proceeds of life insurance, or as gratuities. No payment made by an employer to an employee of the employer may be treated as a gratuity.

(c) Unearned premiums and small loss claims, including claims under nonassessable policies for unearned premiums or other premium refunds.

(d) Except as otherwise provided in paragraph (b), claims of the Federal Government.

(e) Except as otherwise provided in paragraph (b), claims of any state or local government, including, but not limited to, a claim of a state or local government for a penalty or forfeiture.

(f) Wage debts due employees for services performed, not to exceed an amount equal to 2 months of monetary compensation for each employee for services performed within 6 months before the filing of the petition for liquidation or, if rehabilitation preceded liquidation, within 1 year before the filing of the petition for rehabilitation. Officers of the insurer are not entitled to the benefit of this priority. The priority set forth in this paragraph must be in lieu of any other similar priority authorized by law as to wages or compensation of employees.

(g) Residual classification, including any other claims not falling within other classes pursuant to the provisions of this section. Claims for a penalty or forfeiture must be allowed in this class only to the extent of the pecuniary loss sustained from the act, transaction or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby. The remainder of the claims must be postponed to the class of claims specified in paragraph (j).

(h) Judgment claims based solely on judgments. If a claimant files a claim and bases the claim on the judgment and on the underlying facts, the claim must be considered by the liquidator, who shall give the judgment such weight as the liquidator deems appropriate. The claim as allowed must receive the priority it would receive in the absence of the judgment. If the judgment is larger than the allowance on the underlying claim, the remaining portion of the judgment must be treated as if it were a claim based solely on a judgment.

(i) Interest on claims already paid, which must be calculated at the legal rate compounded annually on any claims in the classes specified in paragraphs (a) to (h), inclusive, from the date of the petition for liquidation or the date on which the claim becomes due, whichever is later, until the date on which the dividend is declared. The liquidator, with the approval of the court, may:

(1) Make reasonable classifications of claims for purposes of computing interest;

(2) Make approximate computations; and

(3) Ignore certain classifications and periods as de minimis.

(j) Miscellaneous subordinated claims, with interest as provided in paragraph (i):

(1) Claims subordinated by NRS 696B.430;

(2) Claims filed late;

(3) Portions of claims subordinated pursuant to the provisions of paragraph (g);

(4) Claims or portions of claims the payment of which is provided by other benefits or advantages recovered or recoverable by the claimant; and

(5) Claims not otherwise provided for in this section.

(k) Preferred ownership claims, including surplus or contribution notes, or similar obligations, and premium refunds on assessable policies. Interest at the legal rate must be added to each claim, as provided in paragraphs (i) and (j).

(l) Proprietary claims of shareholders or other owners.

2. If there are no existing or potential claims of the government against the estate, claims for wages have priority over any claims set forth in paragraphs (c) to (k), inclusive, of subsection 1. The provisions of this

subsection must not be construed to require the accumulation of interest for claims as described in paragraph (i) of subsection 1.

Credits

Added by Laws 1971, p. 1897. Amended by Laws 1977, p. 440; Laws 1997, c. 603, § 33; Laws 1999, c. 487, § 4; Laws 2003, c. 495, § 82.

N. R. S. 696B.420, NV ST 696B.420
Current through legislation of the 81st Regular Session (2021) effective as of May 26, 2021. Some sections effective July 1, 2021 are also available; see effective date in individual sections. Text subject to revision and classification by the Legislative Counsel Bureau

End of Document

United States Code Annotated
Title 11. Bankruptcy (Refs & Annos)
Chapter 1. General Provisions (Refs & Annos)

11 U.S.C.A. § 109

§ 109. Who may be a debtor

Effective: December 22, 2010

Currentness

(a) Notwithstanding any other provision of this section, only a person that resides or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title.

(b) A person may be a debtor under chapter 7 of this title only if such person is not--

(1) a railroad;

(2) a domestic insurance company, bank, savings bank, cooperative bank, savings and loan association, building and loan association, homestead association, a New Markets Venture Capital company as defined in section 351 of the Small Business Investment Act of 1958, a small business investment company licensed by the Small Business Administration under section 301 of the Small Business Investment Act of 1958, credit union, or industrial bank or similar institution which is an insured bank as defined in section 3(h) of the Federal Deposit Insurance Act, except that an uninsured State member bank, or a corporation organized under section 25A of the Federal Reserve Act, which operates, or operates as, a multilateral clearing organization pursuant to section 409[1] of the Federal Deposit Insurance Corporation Improvement Act of 1991 may be a debtor if a petition is filed at the direction of the Board of Governors of the Federal Reserve System; or

(3)(A) a foreign insurance company, engaged in such business in the United States; or

(B) a foreign bank, savings bank, cooperative bank, savings and loan association, building and loan association, or credit union, that has a branch or agency (as defined in section 1(b) of the International Banking Act of 1978) in the United States.

(c) An entity may be a debtor under chapter 9 of this title if and only if such entity--

(1) is a municipality;

(2) is specifically authorized, in its capacity as a municipality or by name, to be a debtor under such chapter by State law, or by a governmental officer or organization empowered by State law to authorize such entity to be a debtor under such chapter;

(3) is insolvent;

(4) desires to effect a plan to adjust such debts; and

(5)(A) has obtained the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;

(B) has negotiated in good faith with creditors and has failed to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;

(C) is unable to negotiate with creditors because such negotiation is impracticable; or

(D) reasonably believes that a creditor may attempt to obtain a transfer that is avoidable under section 547 of this title.

(d) Only a railroad, a person that may be a debtor under chapter 7 of this title (except a stockbroker or a commodity broker), and an uninsured State member bank, or a corporation organized under section 25A of the Federal Reserve Act, which operates, or operates as, a multilateral clearing organization pursuant to section 409[1] of the Federal Deposit Insurance Corporation Improvement Act of 1991 may be a debtor under chapter 11 of this title.

(e) Only an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than $419,275 [originally "$250,000", adjusted effective April, 1, 2019][2] and noncontingent, liquidated, secured debts of less than $1,257,850 [originally "$750,000", adjusted effective April 1, 2019][2], or an individual with regular income and such individual's spouse, except a stockbroker or a commodity broker, that owe, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts that aggregate less than $419,275 [originally "$250,000", adjusted effective April, 1, 2019][2] and noncontingent, liquidated, secured debts of less than $1,257,850 [originally "$750,000", adjusted effective April 1, 2019][2] may be a debtor under chapter 13 of this title.

(f) Only a family farmer or family fisherman with regular annual income may be a debtor under chapter 12 of this title.

(g) Notwithstanding any other provision of this section, no individual or family farmer may be a debtor under this title who has been a debtor in a case pending under this title at any time in the preceding 180 days if--

(1) the case was dismissed by the court for willful failure of the debtor to abide by orders of the court, or to appear before the court in proper prosecution of the case; or

(2) the debtor requested and obtained the voluntary dismissal of the case following the filing of a request for relief from the automatic stay provided by section 362 of this title.

(h)(1) Subject to paragraphs (2) and (3), and notwithstanding any other provision of this section other than paragraph (4) of this subsection, an individual may not be a debtor under this title unless such individual has, during the 180-day period ending on the date of filing of the petition by such individual, received from an approved nonprofit budget and credit counseling agency described in section 111(a) an individual or group briefing (including a briefing conducted by telephone or on the Internet) that outlined the opportunities for available credit counseling and assisted such individual in performing a related budget analysis.

(2)(A) Paragraph (1) shall not apply with respect to a debtor who resides in a district for which the United States trustee (or the bankruptcy administrator, if any) determines that the approved nonprofit budget and credit counseling agencies for such district are not reasonably able to provide adequate services to the additional individuals who would otherwise seek credit counseling from such agencies by reason of the requirements of paragraph (1).

(B) The United States trustee (or the bankruptcy administrator, if any) who makes a determination described in subparagraph (A) shall review such determination not later than 1 year after the date of such determination, and not less frequently than annually thereafter. Notwithstanding the preceding sentence, a nonprofit budget and credit counseling agency may be disapproved by the United States trustee (or the bankruptcy administrator, if any) at any time.

(3)(A) Subject to subparagraph (B), the requirements of paragraph (1) shall not apply with respect to a debtor who submits to the court a certification that--

(i) describes exigent circumstances that merit a waiver of the requirements of paragraph (1);

(ii) states that the debtor requested credit counseling services from an approved nonprofit budget and credit counseling agency, but was unable to obtain the services referred to in paragraph (1) during the 7-day period beginning on the date on which the debtor made that request; and

(iii) is satisfactory to the court.

(B) With respect to a debtor, an exemption under subparagraph (A) shall cease to apply to that debtor on the date on which the debtor meets the requirements of paragraph (1), but in no case may the exemption apply to that debtor after the date that is 30 days after the debtor files a petition, except that the court, for cause, may order an additional 15 days.

(4) The requirements of paragraph (1) shall not apply with respect to a debtor whom the court determines, after notice and hearing, is unable to complete those requirements because of incapacity, disability, or active military duty in a military combat zone. For the purposes of this paragraph, incapacity means that the debtor is impaired by reason of mental illness or mental deficiency so that he is incapable of realizing and making rational decisions with respect to his financial responsibilities; and "disability" means that the debtor is so physically impaired as to be unable, after reasonable effort, to participate in an in person, telephone, or Internet briefing required under paragraph (1).

CREDIT(S)

(Pub.L. 95-598, Nov. 6, 1978, 92 Stat. 2557; Pub.L. 97-320, Title VII, § 703(d), Oct. 15, 1982, 96 Stat. 1539; Pub.L. 98-353, Title III, §§ 301, 425, July 10, 1984, 98 Stat. 352, 369; Pub.L. 99-554, Title II, § 253, Oct. 27, 1986, 100 Stat. 3105; Pub.L. 100-597, § 2, Nov. 3, 1988, 102 Stat. 3028; Pub.L. 103-394, Title I, § 108(a), Title II, § 220, Title IV, § 402, Title V, § 501(d)(2), Oct. 22, 1994, 108 Stat. 4111, 4129, 4141, 4143; Pub.L.

106-554, § 1(a)(5) [Title I, § 112(c)(1), (2)], (8) [§ 1(e)], Dec. 21, 2000, 114 Stat. 2763, 2763A-393, 2763A-665; Pub.L. 109-8, Title I, § 106(a), Title VIII, § 802(d)(1), Title X, § 1007(b), Title XII, § 1204(1), Apr. 20, 2005, 119 Stat. 37, 146, 188, 193; Pub.L. 111-16, § 2(1), May 7, 2009, 123 Stat. 1607; Pub.L. 111-327, § 2(a)(6), Dec. 22, 2010, 124 Stat. 3557.)

ADJUSTMENT OF DOLLAR AMOUNTS

<For adjustment of dollar amounts specified in subsec. (e) of this section by the Judicial Conference of the United States, effective Apr. 1, 2019, see note set out under 11 U.S.C.A. § 104.>

<By notice published Feb. 12, 2019, 84 F.R. 3488, the Judicial Conference of the United States adjusted the dollar amounts in provisions specified in subsec. (e) of this section, effective Apr. 1, 2019, as follows:>

<Adjusted $394,725 (each time it appears) to $419,275 (each time it appears).>

<Adjusted $1,184,200 (each time it appears) to $1,257,850 (each time it appears).>

<By notice published Feb. 22, 2016, 81 F.R. 8748, the Judicial Conference of the United States adjusted the dollar amounts in provisions specified in subsec. (e) of this section, effective Apr. 1, 2016, as follows:>

<Adjusted $383,175 (each time it appears) to $394,725 (each time it appears).>

<Adjusted $1,149,525 (each time it appears) to $1,184,200 (each time it appears).>

<By notice published Feb. 21, 2013, 78 F.R. 12089, the Judicial Conference of the United States adjusted the dollar amounts in provisions specified in subsec. (e) of this section, effective Apr. 1, 2013, as follows:>

<Adjusted $360,475 (each time it appears) to $383,175 (each time it appears).>

<Adjusted $1,081,400 (each time it appears) to $1,149,525 (each time it appears).>

<By notice published Feb. 25, 2010, 75 F.R. 8747, the Judicial Conference of the United States adjusted the dollar amounts in provisions specified in subsec. (e) of this section, effective Apr. 1, 2010, as follows:>

<Adjusted $336,900 (each time it appears) to $360,475 (each time it appears).>

<Adjusted $1,010,650 (each time it appears) to $1,081,400 (each time it appears).>

<By notice published Feb. 14, 2007, 72 F.R. 7082, the Judicial Conference of the United States adjusted the dollar amounts in provisions specified in subsec. (e) of this section, effective Apr. 1, 2007, as follows:>

<Adjusted $307,675 (each time it appears) to $336,900 (each time it appears).>

<Adjusted $922,975 (each time it appears) to $1,010,650 (each time it appears).>

<By notice dated Feb. 18, 2004, 69 F.R. 8482, the Judicial Conference of the United States adjusted the dollar amounts in provisions specified in subsec. (e) of this section, effective Apr. 1, 2004, as follows:>

<Adjusted $290,525 (each time it appears) to $307,675 (each time it appears).>

<Adjusted $871,550 to $922,975.>

<By notice dated Feb. 20, 2001, 66 F.R. 10910, the Judicial Conference of the United States adjusted the dollar amounts in provisions specified in subsec. (e) of this section, effective Apr. 1, 2001, as follows:>

<Adjusted $269,250 (each time it appears) to $290,525 (each time it appears).>

<Adjusted $807,750 (each time it appears) to $871,550 (each time it appears).>

<By notice dated Feb. 3, 1998, 63 F.R. 7179, the Judicial Conference of the United States adjusted the dollar amounts in provisions specified in subsec. (e) of this section, effective Apr. 1, 1998, as follows:>

<Adjusted $250,000 (each time it appears) to $269,250 (each time it appears).>

<Adjusted $750,000 (each time it appears) to $807,750 (each time it appears).>

Notes of Decisions (819)

Footnotes

1 Repealed. See References in Text note set out for this section.

2 See Adjustment of Dollar Amounts notes set out under this section and 11 U.S.C.A. § 104.

11 U.S.C.A. § 109, 11 USCA § 109
Current through PL 117-15 with the exception of PL 116-283, Div. A, Title XVIII.

United States Code Annotated
Title 42. The Public Health and Welfare
Chapter 157. Quality Affordable Health Care for All Americans
Subchapter I. Immediate Actions to Preserve and Expand Coverage

42 U.S.C.A. § 18001

§ 18001. Immediate access to insurance for uninsured individuals with a preexisting condition

Effective: March 23, 2010

Currentness

<For Executive Order No. 14009, "Strengthening Medicaid and the Affordable Care Act", see Executive Order No. 14009, January 28, 2021, 86 F.R. 7793.>

(a) In general

Not later than 90 days after March 23, 2010, the Secretary shall establish a temporary high risk health insurance pool program to provide health insurance coverage for eligible individuals during the period beginning on the date on which such program is established and ending on January 1, 2014.

(b) Administration

(1) In general

The Secretary may carry out the program under this section directly or through contracts to eligible entities.

(2) Eligible entities

To be eligible for a contract under paragraph (1), an entity shall--

(A) be a State or nonprofit private entity;

(B) submit to the Secretary an application at such time, in such manner, and containing such information as the Secretary may require; and

(C) agree to utilize contract funding to establish and administer a qualified high risk pool for eligible individuals.

(3) Maintenance of effort

To be eligible to enter into a contract with the Secretary under this subsection, a State shall agree not to reduce the annual amount the State expended for the operation of one or more State high risk pools during the year preceding the year in which such contract is entered into.

(c) Qualified high risk pool

(1) In general

Amounts made available under this section shall be used to establish a qualified high risk pool that meets the requirements of paragraph (2).

(2) Requirements

A qualified high risk pool meets the requirements of this paragraph if such pool--

(A) provides to all eligible individuals health insurance coverage that does not impose any preexisting condition exclusion with respect to such coverage;

(B) provides health insurance coverage--

(i) in which the issuer's share of the total allowed costs of benefits provided under such coverage is not less than 65 percent of such costs; and

(ii) that has an out of pocket limit not greater than the applicable amount described in section 223(c)(2) of Title 26 for the year involved, except that the Secretary may modify such limit if necessary to ensure the pool meets the actuarial value limit under clause (i);

(C) ensures that with respect to the premium rate charged for health insurance coverage offered to eligible individuals through the high risk pool, such rate shall--

(i) except as provided in clause (ii), vary only as provided for under section 300gg of this title (as amended by this Act and notwithstanding the date on which such amendments take effect);

(ii) vary on the basis of age by a factor of not greater than 4 to 1; and

(iii) be established at a standard rate for a standard population; and

(D) meets any other requirements determined appropriate by the Secretary.

(d) Eligible individual

An individual shall be deemed to be an eligible individual for purposes of this section if such individual--

(1) is a citizen or national of the United States or is lawfully present in the United States (as determined in accordance with section 18081 of this title);

(2) has not been covered under creditable coverage (as defined in section 300gg(c)(1) of this title as in effect on March 23, 2010) during the 6-month period prior to the date on which such individual is applying for coverage through the high risk pool; and

(3) has a pre-existing condition, as determined in a manner consistent with guidance issued by the Secretary.

(e) Protection against dumping risk by insurers

(1) In general

The Secretary shall establish criteria for determining whether health insurance issuers and employment-based health plans have discouraged an individual from remaining enrolled in prior coverage based on that individual's health status.

(2) Sanctions

An issuer or employment-based health plan shall be responsible for reimbursing the program under this section for the medical expenses incurred by the program for an individual who, based on criteria established by the Secretary, the Secretary finds was encouraged by the issuer to disenroll from health benefits coverage prior to enrolling in coverage through the program. The criteria shall include at least the following circumstances:

(A) In the case of prior coverage obtained through an employer, the provision by the employer, group health plan, or the issuer of money or other financial consideration for disenrolling from the coverage.

(B) In the case of prior coverage obtained directly from an issuer or under an employment-based health plan--

(i) the provision by the issuer or plan of money or other financial consideration for disenrolling from the coverage; or

(ii) in the case of an individual whose premium for the prior coverage exceeded the premium required by the program (adjusted based on the age factors applied to the prior coverage)--

(I) the prior coverage is a policy that is no longer being actively marketed (as defined by the Secretary) by the issuer; or

(II) the prior coverage is a policy for which duration of coverage form[1] issue or health status are factors that can be considered in determining premiums at renewal.

(3) Construction

Nothing in this subsection shall be construed as constituting exclusive remedies for violations of criteria established under paragraph (1) or as preventing States from applying or enforcing such paragraph or other provisions under law with respect to health insurance issuers.

(f) Oversight

The Secretary shall establish--

(1) an appeals process to enable individuals to appeal a determination under this section; and

(2) procedures to protect against waste, fraud, and abuse.

(g) Funding; termination of authority

(1) In general

There is appropriated to the Secretary, out of any moneys in the Treasury not otherwise appropriated, $5,000,000,000 to pay claims against (and the administrative costs of) the high risk pool under this section that are in excess of the amount of premiums collected from eligible individuals enrolled in the high risk pool. Such funds shall be available without fiscal year limitation.

(2) Insufficient funds

If the Secretary estimates for any fiscal year that the aggregate amounts available for the payment of the expenses of the high risk pool will be less than the actual amount of such expenses, the Secretary shall make such adjustments as are necessary to eliminate such deficit.

(3) Termination of authority

(A) In general

Except as provided in subparagraph (B), coverage of eligible individuals under a high risk pool in a State shall terminate on January 1, 2014.

(B) Transition to Exchange

The Secretary shall develop procedures to provide for the transition of eligible individuals enrolled in health insurance coverage offered through a high risk pool established under this section into qualified health plans offered through an Exchange. Such procedures shall ensure that there is no lapse in coverage with respect to the individual and may extend coverage after the termination of the risk pool involved, if the Secretary determines necessary to avoid such a lapse.

(4) Limitations

The Secretary has the authority to stop taking applications for participation in the program under this section to comply with the funding limitation provided for in paragraph (1).

(5) Relation to State laws

The standards established under this section shall supersede any State law or regulation (other than State licensing laws or State laws relating to plan solvency) with respect to qualified high risk pools which are established in accordance with this section.

CREDIT(S)

(Pub.L. 111-148, Title I, § 1101, Mar. 23, 2010, 124 Stat. 141.)

EXECUTIVE ORDERS

EXECUTIVE ORDER NO. 13765

<January 20, 2017, 82 F.R. 8351>

Minimizing the Economic Burden of the Patient Protection and Affordable Care Act Pending Repeal

By the authority vested in me as President by the Constitution and the laws of the United States of America, it is hereby ordered as follows:

Section 1. It is the policy of my Administration to seek the prompt repeal of the Patient Protection and Affordable Care Act (Public Law 111-148), as amended (the "Act"). In the meantime, pending such repeal, it is imperative for the executive branch to ensure that the law is being efficiently implemented, take all actions consistent with law to minimize the unwarranted economic and regulatory burdens of the Act, and prepare to afford the States more flexibility and control to create a more free and open healthcare market.

Sec. 2. To the maximum extent permitted by law, the Secretary of Health and Human Services (Secretary) and the heads of all other executive departments and agencies (agencies) with authorities and responsibilities under the Act shall exercise all authority and discretion available to them to waive, defer, grant exemptions from, or delay the implementation of any provision or requirement of the Act that would impose a fiscal burden on any State or a cost, fee, tax, penalty, or regulatory burden on individuals, families, healthcare providers, health insurers, patients, recipients of healthcare services, purchasers of health insurance, or makers of medical devices, products, or medications.

Sec. 3. To the maximum extent permitted by law, the Secretary and the heads of all other executive departments and agencies with authorities and responsibilities under the Act, shall exercise all authority and discretion available to them to provide greater flexibility to States and cooperate with them in implementing healthcare programs.

Sec. 4. To the maximum extent permitted by law, the head of each department or agency with responsibilities relating to healthcare or health insurance shall encourage the development of a free and open market in interstate commerce for the offering of healthcare services and health insurance, with the goal of achieving and preserving maximum options for patients and consumers.

Sec. 5. To the extent that carrying out the directives in this order would require revision of regulations issued through notice-and-comment rulemaking, the heads of agencies shall comply with the Administrative Procedure Act and other applicable statutes in considering or promulgating such regulatory revisions.

Sec. 6. (a) Nothing in this order shall be construed to impair or otherwise affect:

(i) the authority granted by law to an executive department or agency, or the head thereof; or

(ii) the functions of the Director of the Office of Management and Budget relating to budgetary, administrative, or legislative proposals.

(b) This order shall be implemented consistent with applicable law and subject to the availability of

appropriations.

(c) This order is not intended to, and does not, create any right or benefit, substantive or procedural, enforceable at law or in equity by any party against the United States, its departments, agencies, or entities, its officers, employees, or agents, or any other person.

DONALD J. TRUMP

EXECUTIVE ORDER NO. 13813

<October 12, 2017, 82 F.R. 46385>

Promoting Healthcare Choice and Competition Across the United States

By the authority vested in me as President by the Constitution and the laws of the United States of America, it is hereby ordered as follows:

Section 1. Policy. (a) It shall be the policy of the executive branch, to the extent consistent with law, to facilitate the purchase of insurance across State lines and the development and operation of a healthcare system that provides high-quality care at affordable prices for the American people. The Patient Protection and Affordable Care Act (PPACA), however, has severely limited the choice of healthcare options available to many Americans and has produced large premium increases in many State individual markets for health insurance. The average exchange premium in the 39 States that are using www.healthcare.gov in 2017 is more than double the average overall individual market premium recorded in 2013. The PPACA has also largely failed to provide meaningful choice or competition between insurers, resulting in one-third of America's counties having only one insurer offering coverage on their applicable government-run exchange in 2017.

(b) Among the myriad areas where current regulations limit choice and competition, my Administration will prioritize three areas for improvement in the near term: association health plans (AHPs), short-term, limited-duration insurance (STLDI), and health reimbursement arrangements (HRAs).

(i) Large employers often are able to obtain better terms on health insurance for their employees than small employers because of their larger pools of insurable individuals across which they can spread risk and administrative costs. Expanding access to AHPs can help small businesses overcome this competitive disadvantage by allowing them to group together to self-insure or purchase large group health insurance. Expanding access to AHPs will also allow more small businesses to avoid many of the PPACA's costly requirements. Expanding access to AHPs would provide more affordable health insurance options to many Americans, including hourly wage earners, farmers, and the employees of small businesses and entrepreneurs that fuel economic growth.

(ii) STLDI is exempt from the onerous and expensive insurance mandates and regulations included in title I of the PPACA. This can make it an appealing and affordable alternative to government-run exchanges for many people without coverage available to them through their workplaces. The previous administration took steps to restrict access to this market by reducing the allowable coverage period from less than 12 months to less than 3 months and by preventing any extensions selected by the policyholder beyond 3 months of total coverage.

(iii) HRAs are tax-advantaged, account-based arrangements that employers can establish for employees to give employees more flexibility and choices regarding their healthcare. Expanding the flexibility and use of HRAs would provide many Americans, including employees who work at small businesses, with more options for financing their healthcare.

(c) My Administration will also continue to focus on promoting competition in healthcare markets and limiting excessive consolidation throughout the healthcare system. To the extent consistent with law, government rules and guidelines affecting the United States healthcare system should:

(i) expand the availability of and access to alternatives to expensive, mandate-laden PPACA insurance, including AHPs, STLDI, and HRAs;

(ii) re-inject competition into healthcare markets by lowering barriers to entry, limiting excessive consolidation, and preventing abuses of market power; and

(iii) improve access to and the quality of information that Americans need to make informed healthcare decisions, including data about healthcare prices and outcomes, while minimizing reporting burdens on affected plans, providers, or payers.

Sec. 2. Expanded Access to Association Health Plans. Within 60 days of the date of this order, the Secretary of Labor shall consider proposing regulations or revising guidance, consistent with law, to expand access to health coverage by allowing more employers to form AHPs. To the extent permitted by law and supported by sound policy, the Secretary should consider expanding the conditions that satisfy the commonality-of-interest requirements under current Department of Labor advisory opinions interpreting the definition of an "employer" under section 3(5) of the Employee Retirement Income Security Act of 1974. The Secretary of Labor should also consider ways to promote AHP formation on the basis of common geography or industry.

Sec. 3. Expanded Availability of Short-Term, Limited-Duration Insurance. Within 60 days of the date of this order, the Secretaries of the Treasury, Labor, and Health and Human Services shall consider proposing regulations or revising guidance, consistent with law, to expand the availability of STLDI. To the extent permitted by law and supported by sound policy, the Secretaries should consider allowing such insurance to cover longer periods and be renewed by the consumer.

Sec. 4. Expanded Availability and Permitted Use of Health Reimbursement Arrangements. Within 120 days of the date of this order, the Secretaries of the Treasury, Labor, and Health and Human Services shall consider proposing regulations or revising guidance, to the extent permitted by law and supported by sound

policy, to increase the usability of HRAs, to expand employers" ability to offer HRAs to their employees, and to allow HRAs to be used in conjunction with nongroup coverage.

Sec. 5. Public Comment. The Secretaries shall consider and evaluate public comments on any regulations proposed under sections 2 through 4 of this order.

Sec. 6. Reports. Within 180 days of the date of this order, and every 2 years thereafter, the Secretary of Health and Human Services, in consultation with the Secretaries of the Treasury and Labor and the Federal Trade Commission, shall provide a report to the President that:

(a) details the extent to which existing State and Federal laws, regulations, guidance, requirements, and policies fail to conform to the policies set forth in section 1 of this order; and

(b) identifies actions that States or the Federal Government could take in furtherance of the policies set forth in section 1 of this order.

Sec. 7. General Provisions. (a) Nothing in this order shall be construed to impair or otherwise affect:

(i) the authority granted by law to an executive department or agency, or the head thereof; or

(ii) the functions of the Director of the Office of Management and Budget relating to budgetary, administrative, or legislative proposals.

(b) This order shall be implemented consistent with applicable law and subject to the availability of appropriations.

(c) This order is not intended to, and does not, create any right or benefit, substantive or procedural, enforceable at law or in equity by any party against the United States, its departments, agencies, or entities, its officers, employees, or agents, or any other person.

DONALD J. TRUMP

EXECUTIVE ORDER NO. 13877

<June 24, 2019, 84 F.R. 30849>

Improving Price and Quality Transparency in American Healthcare To Put Patients First

By the authority vested in me as President by the Constitution and the laws of the United States of America, it is hereby ordered as follows:

Section 1. Purpose. My Administration seeks to enhance the ability of patients to choose the healthcare that is best for them. To make fully informed decisions about their healthcare, patients must know the price and quality of a good or service in advance. With the predominant role that third-party payers and Government programs play in the American healthcare system, however, patients often lack both access to useful price and quality information and the incentives to find low-cost, high-quality care. Opaque pricing structures may benefit powerful special interest groups, such as large hospital systems and insurance companies, but they generally leave patients and taxpayers worse off than would a more transparent system.

Pursuant to Executive Order 13813 of October 12, 2017 (Promoting Healthcare Choice and Competition Across the United States), my Administration issued a report entitled "Reforming America's Healthcare System Through Choice and Competition." The report recommends developing price and quality transparency initiatives to ensure that healthcare patients can make well-informed decisions about their care. In particular, the report describes the characteristics of the most effective price transparency efforts: they distinguish between the charges that providers bill and the rates negotiated between payers and providers; they give patients proper incentives to seek information about the price of healthcare services; and they provide useful price comparisons for "shoppable" services (common services offered by multiple providers through the market, which patients can research and compare before making informed choices based on price and quality).

Shoppable services make up a significant share of the healthcare market, which means that increasing transparency among these services will have a broad effect on increasing competition in the healthcare system as a whole. One study, cited by the Council of Economic Advisers in its 2019 Annual Report, examined a sample of the highest-spending categories of medical cases requiring inpatient and outpatient care. Of the categories of medical cases requiring inpatient care, 73 percent of the 100 highest-spending categories were shoppable. Among the categories of medical cases requiring outpatient care, 90 percent of the 300 highest-spending categories were shoppable. Another study demonstrated that the ability of patients to price-shop imaging services, a particularly fungible and shoppable set of healthcare services, was associated with a per-service savings of up to approximately 19 percent.

Improving transparency in healthcare will also further protect patients from harmful practices such as surprise billing, which occurs when patients receive unexpected bills at highly inflated prices from out-of-network providers they had no opportunity to select in advance. On May 9, 2019, I announced principles to guide efforts to address surprise billing. The principles outline how patients scheduling appointments to receive facility-based care should have access to pricing information related to the providers and services they may need, and the out-of-pocket costs they may incur. Having access to this type of information in advance of care can help patients avoid excessive charges.

Making meaningful price and quality information more broadly available to more Americans will protect patients and increase competition, innovation, and value in the healthcare system.

Sec. 2. Policy. It is the policy of the Federal Government to ensure that patients are engaged with their healthcare decisions and have the information requisite for choosing the healthcare they want and need. The Federal Government aims to eliminate unnecessary barriers to price and quality transparency; to increase the availability of meaningful price and quality information for patients; to enhance patients' control over their own healthcare resources, including through tax-preferred medical accounts; and to protect patients from surprise medical bills.

Sec. 3. Informing Patients About Actual Prices. (a) Within 60 days of the date of this order, the Secretary of Health and Human Services shall propose a regulation, consistent with applicable law, to require hospitals to publicly post standard charge information, including charges and information based on negotiated rates and for common or shoppable items and services, in an easy-to-understand, consumer-friendly, and machine-readable format using consensus-based data standards that will meaningfully inform patients' decision making and allow patients to compare prices across hospitals. The regulation should require the posting of standard charge information for services, supplies, or fees billed by the hospital or provided by employees of the hospital. The regulation should also require hospitals to regularly update the posted information and establish a monitoring mechanism for the Secretary to ensure compliance with the posting requirement, as needed.

(b) Within 90 days of the date of this order, the Secretaries of Health and Human Services, the Treasury, and Labor shall issue an advance notice of proposed rulemaking, consistent with applicable law, soliciting comment on a proposal to require healthcare providers, health insurance issuers, and self-insured group health plans to provide or facilitate access to information about expected out-of-pocket costs for items or services to patients before they receive care.

(c) Within 180 days of the date of this order, the Secretary of Health and Human Services, in consultation with the Attorney General and the Federal Trade Commission, shall issue a report describing the manners in which the Federal Government or the private sector are impeding healthcare price and quality transparency for patients, and providing recommendations for eliminating these impediments in a way that promotes competition. The report should describe why, under current conditions, lower-cost providers generally avoid healthcare advertising.

Sec. 4. Establishing a Health Quality Roadmap. Within 180 days of the date of this order, the Secretaries of Health and Human Services, Defense, and Veterans Affairs shall develop a Health Quality Roadmap (Roadmap) that aims to align and improve reporting on data and quality measures across Medicare, Medicaid, the Children's Health Insurance Program, the Health Insurance Marketplace, the Military Health System, and the Veterans Affairs Health System. The Roadmap shall include a strategy for establishing, adopting, and publishing common quality measurements; aligning inpatient and outpatient measures; and eliminating low-value or counterproductive measures.

Sec. 5. Increasing Access to Data to Make Healthcare Information More Transparent and Useful to Patients. Within 180 days of the date of this order, the Secretary of Health and Human Services, in consultation with the Secretaries of the Treasury, Defense, Labor, and Veterans Affairs, and the Director of the Office of Personnel Management, shall increase access to de-identified claims data from taxpayer-funded healthcare programs and group health plans for researchers, innovators, providers, and entrepreneurs, in a manner that is consistent with applicable law and that ensures patient privacy and security. Providing access to this data will facilitate the development of tools that empower patients to be better informed as they make decisions related to healthcare goods and services. Access to this data will also enable researchers and entrepreneurs to locate

inefficiencies and opportunities for improvement, such as patterns of performance of medical procedures that are outside the recommended standards of care. Such data may be derived from the Transformed Medicaid Statistical Information System (T-MSIS) and other sources. As part of this process, the Secretary of Health and Human Services shall make a list of priority datasets that, if de-identified, could advance the policies set forth by this order, and shall report to the President on proposed plans for future release of these priority datasets and on any barriers to their release.

Sec. 6. Empowering Patients by Enhancing Control Over Their Healthcare Resources. (a) Within 120 days of the date of this order, the Secretary of the Treasury, to the extent consistent with law, shall issue guidance to expand the ability of patients to select high-deductible health plans that can be used alongside a health savings account, and that cover low-cost preventive care, before the deductible, for medical care that helps maintain health status for individuals with chronic conditions.

(b) Within 180 days of the date of this order, the Secretary of the Treasury, to the extent consistent with law, shall propose regulations to treat expenses related to certain types of arrangements, potentially including direct primary care arrangements and healthcare sharing ministries, as eligible medical expenses under section 213(d) of title 26, United States Code.

(c) Within 180 days of the date of this order, the Secretary of the Treasury, to the extent consistent with law, shall issue guidance to increase the amount of funds that can carry over without penalty at the end of the year for flexible spending arrangements.

Sec. 7. Addressing Surprise Medical Billing. Within 180 days of the date of this order, the Secretary of Health and Human Services shall submit a report to the President on additional steps my Administration may take to implement the principles on surprise medical billing announced on May 9, 2019.

Sec. 8. General Provisions. (a) Nothing in this order shall be construed to impair or otherwise affect:

(i) the authority granted by law to an executive department or agency, or the head thereof; or

(ii) the functions of the Director of the Office of Management and Budget relating to budgetary, administrative, or legislative proposals.

(b) This order shall be implemented consistent with applicable law and subject to the availability of appropriations.

(c) This order is not intended to, and does not, create any right or benefit, substantive or procedural, enforceable at law or in equity by any party against the United States, its departments, agencies, or entities, its officers, employees, or agents, or any other person.

DONALD J. TRUMP

Footnotes

[1] So in original. Probably should be “from”.

42 U.S.C.A. § 18001, 42 USCA § 18001
Current through PL 117-15 with the exception of PL 116-283, Div. A, Title XVIII.

End of Document

United States Code Annotated
Title 42. The Public Health and Welfare
Chapter 157. Quality Affordable Health Care for All Americans
Subchapter III. Available Coverage Choices for All Americans
Part B. Consumer Choices and Insurance Competition Through Health Benefit Exchanges

42 U.S.C.A. § 18031

§ 18031. Affordable choices of health benefit plans

Effective: December 20, 2019

Currentness

(a) Assistance to States to establish American Health Benefit Exchanges

(1) Planning and establishment grants

There shall be appropriated to the Secretary, out of any moneys in the Treasury not otherwise appropriated, an amount necessary to enable the Secretary to make awards, not later than 1 year after March 23, 2010, to States in the amount specified in paragraph (2) for the uses described in paragraph (3).

(2) Amount specified

For each fiscal year, the Secretary shall determine the total amount that the Secretary will make available to each State for grants under this subsection.

(3) Use of funds

A State shall use amounts awarded under this subsection for activities (including planning activities) related to establishing an American Health Benefit Exchange, as described in subsection (b).

(4) Renewability of grant

(A) In general

Subject to subsection (d)(4), the Secretary may renew a grant awarded under paragraph (1) if the State recipient of such grant--

(i) is making progress, as determined by the Secretary, toward--

(I) establishing an Exchange; and

(II) implementing the reforms described in subtitles A and C (and the amendments made by such subtitles); and

(ii) is meeting such other benchmarks as the Secretary may establish.

(B) Limitation

No grant shall be awarded under this subsection after January 1, 2015.

(5) Technical assistance to facilitate participation in SHOP Exchanges

The Secretary shall provide technical assistance to States to facilitate the participation of qualified small businesses in such States in SHOP Exchanges.

(b) American Health Benefit Exchanges

(1) In general

Each State shall, not later than January 1, 2014, establish an American Health Benefit Exchange (referred to in this title as an "Exchange") for the State that--

(A) facilitates the purchase of qualified health plans;

(B) provides for the establishment of a Small Business Health Options Program (in this title referred to as a "SHOP Exchange") that is designed to assist qualified employers in the State who are small employers in facilitating the enrollment of their employees in qualified health plans offered in the small group market in the State; and

(C) meets the requirements of subsection (d).

(2) Merger of individual and SHOP Exchanges

A State may elect to provide only one Exchange in the State for providing both Exchange and SHOP Exchange services to both qualified individuals and qualified small employers, but only if the Exchange has adequate resources to assist such individuals and employers.

(c) Responsibilities of the Secretary

(1) In general

The Secretary shall, by regulation, establish criteria for the certification of health plans as qualified health plans. Such criteria shall require that, to be certified, a plan shall, at a minimum--

(A) meet marketing requirements, and not employ marketing practices or benefit designs that have the effect of discouraging the enrollment in such plan by individuals with significant health needs;

(B) ensure a sufficient choice of providers (in a manner consistent with applicable network adequacy provisions under section 2702(c) of the Public Health Service Act), and provide information to enrollees and prospective enrollees on the availability of in-network and out-of-network providers;

(C) include within health insurance plan networks those essential community providers, where available, that serve predominately low-income, medically-underserved individuals, such as health care providers

defined in section 340B(a)(4) of the Public Health Service Act and providers described in section 1927(c)(1)(D)(i)(IV) of the Social Security Act as set forth by section 221 of Public Law 111-8, except that nothing in this subparagraph shall be construed to require any health plan to provide coverage for any specific medical procedure;

(D)(i) be accredited with respect to local performance on clinical quality measures such as the Healthcare Effectiveness Data and Information Set, patient experience ratings on a standardized Consumer Assessment of Healthcare Providers and Systems survey, as well as consumer access, utilization management, quality assurance, provider credentialing, complaints and appeals, network adequacy and access, and patient information programs by any entity recognized by the Secretary for the accreditation of health insurance issuers or plans (so long as any such entity has transparent and rigorous methodological and scoring criteria); or

(ii) receive such accreditation within a period established by an Exchange for such accreditation that is applicable to all qualified health plans;

(E) implement a quality improvement strategy described in subsection (g)(1);

(F) utilize a uniform enrollment form that qualified individuals and qualified employers may use (either electronically or on paper) in enrolling in qualified health plans offered through such Exchange, and that takes into account criteria that the National Association of Insurance Commissioners develops and submits to the Secretary;

(G) utilize the standard format established for presenting health benefits plan options;

(H) provide information to enrollees and prospective enrollees, and to each Exchange in which the plan is offered, on any quality measures for health plan performance endorsed under section 399JJ of the Public Health Service Act, as applicable; and

(I) report to the Secretary at least annually and in such manner as the Secretary shall require, pediatric quality reporting measures consistent with the pediatric quality reporting measures established under section 1139A of the Social Security Act.

(2) Rule of construction

Nothing in paragraph (1)(C) shall be construed to require a qualified health plan to contract with a provider described in such paragraph if such provider refuses to accept the generally applicable payment rates of such plan.

(3) Rating system

The Secretary shall develop a rating system that would rate qualified health plans offered through an Exchange in each benefits level on the basis of the relative quality and price. The Exchange shall include the quality rating in the information provided to individuals and employers through the Internet portal established under paragraph (4).

(4) Enrollee satisfaction system

The Secretary shall develop an enrollee satisfaction survey system that would evaluate the level of enrollee satisfaction with qualified health plans offered through an Exchange, for each such qualified health plan that had more than 500 enrollees in the previous year. The Exchange shall include enrollee satisfaction information in the information provided to individuals and employers through the Internet portal established under paragraph (5) in a manner that allows individuals to easily compare enrollee satisfaction levels between comparable plans.

(5) Internet portals

The Secretary shall--

(A) continue to operate, maintain, and update the Internet portal developed under section 18003(a) of this title and to assist States in developing and maintaining their own such portal; and

(B) make available for use by Exchanges a model template for an Internet portal that may be used to direct qualified individuals and qualified employers to qualified health plans, to assist such individuals and employers in determining whether they are eligible to participate in an Exchange or eligible for a premium tax credit or cost-sharing reduction, and to present standardized information (including quality ratings) regarding qualified health plans offered through an Exchange to assist consumers in making easy health insurance choices.

Such template shall include, with respect to each qualified health plan offered through the Exchange in each rating area, access to the uniform outline of coverage the plan is required to provide under section

2716 of the Public Health Service Act and to a copy of the plan's written policy.

(6) Enrollment periods

The Secretary shall require an Exchange to provide for--

(A) an initial open enrollment, as determined by the Secretary (such determination to be made not later than July 1, 2012);

(B) annual open enrollment periods, as determined by the Secretary for calendar years after the initial enrollment period;

(C) special enrollment periods specified in section 9801 of Title 26 and other special enrollment periods under circumstances similar to such periods under part D of title XVIII of the Social Security Act; and

(D) special monthly enrollment periods for Indians (as defined in section 1603 of Title 25).

(7) Reenrollment of certain individuals in qualified health plans in certain exchanges

(A) In general

In the case of an Exchange that the Secretary operates pursuant to section 18041(c)(1) of this title, the Secretary shall establish a process under which an individual described in subparagraph (B) is reenrolled for plan year 2021 in a qualified health plan offered through such Exchange. Such qualified health plan under which such individual is so reenrolled shall be--

(i) if available for plan year 2021, the qualified health plan under which such individual is enrolled during the annual open enrollment period for such plan year; and

(ii) if such qualified health plan is not available for plan year 2021, a qualified health plan offered through such Exchange determined appropriate by the Secretary.

(B) Individual described

An individual described in this subsection is an individual who, with respect to plan year 2020--

(i) resides in a State with an Exchange described in subparagraph (A);

(ii) is enrolled in a qualified health plan during such plan year and does not enroll in a qualified health plan for plan year 2021 during the annual open enrollment period for such plan year 2021; and

(iii) does not elect to disenroll under a qualified health plan for plan year 2021 during such annual open enrollment period.

(d) Requirements

(1) In general

An Exchange shall be a governmental agency or nonprofit entity that is established by a State.

(2) Offering of coverage

(A) In general

An Exchange shall make available qualified health plans to qualified individuals and qualified employers.

(B) Limitation

(i) In general

An Exchange may not make available any health plan that is not a qualified health plan.

(ii) Offering of stand-alone dental benefits

Each Exchange within a State shall allow an issuer of a plan that only provides limited scope dental benefits meeting the requirements of section 9832(c)(2)(A) of Title 26 to offer the plan through the Exchange (either separately or in conjunction with a qualified health plan) if the plan provides pediatric dental benefits meeting the requirements of section 18022(b)(1)(J) of this title).

(3) Rules relating to additional required benefits

(A) In general

Except as provided in subparagraph (B), an Exchange may make available a qualified health plan notwithstanding any provision of law that may require benefits other than the essential health benefits specified under section 18022(b) of this title.

(B) States may require additional benefits

(i) In general

Subject to the requirements of clause (ii), a State may require that a qualified health plan offered in such State offer benefits in addition to the essential health benefits specified under section 18022(b) of this title.

(ii) State must assume cost

A State shall make payments--

(I) to an individual enrolled in a qualified health plan offered in such State; or

(II) on behalf of an individual described in subclause (I) directly to the qualified health plan in which

such individual is enrolled;

to defray the cost of any additional benefits described in clause (i).

(4) Functions

An Exchange shall, at a minimum--

(A) implement procedures for the certification, recertification, and decertification, consistent with guidelines developed by the Secretary under subsection (c), of health plans as qualified health plans;

(B) provide for the operation of a toll-free telephone hotline to respond to requests for assistance;

(C) maintain an Internet website through which enrollees and prospective enrollees of qualified health plans may obtain standardized comparative information on such plans;

(D) assign a rating to each qualified health plan offered through such Exchange in accordance with the criteria developed by the Secretary under subsection (c)(3);

(E) utilize a standardized format for presenting health benefits plan options in the Exchange, including the use of the uniform outline of coverage established under section 2715 of the Public Health Service Act;

(F) in accordance with section 18083 of this title, inform individuals of eligibility requirements for the medicaid program under title XIX of the Social Security Act, the CHIP program under title XXI of such Act, or any applicable State or local public program and if through screening of the application by the Exchange, the Exchange determines that such individuals are eligible for any such program, enroll such individuals in such program;

(G) establish and make available by electronic means a calculator to determine the actual cost of coverage after the application of any premium tax credit under section 36B of Title 26 and any cost-sharing reduction under section 18071 of this title;

(H) subject to section 18081 of this title, grant a certification attesting that, for purposes of the individual responsibility penalty under section 5000A of Title 26, an individual is exempt from the individual requirement or from the penalty imposed by such section because--

(i) there is no affordable qualified health plan available through the Exchange, or the individual's employer, covering the individual; or

(ii) the individual meets the requirements for any other such exemption from the individual responsibility requirement or penalty;

(I) transfer to the Secretary of the Treasury--

(i) a list of the individuals who are issued a certification under subparagraph (H), including the name and taxpayer identification number of each individual;

(ii) the name and taxpayer identification number of each individual who was an employee of an employer but who was determined to be eligible for the premium tax credit under section 36B of Title 26 because--

(I) the employer did not provide minimum essential coverage; or

(II) the employer provided such minimum essential coverage but it was determined under section 36B(c)(2)(C) of such title to either be unaffordable to the employee or not provide the required minimum actuarial value; and

(iii) the name and taxpayer identification number of each individual who notifies the Exchange under section 18081(b)(4) of this title that they have changed employers and of each individual who ceases coverage under a qualified health plan during a plan year (and the effective date of such cessation);

(J) provide to each employer the name of each employee of the employer described in subparagraph (I)(ii) who ceases coverage under a qualified health plan during a plan year (and the effective date of such cessation); and

(K) establish the Navigator program described in subsection (i).

(5) Funding limitations

(A) No Federal funds for continued operations

In establishing an Exchange under this section, the State shall ensure that such Exchange is self-sustaining beginning on January 1, 2015, including allowing the Exchange to charge assessments or user fees to participating health insurance issuers, or to otherwise generate funding, to support its operations.

(B) Prohibiting wasteful use of funds

In carrying out activities under this subsection, an Exchange shall not utilize any funds intended for the administrative and operational expenses of the Exchange for staff retreats, promotional giveaways, excessive executive compensation, or promotion of Federal or State legislative and regulatory modifications.

(6) Consultation

An Exchange shall consult with stakeholders relevant to carrying out the activities under this section, including--

(A) educated health care consumers who are enrollees in qualified health plans;

(B) individuals and entities with experience in facilitating enrollment in qualified health plans;

(C) representatives of small businesses and self-employed individuals;

(D) State Medicaid offices; and

(E) advocates for enrolling hard to reach populations.

(7) Publication of costs

An Exchange shall publish the average costs of licensing, regulatory fees, and any other payments required by the Exchange, and the administrative costs of such Exchange, on an Internet website to educate consumers on such costs. Such information shall also include monies lost to waste, fraud, and abuse.

(e) Certification

(1) In general

An Exchange may certify a health plan as a qualified health plan if--

(A) such health plan meets the requirements for certification as promulgated by the Secretary under subsection (c)(1); and

(B) the Exchange determines that making available such health plan through such Exchange is in the interests of qualified individuals and qualified employers in the State or States in which such Exchange operates, except that the Exchange may not exclude a health plan--

(i) on the basis that such plan is a fee-for-service plan;

(ii) through the imposition of premium price controls; or

(iii) on the basis that the plan provides treatments necessary to prevent patients' deaths in circumstances the Exchange determines are inappropriate or too costly.

(2) Premium considerations

The Exchange shall require health plans seeking certification as qualified health plans to submit a justification for any premium increase prior to implementation of the increase. Such plans shall prominently

post such information on their websites. The Exchange shall take this information, and the information and the recommendations provided to the Exchange by the State under section 2794(b)(1) of the Public Health Service Act (relating to patterns or practices of excessive or unjustified premium increases), into consideration when determining whether to make such health plan available through the Exchange. The Exchange shall take into account any excess of premium growth outside the Exchange as compared to the rate of such growth inside the Exchange, including information reported by the States.

(3) Transparency in coverage

(A) In general

The Exchange shall require health plans seeking certification as qualified health plans to submit to the Exchange, the Secretary, the State insurance commissioner, and make available to the public, accurate and timely disclosure of the following information:

(i) Claims payment policies and practices.

(ii) Periodic financial disclosures.

(iii) Data on enrollment.

(iv) Data on disenrollment.

(v) Data on the number of claims that are denied.

(vi) Data on rating practices.

(vii) Information on cost-sharing and payments with respect to any out-of-network coverage.

(viii) Information on enrollee and participant rights under this title.

(ix) Other information as determined appropriate by the Secretary.

(B) Use of plain language

The information required to be submitted under subparagraph (A) shall be provided in plain language. The term "plain language" means language that the intended audience, including individuals with limited English proficiency, can readily understand and use because that language is concise, well-organized, and follows other best practices of plain language writing. The Secretary and the Secretary of Labor shall jointly develop and issue guidance on best practices of plain language writing.

(C) Cost sharing transparency

The Exchange shall require health plans seeking certification as qualified health plans to permit individuals to learn the amount of cost-sharing (including deductibles, copayments, and coinsurance) under the individual's plan or coverage that the individual would be responsible for paying with respect to the furnishing of a specific item or service by a participating provider in a timely manner upon the request of the individual. At a minimum, such information shall be made available to such individual through an Internet website and such other means for individuals without access to the Internet.

(D) Group health plans

The Secretary of Labor shall update and harmonize the Secretary's rules concerning the accurate and timely disclosure to participants by group health plans of plan disclosure, plan terms and conditions, and periodic financial disclosure with the standards established by the Secretary under subparagraph (A).

(f) Flexibility

(1) Regional or other interstate Exchanges

An Exchange may operate in more than one State if--

(A) each State in which such Exchange operates permits such operation; and

(B) the Secretary approves such regional or interstate Exchange.

(2) Subsidiary Exchanges

A State may establish one or more subsidiary Exchanges if--

(A) each such Exchange serves a geographically distinct area; and

(B) the area served by each such Exchange is at least as large as a rating area described in section 2701(a) of the Public Health Service Act.

(3) Authority to contract

(A) In general

A State may elect to authorize an Exchange established by the State under this section to enter into an agreement with an eligible entity to carry out 1 or more responsibilities of the Exchange.

(B) Eligible entity

In this paragraph, the term "eligible entity" means--

(i) a person--

(I) incorporated under, and subject to the laws of, 1 or more States;

(II) that has demonstrated experience on a State or regional basis in the individual and small group health insurance markets and in benefits coverage; and

(III) that is not a health insurance issuer or that is treated under subsection (a) or (b) of section 52 of Title 26 as a member of the same controlled group of corporations (or under common control with) as a health insurance issuer; or

(ii) the State medicaid agency under title XIX of the Social Security Act.

(g) Rewarding quality through market-based incentives

(1) Strategy described

A strategy described in this paragraph is a payment structure that provides increased reimbursement or other incentives for--

(A) improving health outcomes through the implementation of activities that shall include quality reporting, effective case management, care coordination, chronic disease management, medication and care compliance initiatives, including through the use of the medical home model, for treatment or services under the plan or coverage;

(B) the implementation of activities to prevent hospital readmissions through a comprehensive program for hospital discharge that includes patient-centered education and counseling, comprehensive discharge planning, and post discharge reinforcement by an appropriate health care professional;

(C) the implementation of activities to improve patient safety and reduce medical errors through the appropriate use of best clinical practices, evidence based medicine, and health information technology under the plan or coverage;

(D) the implementation of wellness and health promotion activities; and

(E) the implementation of activities to reduce health and health care disparities, including through the use of language services, community outreach, and cultural competency trainings.

(2) Guidelines

The Secretary, in consultation with experts in health care quality and stakeholders, shall develop guidelines concerning the matters described in paragraph (1).

(3) Requirements

The guidelines developed under paragraph (2) shall require the periodic reporting to the applicable Exchange of the activities that a qualified health plan has conducted to implement a strategy described in paragraph (1).

(h) Quality improvement

(1) Enhancing patient safety

Beginning on January 1, 2015, a qualified health plan may contract with--

(A) a hospital with greater than 50 beds only if such hospital--

(i) utilizes a patient safety evaluation system as described in part C of title IX of the Public Health Service Act; and

(ii) implements a mechanism to ensure that each patient receives a comprehensive program for hospital discharge that includes patient-centered education and counseling, comprehensive discharge planning, and post discharge reinforcement by an appropriate health care professional; or

(B) a health care provider only if such provider implements such mechanisms to improve health care quality as the Secretary may by regulation require.

(2) Exceptions

The Secretary may establish reasonable exceptions to the requirements described in paragraph (1).

(3) Adjustment

The Secretary may by regulation adjust the number of beds described in paragraph (1)(A).

(i) Navigators

(1) In general

An Exchange shall establish a program under which it awards grants to entities described in paragraph (2) to carry out the duties described in paragraph (3).

(2) Eligibility

(A) In general

To be eligible to receive a grant under paragraph (1), an entity shall demonstrate to the Exchange involved that the entity has existing relationships, or could readily establish relationships, with employers and employees, consumers (including uninsured and underinsured consumers), or self-employed individuals likely to be qualified to enroll in a qualified health plan.

(B) Types

Entities described in subparagraph (A) may include trade, industry, and professional associations, commercial fishing industry organizations, ranching and farming organizations, community and consumer-focused nonprofit groups, chambers of commerce, unions, resource partners of the Small Business Administration, other licensed insurance agents and brokers, and other entities that--

(i) are capable of carrying out the duties described in paragraph (3);

(ii) meet the standards described in paragraph (4); and

(iii) provide information consistent with the standards developed under paragraph (5).

(3) Duties

An entity that serves as a navigator under a grant under this subsection shall--

(A) conduct public education activities to raise awareness of the availability of qualified health plans;

(B) distribute fair and impartial information concerning enrollment in qualified health plans, and the availability of premium tax credits under section 36B of Title 26 and cost-sharing reductions under section 18071 of this title;

(C) facilitate enrollment in qualified health plans;

(D) provide referrals to any applicable office of health insurance consumer assistance or health insurance ombudsman established under section 2793 of the Public Health Service Act, or any other appropriate State agency or agencies, for any enrollee with a grievance, complaint, or question regarding their health plan, coverage, or a determination under such plan or coverage; and

(E) provide information in a manner that is culturally and linguistically appropriate to the needs of the population being served by the Exchange or Exchanges.

(4) Standards

(A) In general

The Secretary shall establish standards for navigators under this subsection, including provisions to ensure that any private or public entity that is selected as a navigator is qualified, and licensed if appropriate, to engage in the navigator activities described in this subsection and to avoid conflicts of interest. Under such standards, a navigator shall not--

(i) be a health insurance issuer; or

(ii) receive any consideration directly or indirectly from any health insurance issuer in connection with the enrollment of any qualified individuals or employees of a qualified employer in a qualified health plan.

(5) Fair and impartial information and services

The Secretary, in collaboration with States, shall develop standards to ensure that information made available by navigators is fair, accurate, and impartial.

(6) Funding

Grants under this subsection shall be made from the operational funds of the Exchange and not Federal funds received by the State to establish the Exchange.

(j) Applicability of mental health parity

Section 2726 of the Public Health Service Act shall apply to qualified health plans in the same manner and to the same extent as such section applies to health insurance issuers and group health plans.

(k) Conflict

An Exchange may not establish rules that conflict with or prevent the application of regulations promulgated by the Secretary under this subchapter.

CREDIT(S)

(Pub.L. 111-148, Title I, § 1311, Title X, §§ 10104(e) to (h), 10203(a), Mar. 23, 2010, 124 Stat. 173, 900, 927; Pub.L. 116-94, Div. N, Title I, § 608, Dec. 20, 2019, 133 Stat. 3130.)

Notes of Decisions (21)

§ 18031. Affordable choices of health benefit plans, 42 USCA § 18031

42 U.S.C.A. § 18031, 42 USCA § 18031
Current through PL 117-15 with the exception of PL 116-283, Div. A, Title XVIII.

End of Document

West's Nevada Revised Statutes Annotated
Nevada Rules of Court
Rules of Appellate Procedure (Refs & Annos)
II. Appeals from Judgments and Orders of District Courts

Nevada Rules of Appellate Procedure, Rule 4

Rule 4. Appeal--When Taken

Currentness

(a) Appeals in Civil Cases.

(1) *Time and Location for Filing a Notice of Appeal.* In a civil case in which an appeal is permitted by law from a district court, the notice of appeal required by Rule 3 shall be filed with the district court clerk. Except as provided in Rule 4(a)(4), a notice of appeal must be filed after entry of a written judgment or order, and no later than 30 days after the date that written notice of entry of the judgment or order appealed from is served. If an applicable statute provides that a notice of appeal must be filed within a different time period, the notice of appeal required by these Rules must be filed within the time period established by the statute.

(2) *Multiple Appeals.* If one party timely files a notice of appeal, any other party may file and serve a notice of appeal within 14 days after the date when the first notice was served, or within the time otherwise prescribed by Rule 4(a), whichever period last expires.

(3) *Entry Defined.* A judgment or order is entered for purposes of this Rule when it is signed by the judge or by the clerk, as the case may be, and filed with the clerk. A notice or stipulation of dismissal filed under NRCP 41(a)(1) has the same effect as a judgment or order signed by the judge and filed by the clerk and constitutes entry of a judgment or order for purposes of this Rule. If that notice or stipulation dismisses all unresolved claims pending in an action in the district court, the notice or stipulation constitutes entry of a final judgment or order for purposes of this Rule.

(4) *Effect of Certain Motions on a Notice of Appeal.* If a party timely files in the district court any of the following motions under the Nevada Rules of Civil Procedure, the time to file a notice of appeal runs for all parties from entry of an order disposing of the last such remaining motion, and the notice of appeal must be filed no later than 30 days from the date of service of written notice of entry of that order:

(A) a motion for judgment under Rule 50(b);

(B) a motion under Rule 52(b) to amend or make additional findings of fact;

(C) a motion under Rule 59 to alter or amend the judgment;

(D) a motion for a new trial under Rule 59.

(5) *Appeal From Certain Amended Judgments and Post-Judgment Orders.* An appeal from a judgment substantively altered or amended upon the granting of a motion listed in Rule 4(a)(4), or from an order granting or denying a new trial, is taken by filing a notice of appeal, or amended notice of appeal, in compliance with Rule 3. The notice of appeal or amended notice of appeal must be filed after entry of a written order disposing of the last such remaining timely motion and no later than 30 days from the date of service of written notice of entry of that order.

(6) *Premature Notice of Appeal.* A premature notice of appeal does not divest the district court of jurisdiction. The court may dismiss as premature a notice of appeal filed after the oral pronouncement of a decision or order but before entry of the written judgment or order, or before entry of the written disposition of the last-remaining timely motion listed in Rule 4(a)(4). If, however, a written order or judgment, or a written disposition of the last-remaining timely motion listed in Rule 4(a)(4), is entered before dismissal of the premature appeal, the notice of appeal shall be considered filed on the date of and after entry of the order, judgment or written disposition of the last-remaining timely motion.

(7) *Amended Notice of Appeal.* No additional fees shall be required if any party files an amended notice of appeal in order to comply with the provisions of this Rule.

(b) Appeals in Criminal Cases.

(1) *Time for Filing a Notice of Appeal.*

(A) Appeal by Defendant or Petitioner. Except as otherwise provided in NRS 34.560(2), NRS 34.575(1), NRS 176.09183(6), NRS 177.055, and Rule 4(c), the notice of appeal by a defendant or petitioner in a criminal case shall be filed with the district court clerk within 30 days after the entry of the judgment or order being appealed.

(B) Appeal by the State. Except as otherwise provided in NRS 34.575(2), NRS 176.09183(4), and NRS 177.015(2), when an appeal by the state is authorized by statute, the notice of appeal shall be filed with the district court clerk within 30 days after the entry of the judgment or order being appealed.

(2) *Filing Before Entry of Judgment.* A notice of appeal filed after the announcement of a decision, sentence or order--but before entry of the judgment or order--shall be treated as filed after such entry and on the day thereof.

(3) *Effect of a Motion on a Notice of Appeal.*

(A) If a defendant timely files a motion in arrest of judgment or a motion for a new trial on any ground other than newly discovered evidence and the motion has not been denied by oral pronouncement or entry of a written order when the judgment of conviction is entered, the notice of appeal from the judgment of conviction may be filed within 30 days after the entry of an order denying the motion.

(B) If a defendant files a motion for a new trial based on the ground of newly discovered evidence before entry of the judgment of conviction and the motion has not been denied by oral pronouncement or entry of a written order when the judgment of conviction is entered, the notice of appeal from the judgment of conviction may be filed within 30 days after the entry of an order denying the motion. If a defendant makes such a motion within 30 days after the entry of the judgment of conviction, the time for the defendant to file the notice of appeal from the judgment of conviction will be similarly extended.

(4) *Entry Defined.* A judgment or order is entered for purposes of this Rule when it is signed by the judge and filed with the clerk.

(5) *Time for Entry of Judgment; Content of Judgment or Order in Postconviction Matters.*

(A) Judgment of Conviction. The district court judge shall enter a written judgment of conviction within 14 days after sentencing.

(B) Order Resolving Postconviction Matter. The district court judge shall enter a written judgment or order finally resolving any postconviction matter within 21 days after the district court judge's oral pronouncement of a final decision in such a matter. The judgment or order in any postconviction matter must contain specific findings of fact and conclusions of law supporting the district court's decision.

(C) Sanctions; Counsel's Failure to Timely Prepare Judgment or Order. The court may impose sanctions on any counsel instructed by the district court judge to draft the judgment or order and who does not submit the proposed judgment or order to the district court judge within the applicable time periods specified in Rule 4(b)(5).

(6) *Withdrawal of Appeal.* If an appellant no longer desires to pursue an appeal after the notice of appeal is filed, counsel for appellant shall file with the clerk of the Supreme Court a notice of withdrawal of appeal. The notice of withdrawal of appeal shall substantially comply with Form 8 in the Appendix of Forms.

(c) Untimely Direct Appeal From a Judgment of Conviction and Sentence.

(1) *When an Untimely Direct Appeal From a Judgment of Conviction and Sentence May Be Filed.* An untimely notice of appeal from a judgment of conviction and sentence may be filed only under the following circumstances:

(A) A postconviction petition for a writ of habeas corpus has been timely and properly filed in accordance with the provisions of NRS 34.720 to 34.830, asserting a viable claim that the petitioner was unlawfully deprived of the right to a timely direct appeal from a judgment of conviction and sentence; and

(B) The district court in which the petition is considered enters a written order containing:

(i) specific findings of fact and conclusions of law finding that the petitioner has established a valid appeal-deprivation claim and is entitled to a direct appeal with the assistance of appointed or retained appellate counsel;

(ii) if the petitioner is indigent, directions for the appointment of appellate counsel, other than counsel for the defense in the proceedings leading to the conviction, to represent the petitioner in the direct appeal from the conviction and sentence; and

(iii) directions to the district court clerk to prepare and file--within 7 days of the entry of the district court's order--a notice of appeal from the judgment of conviction and sentence on the petitioner's behalf in substantially the form provided in Form 1 in the Appendix of Forms.

(C) If a federal court of competent jurisdiction issues a final order directing the state to provide a direct appeal to a federal habeas corpus petitioner, the petitioner or his or her counsel shall file the federal court order within 30 days of entry of the order in the district court in which petitioner's criminal case was pending. The clerk of the district court shall prepare and file--within 30 days of filing of the federal court order in the district court--a notice of appeal from the judgment of conviction and sentence on the petitioner's behalf in substantially the form provided in Form 1 in the Appendix of Forms.

(2) *Service by the District Court Clerk.* The district court clerk shall serve certified copies of the district court's written order and the notice of appeal required by Rule 4(c) on the petitioner and petitioner's counsel in the postconviction proceeding, if any, the respondent, the Attorney General, the district attorney of the county in which the petitioner was convicted, the appellate counsel appointed to represent the petitioner in the direct appeal, if any, and the clerk of the Supreme Court.

(3) *Notice of Appeal Filed by Petitioner's Counsel or Petitioner.* If the district court has entered an order containing the findings required by Rule 4(c)(1)(B) and the district court clerk has not yet prepared and filed the notice of appeal on the petitioner's behalf, the petitioner or petitioner's counsel may file the notice of appeal from the judgment of conviction and sentence.

(4) *Motion to Dismiss Appeal.* The state may challenge a district court's written order granting an appeal-deprivation claim by filing a motion to dismiss the appeal with the clerk of the Supreme Court within 30 days after the date on which the appeal is docketed in the Supreme Court. The state's motion to dismiss shall be properly supported with all documents relating to the district court proceeding that are necessary to the Supreme Court's or Court of Appeals' complete understanding of the matter.

(5) *Effect on Procedural Bars.* When a direct appeal of a criminal conviction and sentence is conducted under this Rule, the timeliness provisions governing any subsequent habeas corpus attack on the judgment shall begin to run upon the termination of the direct appeal, as provided in NRS 34.726(1) and NRS 34.800(2). A habeas corpus petition filed after a direct appeal conducted under this Rule shall not be deemed a "second or successive petition" under NRS 34.810(2).

(d) Appeal by an Inmate Confined in an Institution. If an inmate confined in an institution files a notice of appeal in either a civil or a criminal case, the notice is timely if it is delivered to a prison official for mailing on or before the last day for filing. If the institution has a notice-of-appeal log or another system designed for legal mail, the inmate must use that log or system to receive the benefit of this Rule.

(e) Mistaken Filing in the Supreme Court. If a notice of appeal in either a civil or a criminal case is mistakenly filed in the Supreme Court rather than the district court, the clerk of the Supreme Court must note on the notice the date when it was received and send it to the district court clerk. The notice is then considered filed

in the district court on the date so noted.

(f) Expediting Criminal Appeals. The court may, by a majority of its members, make orders to expedite the handling of criminal appeals, including without limitation the following:

(1) Elimination of steps in preparation of the record and the briefs.

(2) Expediting preparation of stenographic transcripts.

(3) Priority of calendaring for oral argument.

(4) Utilization of court opinions or per curiam orders.

(5) Other lawful measures reasonably calculated to expedite the appeal and promote justice.

Credits

Amended effective September 1, 1989; February 22, 1998; December 16, 2004; July 1, 2009; January 20, 2015; October 1, 2015; March 1, 2019.

Editors' Notes

ADVISORY COMMITTEE NOTES

Subdivision (a) is revised to delete references to federal proceedings in admiralty and bankruptcy, and to substitute a reference to Nevada Rules of Civil Procedure rather than the federal rules. Also, the rule is revised to preserve existing Nevada law providing that the 30-day period within which an appeal may be taken runs from the date of service of written notice of entry of judgment or order appealed from, rather than the date of entry of judgment or order appealed from, under federal law. In addition, existing Nevada law, to the effect that a judgment or order is "entered" when it is signed by the court and filed with the clerk, is preserved, rather than when it is entered in a civil docket, as under federal law.

The provision in the first paragraph of subdivision (a), authorizing any other party to file a notice of appeal within 14 days after service of the first notice of appeal represents a departure from existing Nevada law, which requires notices of appeal by all parties wishing to appeal within 30 days after service of written notice of entry of judgment. The committee felt this provision desirable, for it allows parties other than the first appellant a

reasonable time within which to decide whether to perfect an appeal of their own after the first appeal has been commenced.

The second paragraph of subdivision (a) is revised to include in part (4) orders granting as well as denying motions for new trial, to preserve current law as stated in N.R.C.P. 73(a).

The third paragraph of subdivision (a) of the federal rule, authorizing the district court to extend time beyond the 30-day appeal period for filing the notice of appeal, was deleted as unnecessary and undesirable under Nevada practice.

Subdivision (b), governing appeals in criminal cases is revised to substitute “state” for “government,” and to preserve existing Nevada law to the effect that a judgment or order is “entered” when signed by the court and filed with the clerk. The appeal period is altered to conform with NRS 177.066, which prescribes 30 days from the rendition of the judgment or order of the district court.

Subdivision (c) was added pursuant to the court’s suggestion to the committee (paragraph 14) that provision be made for expediting criminal appeals where appropriate.

Notes of Decisions (94)

Rules App. Proc., Rule 4, NV ST RAP Rule 4
Current with amendments received through April 15, 2021.

West's Nevada Revised Statutes Annotated
Nevada Rules of Court
Rules of Appellate Procedure (Refs & Annos)
II. Appeals from Judgments and Orders of District Courts

Nevada Rules of Appellate Procedure, Rule 17

Rule 17. Division of Cases Between the Supreme Court and the Court of Appeals

Currentness

(a) Cases Retained by the Supreme Court. The Supreme Court shall hear and decide the following:

(1) All death penalty cases;

(2) Cases involving ballot or election questions;

(3) Cases involving judicial discipline;

(4) Cases involving attorney admission, suspension, discipline, disability, reinstatement, and resignation;

(5) Cases involving the approval of prepaid legal service plans;

(6) Questions of law certified by a federal court;

(7) Disputes between branches of government or local governments;

(8) Administrative agency cases involving tax, water, or public utilities commission determinations;

(9) Cases originating in business court;

(10) Cases involving the termination of parental rights or NRS Chapter 432B;

(11) Matters raising as a principal issue a question of first impression involving the United States or Nevada Constitutions or common law; and

(12) Matters raising as a principal issue a question of statewide public importance, or an issue upon which there is an inconsistency in the published decisions of the Court of Appeals or of the Supreme Court or a conflict between published decisions of the two courts.

(b) Cases Assigned to Court of Appeals. The Court of Appeals shall hear and decide only those matters assigned to it by the Supreme Court and those matters within its original jurisdiction. Except as provided in Rule 17(a), the Supreme Court may assign to the Court of Appeals any case filed in the Supreme Court. The following case categories are presumptively assigned to the Court of Appeals:

(1) Appeals from a judgment of conviction based on a plea of guilty, guilty but mentally ill, or nolo contendere (Alford);

(2) Appeals from a judgment of conviction based on a jury verdict that

(A) do not involve a conviction for any offenses that are category A or B felonies; or

(B) challenge only the sentence imposed and/or the sufficiency of the evidence;

(3) Postconviction appeals that involve a challenge to a judgment of conviction or sentence for offenses that are not category A felonies;

(4) Postconviction appeals that involve a challenge to the computation of time served under a judgment of conviction, a motion to correct an illegal sentence, or a motion to modify a sentence;

(5) Appeals from a judgment, exclusive of interest, attorney fees, and costs, of $250,000 or less in a tort case;

(6) Cases involving a contract dispute where the amount in controversy is less than $75,000;

(7) Appeals from postjudgment orders in civil cases;

(8) Cases involving statutory lien matters under NRS Chapter 108;

(9) Administrative agency cases except those involving tax, water, or public utilities commission determinations;

(10) Cases involving family law matters other than termination of parental rights or NRS Chapter 432B proceedings;

(11) Appeals challenging venue;

(12) Cases challenging the grant or denial of injunctive relief;

(13) Pretrial writ proceedings challenging discovery orders or orders resolving motions in limine;

(14) Cases involving trust and estate matters in which the corpus has a value of less than $5,430,000; and

(15) Cases arising from the foreclosure mediation program.

(c) Consideration of Workload. In assigning cases to the Court of Appeals, due regard will be given to the workload of each court.

(d) Routing Statements; Finality. A party who believes that a matter presumptively assigned to the Court of Appeals should be retained by the Supreme Court may state the reasons as enumerated in (a) of this Rule in the routing statement of the briefs as provided in Rules 3C, 3E, and 28 or a writ petition as provided in Rule 21. A party may not file a motion or other pleading seeking reassignment of a case that the Supreme Court has assigned to the Court of Appeals.

(e) Transfer and Notice. Upon the transfer of a case to the Court of Appeals, the clerk shall issue a notice to the parties. With the exception of a petition for Supreme Court review under Rule 40B, any pleadings in a case after it has been transferred to the Court of Appeals shall be entitled "In the Court of Appeals of the State of Nevada."

Credits

Adopted effective January 20, 2015. Amended effective January 1, 2017; October 21, 2018.

Editors' Notes

ADVISORY COMMITTEE NOTES

Nothing in Rule 17(b)(8) should be interpreted to deviate from current jurisprudence regarding challenges to discovery orders and orders resolving motions in limine.

Rules App. Proc., Rule 17, NV ST RAP Rule 17
Current with amendments received through April 15, 2021.

West's Nevada Revised Statutes Annotated
Nevada Rules of Court
Rules of Professional Conduct
Client-Lawyer Relationship

Rules of Prof.Conduct, Rule 1.7

Rule 1.7. Conflict of Interest: Current Clients

Currentness

(a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

(1) The representation of one client will be directly adverse to another client; or

(2) There is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

(b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:

(1) The lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;

(2) The representation is not prohibited by law;

(3) The representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and

(4) Each affected client gives informed consent, confirmed in writing.

Credits

Adopted effective May 1, 2006.

Editors' Notes

MODEL RULE COMPARISON

2006 Comparison

Rule 1.7 (formerly Supreme Court Rule 157) is the same as ABA Model Rule 1.7.

Notes of Decisions (17)

Rules of Prof. Conduct, Rule 1.7, NV ST RPC Rule 1.7
Current with amendments received through April 15, 2021.

West's Nevada Revised Statutes Annotated
Nevada Rules of Court
Rules of Professional Conduct
Client-Lawyer Relationship

Rules of Prof.Conduct, Rule 1.9

Rule 1.9. Duties to Former Clients

Currentness

(a) A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing.

(b) A lawyer shall not knowingly represent a person in the same or a substantially related matter in which a firm with which the lawyer formerly was associated had previously represented a client:

(1) Whose interests are materially adverse to that person; and

(2) About whom the lawyer had acquired information protected by Rules 1.6 and 1.9(c) that is material to the matter;

(3) Unless the former client gives informed consent, confirmed in writing.

(c) A lawyer who has formerly represented a client in a matter or whose present or former firm has formerly represented a client in a matter shall not thereafter:

(1) Use information relating to the representation to the disadvantage of the former client except as these Rules would permit or require with respect to a client, or when the information has become generally known; or

(2) Reveal information relating to the representation except as these Rules would permit or require with respect to a client.

Credits

Adopted effective May 1, 2006.

Editors' Notes

MODEL RULE COMPARISON

2006 Comparison

Rule 1.9 (formerly Supreme Court Rule 159) is the same as ABA Model Rule 1.9.

Notes of Decisions (38)

Rules of Prof. Conduct, Rule 1.9, NV ST RPC Rule 1.9
Current with amendments received through April 15, 2021.

Purdon's Pennsylvania Statutes and Consolidated Statutes
Rules of Professional Conduct (Refs & Annos)
Client-Lawyer Relationship (Refs & Annos)

Rules of Prof. Conduct, Rule 1.7, 42 Pa.C.S.A.

Rule 1.7. Conflict of Interest: Current Clients

Currentness

(a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

(1) the representation of one client will be directly adverse to another client; or

(2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

(b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:

(1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;

(2) the representation is not prohibited by law;

(3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and

(4) each affected client gives informed consent.

Credits

Adopted Oct. 16, 1987, effective April 1, 1988. Amended Aug. 23, 2004, effective Jan. 1, 2005. *Comment* revised Dec. 30, 2014, effective in 60 days [March 2, 2015].

Editors' Notes

EXPLANATORY COMMENT

General Principles

[1] Loyalty and independent judgment are essential elements in the lawyer's relationship to a client. Concurrent conflicts of interest can arise from the lawyer's responsibilities to another client, a former client or a third person or from the lawyer's own interests. For specific Rules regarding certain concurrent conflicts of interest, see Rule 1.8. For former client conflicts of interest, see Rule 1.9. For conflicts of interest involving prospective clients, see Rule 1.18. For the definition of " informed consent," see Rule 1.0(e).

[2] Resolution of a conflict of interest problem under this Rule requires the lawyer to: 1) clearly identify the client or clients; 2) determine whether a conflict of interest exists; 3) decide whether the representation may be undertaken despite the existence of a conflict, i.e., whether the conflict is consentable; and 4) if so, consult with the clients affected under paragraph (a) and obtain their informed consent. The clients affected under paragraph (a) include the clients referred to in paragraph (a)(1) and the clients whose representation might be materially limited under paragraph (a)(2).

[3] A conflict of interest may exist before representation is undertaken, in which event the representation must be declined, unless the lawyer obtains the informed consent of each client under the conditions of paragraph (b). To determine whether a conflict of interest exists, a lawyer should adopt reasonable procedures, appropriate for the size and type of firm and practice, to determine in both litigation and non-litigation matters the persons and issues involved. See also Comment to Rule 5.1. Ignorance caused by a failure to institute such procedures will not excuse a lawyer's violation of this Rule. As to whether a client-lawyer relationship exists or, having once been established, is continuing, see Comment to Rule 1.3 and Scope.

[4] If a conflict arises after representation has been undertaken, the lawyer ordinarily must withdraw from the representation, unless the lawyer has obtained the informed consent of the client under the conditions of paragraph (b). See Rule 1.16. Where more than one client is involved, whether the lawyer may continue to represent any of the clients is determined both by the lawyer's ability to comply with duties owed to the former client and by the lawyer's ability to represent adequately the remaining client or clients, given the lawyer's duties to the former client. See Rule 1.9. See also Comments [5] and [29].

[5] Unforeseeable developments, such as changes in corporate and other organizational affiliations or the addition or realignment of parties in litigation, might create conflicts in the midst of a representation, as when a company sued by the lawyer on behalf of one client is bought by another client represented by the lawyer in an unrelated matter. Depending on the circumstances, the lawyer may have the option to withdraw from one of the representations in order to avoid the conflict. The lawyer must seek court approval where necessary and take steps to minimize harm to the clients. See Rule 1.16. The lawyer must continue to protect the confidences of the client from whose representation the lawyer has withdrawn. See Rule 1.9(c).

Identifying Conflicts of Interest: Directly Adverse

[6] Loyalty to a current client prohibits undertaking representation directly adverse to that client without that client's informed consent. Thus, absent consent, a lawyer may not act as an advocate in one matter against a person the lawyer represents in some other matter, even when the matters are wholly unrelated. The client as to whom the representation is directly adverse is likely to feel betrayed, and the resulting damage to the client-lawyer relationship is likely to impair the lawyer's ability to represent the client effectively. In addition, the client on whose behalf the adverse representation is undertaken reasonably may fear that the lawyer will pursue that client's case less effectively out of deference to the other client, i.e., that the representation may be materially limited by the lawyer's interest in retaining the current client. Similarly, a directly adverse conflict may arise when a lawyer is required to cross-examine a client who appears as a witness in a lawsuit involving another client, as when the testimony will be damaging to the client who is represented in the lawsuit. On the other hand, simultaneous representation in unrelated matters of clients whose interests are only economically adverse, such as representation of competing economic enterprises in unrelated litigation, does not ordinarily constitute a conflict of interest and thus may not require consent of the respective clients.

[7] Directly adverse conflicts can also arise in transactional matters. For example, if lawyer is asked to represent the seller of a business in negotiations with a buyer represented by the lawyer, not in the same transaction but in another, unrelated matter, the lawyer could not undertake the representation without the informed consent of each client.

[8] Even where there is no direct adverseness, a conflict of interest exists if there is a significant risk that a lawyer's ability to consider, recommend or carry out an appropriate course of action for the client will be materially limited as a result of the lawyer's other responsibilities or interests. For example, a lawyer asked to represent several individuals seeking to form a joint venture is likely to be materially limited in the lawyer's ability to recommend or advocate all possible positions that each might take because of the lawyer's duty of loyalty to the others. The conflict in effect forecloses alternatives that would otherwise be available to the client. The mere possibility of subsequent harm does not itself require disclosure and consent. The critical questions are the likelihood that a difference in interests will eventuate and, if it does, whether it will materially interfere with the lawyer's independent professional judgment in considering alternatives or foreclose courses of action that reasonably should be pursued on behalf of the client.

Lawyer's Responsibilities to Former Clients and Other Third Persons

[9] In addition to conflicts with other current clients, a lawyer's duties of loyalty and independence may be materially limited by responsibilities to former clients under Rule 1.9 or by the lawyer's responsibilities to other persons, such as fiduciary duties arising from a lawyer's service as a trustee, executor or corporate director.

Personal Interest Conflicts

[10] The lawyer's own interests should not be permitted to have an adverse effect on representation of a client. For example, if the probity of a lawyer's own conduct in a transaction is in serious question, it may be difficult or impossible for the lawyer to give a client detached advice. Similarly, when a lawyer has discussions concerning possible employment with an opponent of the lawyer's client, or with a law firm representing the opponent, such discussions could materially limit the lawyer's representation of the client. In addition, a lawyer may not allow related business interests to affect representation, for example, by referring clients to an enterprise in which the lawyer has an undisclosed financial interest. See Rule 5.8 for specific Rules that prohibit or restrict a lawyer's involvement in the offer, sale, or placement of investment products regardless of an actual conflict or the potential for conflict. See Rule 1.8 for specific Rules pertaining to a number of personal interest conflicts, including business transactions with clients. See also Rule 1.10 (personal interest conflicts under Rule 1.7 ordinarily are not imputed to other lawyers in a law firm).

[11] When lawyers representing different clients in the same matter or in substantially related matters are closely related by blood or marriage, there may be a significant risk that client confidences will be revealed and that the lawyer's family relationship will interfere with both loyalty and independent professional judgment. As a result, each client is entitled to know of the existence and implications of the relationship between the lawyers before the lawyer agrees to undertake the representation. Thus, a lawyer related to another lawyer, e.g., as parent, child, sibling or spouse, ordinarily may not represent a client in a matter where that lawyer is representing another party, unless each client gives informed consent. The disqualification arising from a close family relationship is personal and ordinarily is not imputed to members of firms with whom the lawyers are associated. See Rule 1.10.

[12] A lawyer is prohibited from engaging in sexual relationships with a client unless the sexual relationship predates the formation of the client-lawyer relationship. See Rule 1.8(j).

Interest of Person Paying for a Lawyer's Service

[13] A lawyer may be paid from a source other than the client, including a co-client, if the client is informed of that fact and consents and the arrangement does not compromise the lawyer's duty of loyalty or independent judgment to the client. See Rule 1.8(f). If acceptance of the payment from any other source presents a significant risk that the lawyer's representation of the client will be materially limited by the lawyer's own interest in accommodating the person paying the lawyer's fee or by the lawyer's responsibilities to a payer who is also a co-client, then the lawyer must comply with the requirements of paragraph (b) before accepting the representation, including determining whether the conflict is consentable and, if so, that the client has adequate information about the material risks of the representation.

Prohibited Representations

[14] Ordinarily, clients may consent to representation notwithstanding a conflict. However, as indicated in paragraph 1.7(b), some conflicts are nonconsentable, meaning that the lawyer involved cannot properly ask for such agreement or provide representation on the basis of the client's consent. When the lawyer is representing more than one client, the question of consentability must be resolved as to each client.

[15] Consentability is typically determined by considering whether the interests of the clients will be adequately protected if the clients are permitted to give their informed consent to representation burdened by a conflict of interest. Thus, under paragraph (b)(1), representation is prohibited if in the circumstances the lawyer cannot reasonably conclude that the lawyer will be able to provide competent and diligent representation. See Rule 1.1 (competence) and Rule 1.3 (diligence).

[16] Paragraph (b)(2) describes conflicts that are nonconsentable because the representation is prohibited by applicable law. For example, in some states substantive law provides that the same lawyer may not represent more than one defendant in a capital case, even with the consent of the clients, and under federal criminal statutes certain representations by a former government lawyer are prohibited, despite the informed consent of the former client. In addition, decisional law in some states limits the ability of a governmental client, such as a municipality, to consent to a conflict of interest.

[17] Paragraph (b)(3) describes conflicts that are nonconsentable because of the institutional interest in vigorous development of each client's position when the clients are aligned directly against each other in the same litigation or other proceeding before a tribunal. Whether clients are aligned directly against each other within the meaning of this paragraph requires examination of the context of the proceeding. Although this paragraph does not preclude a lawyer's multiple representation of adverse parties to a mediation (because mediation is not a proceeding before a "tribunal" under Rule 1.0(m)), such representation may be precluded by paragraph (b)(1).

Informed Consent

[18] Informed consent requires that each affected client be aware of the relevant circumstances and of the material and reasonably foreseeable ways that the conflict could have adverse effects on the interests of that client. See Rule 1.0(e) (informed consent). The information required depends on the nature of the conflict and the nature of the risks involved. When representation of multiple clients in a single matter is undertaken, the information must include the implications of the common representation, including possible effects on loyalty, confidentiality and the attorney- client privilege and the advantages and risks involved. See Comment, paragraphs [30] and [31] (effect of common representation on confidentiality).

[19] Under some circumstances it may be impossible to make the disclosure necessary to obtain

consent. For example, when the lawyer represents different clients in related matters and one of the clients refuses to consent to the disclosure necessary to permit the other client to make an informed decision, the lawyer cannot properly ask the latter to consent. In some cases the alternative to common representation can be that each party may have to obtain separate representation with the possibility of incurring additional costs. These costs, along with the benefits of securing separate representation, are factors that may be considered by the affected client in determining whether common representation is in the client's interests.

Confirming Consent

[20] Paragraph (b) requires the lawyer to obtain the informed consent of the client to a concurrent conflict of interest. The client's consent need not be confirmed in writing to be effective. Rather, a writing tends to impress upon clients the seriousness of the decision the client is being asked to make and to avoid disputes or ambiguities that might later occur in the absence of a writing. See also Rule 1.0(b) (writing includes electronic transmission).

Revoking Consent

[21] A client who has given consent to a conflict may revoke the consent and, like any other client, may terminate the lawyer's representation at any time. Whether revoking consent to the client's own representation precludes the lawyer from continuing to represent other clients depends on the circumstances, including the nature of the conflict, whether the client revoked consent because of a material change in circumstances, the reasonable expectations of the other client and whether material detriment to the other clients or the lawyer would result.

Consent to Future Conflict

[22] Whether a lawyer may properly request a client to waive conflicts that might arise in the future is subject to the test of paragraph (b). The effectiveness of such waivers is generally determined by the extent to which the client reasonably understands the material risks that the waiver entails. The more comprehensive the explanation of the types of future representations that might arise and the actual and reasonably foreseeable adverse consequences of those representations, the greater the likelihood that the client will have the requisite understanding. Thus, if the client agrees to consent to a particular type of conflict with which the client is already familiar, then the consent ordinarily will be effective with regard to that type of conflict. If the consent is general and open-ended, then the consent ordinarily will be ineffective, because it is not reasonably likely that the client will have understood the material risks involved. On the other hand, if the client is an experienced user of the legal services involved and is reasonably informed regarding the risk that a conflict may arise, such consent is more likely to be effective, particularly if, e.g., the client is independently represented by other counsel in giving consent and the consent is limited to future conflicts unrelated to the subject of the representation. In any case, advance consent cannot be effective if the circumstances that materialize in the future are such as would make the conflict nonconsentable under paragraph (b).

Conflicts in Litigation

[23] Paragraph (b)(3) prohibits representation of opposing parties in the same litigation, regardless of the clients' consent. On the other hand, simultaneous representation of parties whose interests in litigation may conflict, such as co-plaintiffs or co-defendants, is governed by paragraph (a)(2). A conflict may exist by reason of substantial discrepancy in the parties' testimony, incompatibility in positions in relation to an opposing party or the fact that there are substantially different possibilities of settlement of the claims or liabilities in question. Such conflicts can arise in criminal cases as well as in civil cases. The potential for conflict of interest in representing multiple defendants in a criminal case is so grave that ordinarily a lawyer should decline to represent more than one co-defendant. On the other hand, common representation of persons having similar interests in civil litigation is proper if the requirements of paragraph (b) are met.

[24] Ordinarily a lawyer may take inconsistent legal positions in different tribunals at different times on behalf of different clients. The mere fact that advocating a legal position on behalf of one client might create precedent adverse to the interests of a client represented by the lawyer in an unrelated matter does not create a conflict of interest. A conflict of interest exists, however, if there is a significant risk that a lawyer's action on behalf of one client will materially limit the lawyer's effectiveness in representing another client in a different case, for example, when a decision favoring one client will create a precedent likely to seriously weaken the position taken on behalf of the other client. Factors relevant in determining whether the clients need to be advised of the risk include: where the cases are pending, whether the issue is substantive or procedural, the temporal relationship between the matters, the significance of the issue to the immediate and long-term interests of the clients involved and the clients' reasonable expectations in retaining the lawyer. If there is significant risk of material limitation, then absent informed consent of the affected clients, the lawyer must refuse one of the representations or withdraw from one or both matters.

[25] When a lawyer represents or seeks to represent a class of plaintiffs or defendants in a class-action lawsuit, unnamed members of the class are ordinarily not considered to be clients of the lawyer for purposes of applying paragraph (a)(1) of this Rule. Thus, the lawyer does not typically need to get the consent of such a person before representing a client suing the person in an unrelated matter. Similarly, a lawyer seeking to represent an opponent in a class action does not typically need the consent of an unnamed member of the class whom the lawyer represents in an unrelated matter.

Nonlitigation Conflicts

[26] Conflicts of interest under paragraphs (a)(1) and (a)(2) arise in contexts other than litigation. For a discussion of directly adverse conflicts in transactional matters, see Comment [7]. Relevant factors in determining whether there is significant potential for material limitation include the duration and intimacy of the lawyer's relationship with the client or clients involved, the functions being performed by the lawyer, the likelihood that disagreements will arise and the likely prejudice to the client from the conflict. The question is often one of proximity and degree. See Comment [8].

[27] For example, conflict questions may arise in estate planning and estate administration. A lawyer may be called upon to prepare wills for several family members, such as husband and wife, and, depending upon the circumstances, a conflict of interest may be present. In estate administration the

identity of the client may be unclear under the law of a particular jurisdiction. Under one view, the client is the fiduciary; under another view the client is the estate or trust, including its beneficiaries. In order to comply with conflict of interest rules, the lawyer should make clear the lawyer's relationship to the parties involved.

[28] Whether a conflict is consentable depends on the circumstances. For example, lawyer may not represent multiple parties to a negotiation whose interests are fundamentally antagonistic to each other, but common representation is permissible where the clients are generally aligned in interest even though there is some difference in interest among them. Thus, a lawyer may seek to establish or adjust a relationship between clients on an amicable and mutually advantageous basis, for example, in helping to organize a business in which two or more clients are entrepreneurs, working out the financial reorganization of an enterprise in which two or more clients have an interest or arranging a property distribution in settlement of an estate. The lawyer seeks to resolve potentially adverse interests by developing the parties' mutual interests. Otherwise, each party might have to obtain separate representation, with the possibility of incurring additional cost, complication or even litigation. Given these and other relevant factors, the clients may prefer that the lawyer act for all of them.

Special Considerations in Common Representation

[29] In considering whether to represent multiple clients in the same matter, a lawyer should be mindful that if the common representation fails because the potentially adverse interests cannot be reconciled, the result can be additional cost, embarrassment and recrimination. Ordinarily, the lawyer will be forced to withdraw from representing all of the clients if the common representation fails. In some situations, the risk of failure is so great the multiple representation is plainly impossible. For example, a lawyer cannot undertake common representation of clients where contentious litigation or negotiations between them are imminent or contemplated. Moreover, because the lawyer is required to be impartial between commonly represented clients, representation of multiple clients is improper when it is unlikely that impartiality can be maintained. Generally, if the relationship between the parties has already assumed antagonism, the possibility that the clients' interests can be adequately served by common representation is not very good. Other relevant factors are whether the lawyer subsequently will represent both parties on a continuing basis and whether the situation involves creating or terminating a relationship between the parties.

[30] A particularly important factor in determining the appropriateness of common representation is the effect on client-lawyer confidentiality and the attorney-client privilege. With regard to the attorney-client privilege, the prevailing rule is that, as between commonly represented clients, the privilege does not attach. Hence, it must be assumed that if litigation eventuates between the clients, the privilege will not protect any such communications, and the clients should be so advised.

[31] As to the duty of confidentiality, continued common representation will almost certainly be inadequate if one client asks the lawyer not to disclose to the other client information relevant to the common representation. This is so because the lawyer has an equal duty of loyalty to each client, and each client has the right to be informed of anything bearing on the representation that might affect that client's interests and the right to expect that the lawyer will use that information to that client's benefit. See Rule 1.4. The lawyer should, at the outset of the common representation and as part of the

process of obtaining each client's informed consent, advise each client that information will be shared and that the lawyer will have to withdraw if one client decides that some matter material to the representation should be kept from the other. In limited circumstances, it may be appropriate for the lawyer to proceed with the representation when the clients have agreed, after being properly informed, that the lawyer will keep certain information confidential. For example, the lawyer may reasonably conclude that failure to disclose one client's trade secrets to another client will not adversely affect representation involving a joint venture between the clients and agree to keep that information confidential with the informed consent of both clients.

[32] When seeking to establish or adjust a relationship between clients, the lawyer should make clear that the lawyer's role is not that of partisanship normally expected in other circumstances and, thus, that the clients may be required to assume greater responsibility for decisions than when each client is separately represented. Any limitations on the scope of the representation made necessary as a result of the common representation should be fully explained to the clients at the outset of the representation. See Rule 1.2(c).

[33] Subject to the above limitations, each client in the common representation has the right to loyal and diligent representation and the protection of Rule 1.9 concerning the obligations to a former client. The client also has the right to discharge the lawyer as stated in Rule 1.16.

Organizational Clients

[34] A lawyer who represents a corporation or other organization does not, by virtue of that representation, necessarily represent any constituent or affiliated organization, such as parent or subsidiary. See Rule 1.13(a). Thus, the lawyer for an organization is not barred from accepting representation adverse to an affiliate in an unrelated matter, unless the circumstances are such that the affiliate should also be considered a client of the lawyer, there is an understanding between the lawyer and the organizational client that the lawyer will avoid representation adverse to the client's affiliates, or the lawyer's obligations to either the organizational client or the new client are likely to limit materially the lawyer's representation of the other client.

[35] A lawyer for a corporation or other organization who is also a member of its board of directors should determine whether the responsibilities of the two roles may conflict. The lawyer may be called on to advise the corporation in matters involving actions of the directors. Consideration should be given to the frequency with which such situations may arise, the potential intensity of the conflict, the effect of the lawyer's resignation from the board and the possibility of the corporation's obtaining legal advice from another lawyer in such situations. If there is material risk that the dual role will compromise the lawyer's independence of professional judgment, the lawyer should not serve as a director or should cease to act as the corporation's lawyer when conflicts of interest arise. The lawyer should advise the other members of the board that in some circumstances matters discussed at board meetings while the lawyer is present in the capacity of director might not be protected by the attorney-client privilege and that conflict of interest considerations might require the lawyer's recusal as a director or might require the lawyer and the lawyer's firm to decline representation of the corporation in a matter.

CODE OF PROF. RESP. COMPARISON

DR 5-101(A) provides that "Except with the consent of his client after full disclosure, a lawyer shall not accept employment if the exercise of his professional judgment on behalf of his client will be or reasonably may be affected by his own financial, business, property, or personal interests." DR 5-105(A) provides that "A lawyer shall decline proffered employment if the exercise of his independent professional judgment in behalf of a client will be or is likely to be adversely affected by the acceptance of the proffered employment, or if it would be likely to involve him in representing differing interests, except to the extent permitted under DR 5-105(C)." DR 5-105(C) provides that "In the situations covered by DR 5-105(A) and (B), a lawyer may represent multiple clients if it is obvious that he can adequately represent the interest of each and if each consents to the representation after full disclosure of the possible effect of such representation on the exercise of his independent professional judgment on behalf of each." DR 5-107(B) provides that "A lawyer shall not permit a person who recommends, employs, or pays him to render legal services for another to direct or regulate his professional judgment in rendering such services."

Rule 1.7 goes beyond DR 5-105(A) in requiring that, when the lawyer's other interests are involved, not only must the client consent after consultation but also that, independent of such consent, the representation reasonably appears not to be adversely affected by the lawyer's other interests. This requirement appears to be the intended meaning of the provision in DR 5-105(C) that "it is obvious that he can adequately represent" the client, and is implicit in EC 5-2, which states that "A lawyer should not accept proffered employment if his personal interests or desires will, or there is a reasonable possibility that they will, affect adversely the advice to be given or services to be rendered the prospective client."

Notes of Decisions (40)

Rules of Prof. Conduct, Rule 1.7, 42 Pa.C.S.A., PA ST RPC Rule 1.7
Current with amendments received through May 15, 2021.

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A letter to all Nevadans

Xerox is committed to making Nevada Health Link better.

As the contracted vendor for Nevada's health insurance exchange, we recognize and truly regret any challenges you may have encountered when dealing with the system.

Given the importance of getting this right, we're dedicating significant and widespread resources from throughout our company to address the issues most important to you—the customers.

Long wait times for the call center, website errors and other processing delays are unacceptable. As a result, we have brought in hundreds of additional staff over the last few weeks to help solve these issues.

Like you, we want a Nevada Health Link that is easy to access and simple to use. Though every issue won't be solved overnight, we have made steady progress, and we are confident that you will see these improvements continue over the coming days and weeks.

Nevada Health Link has to be a service of which both Xerox and all Nevadans can be proud. We are sincerely dedicated to reaching that goal.

Ursula M. Burns
Chairman and CEO, Xerox Corporation

For more information about our work with Nevada Health Link, go to:
xerox.com/NevadaHealthLink

West's Nevada Revised Statutes Annotated
Constitution of the State of Nevada
Article 6. Judicial Department

N.R.S. Const. Art. 6, § 4

§ 4. Jurisdiction of Supreme Court and court of appeals; appointment of judge to sit for disabled or disqualified justice or judge

Currentness

1. The Supreme Court and the court of appeals have appellate jurisdiction in all civil cases arising in district courts, and also on questions of law alone in all criminal cases in which the offense charged is within the original jurisdiction of the district courts. The Supreme Court shall fix by rule the jurisdiction of the court of appeals and shall provide for the review, where appropriate, of appeals decided by the court of appeals. The Supreme Court and the court of appeals have power to issue writs of *mandamus, certiorari,* prohibition, *quo warranto* and *habeas corpus* and also all writs necessary or proper to the complete exercise of their jurisdiction. Each justice of the Supreme Court and judge of the court of appeals may issue writs of *habeas corpus* to any part of the State, upon petition by, or on behalf of, any person held in actual custody in this State and may make such writs returnable before the issuing justice or judge or the court of which the justice or judge is a member, or before any district court in the State or any judge of a district court.

2. In case of the disability or disqualification, for any cause, of a justice of the Supreme Court, the Governor may designate a judge of the court of appeals or a district judge to sit in the place of the disqualified or disabled justice. The judge designated by the Governor is entitled to receive his actual expense of travel and otherwise while sitting in the supreme court.

3. In the case of the disability or disqualification, for any cause, of a judge of the court of appeals, the Governor may designate a district judge to sit in the place of the disabled or disqualified judge. The judge whom the Governor designates is entitled to receive his actual expense of travel and otherwise while sitting in the court of appeals.

Credits

Approved and ratified 1864. Amended 1920, 1976, 1978, 2014.

Notes of Decisions (142)

§ 4. Jurisdiction of Supreme Court and court of appeals;..., NV CONST Art. 6, § 4

N. R. S. Const. Art. 6, § 4, NV CONST Art. 6, § 4
Current through legislation of the 81st Regular Session (2021) effective as of May 26, 2021. Some sections effective July 1, 2021 are also available; see effective date in individual sections. Text subject to revision and classification by the Legislative Counsel Bureau

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§ 96.01 History of Insurance Insolvency

[1] State Insurance Receivership Laws

Insurer receiverships are governed under state insurance receivership laws rather than the Bankruptcy Code. *Section 109(b) of the Bankruptcy Code* expressly exempts a domestic insurance company from being a debtor under the Bankruptcy Code.[1] Insurers have been excluded as debtors under federal bankruptcy law since the enactment of the Federal Bankruptcy Act of 1898 ("the 1898 Act"), which was the first modern bankruptcy act.[2] Prior to the 1898 Act, insurers were subject to bankruptcy laws.[3] Courts interpreting Congress' reasons for

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Updates by Stephen Pate, a Member of Cozen O'Connor in Houston, Texas.

[1] **US—***11 U.S.C. § 109(b)*.

See also **US/IL—***In the Matter of Estate of MedCare HMO, 998 F.2d 436 (7th Cir. 1993)*; *In re Auto. Prof'ls, Inc. 370 B.R. 161 (Bankr. N.D. Ill. 2007)*.

[2] **US/WV—***Sims v. Fid. Assurance Ass'n, 129 F.2d 442, 448 (4th Cir. 1942)*, *aff'd*, *318 U.S. 608 (1943)*.

See also **US/GA—*In re Supreme Lodge of the Masons Annuity, 286 F. 180, 184 (N.D. Ga. 1923)***.

[3] **US/WV—***Sims v. Fid. Assurance Ass'n, 129 F.2d 442, 448 (4th Cir. 1942)*, *aff'd*, *318 U.S. 608 (1943)*.

exempting insurers from the 1898 Act indicated that because insurers are affected with a public interest and are regulated by state regulators possessing specialized knowledge and insurance expertise, insurer insolvencies are better handled by state insurance receivers than by bankruptcy trustees.[4]

For over a century, insurer insolvencies have been governed under state law. In 1967, Wisconsin enacted the first comprehensive insurance receivership statute, which was largely based upon the 1898 Act.[5] Shortly thereafter, the National Association of Insurance Commissioners ("NAIC") decided to use the Wisconsin Act as the model for the NAIC Insurer Receivership Model Act, which over time has been enacted in one form or another in most states.[6] A majority of states enacted a form of the 1995 NAIC Insurer Receivership Model Act (or its predecessor) but only a few states have enacted the 2007 NAIC Insurer Receivership Model Act, which is based in part on the current Bankruptcy Code. Consequently, in interpreting state insurance receivership laws, one is more informed by reviewing the 1898 Act than the current Bankruptcy Code. The current Bankruptcy Code was enacted in 1978 and substantially overhauled the prior act.

Cross References:

The various provisions of NAIC's Insurer Receiver Model Act are analyzed throughout Chapters 98, 99, and 100.

In the late 1960s, following several large property and casualty insurance insolvencies, the states began to establish guaranty associations to provide a safety net to protect the policyholders of insolvent insurers.[7] During the 1970s, the NAIC created the property and casualty and life and health guaranty association model acts, which the states began to enact in one form or another.[8]

Today, insurance receivers and the state guaranty associations work together to ensure the prompt payment of policyholder claims while the receiver marshals and distributes the assets of the insolvent insurer. Together, they form a comprehensive system for protecting policyholders from the often devastating harm resulting from insurer insolvencies.

Historically, insurer receiverships occurred due to downturns in the economy, inadequate pricing and reserving, rapid expansion or mismanagement. Prior to the 1980s, insurance insolvencies tended to be smaller, single state insurers. The decade between the mid-1980s and the mid-1990s saw a significant number of large or multi-state insurer insolvencies. In February 1990, Representative John Dingell of Michigan chaired a congressional committee that investigated a handful of large insurance insolvencies and produced a report called "Failed Promises: Insurance Company Insolvencies."[9] The report highlighted several factors contributing to the large insolvencies, including, a failure of state regulation.[10]

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[4] **US/WV—***Sims v. Fid. Assurance Ass'n, 129 F.2d 442, 449 (4th Cir. 1942)*, *aff'd*, *318 U.S. 608 (1943)*.

[5] REFERENCE HANDBOOK ON INSURANCE COMPANY INSOLVENCY, THIRD EDITION, p. 53 (Am. Bar. Ass'n Tort and Insurance Practice Section 1993). *See also* Wisconsin Senate Bill 303 (Aug. 4, 1967).

[6] REFERENCE HANDBOOK ON INSURANCE COMPANY INSOLVENCY, THIRD EDITION, p. 53 (Am. Bar. Ass'n Tort and Insurance Practice Section 1993).

[7] *http://www.westernguarantyfundservices.org/index.php/insurance-guaranty-associations*; *http://www.westernguarantyfundservices.org/index.php/faqs*.

[8] *http://www.westernguarantyfundservices.org/index.php/insurance-guaranty-associations*.

[9] "Failed Promises: Insurance Company Insolvencies," Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce, U.S. House of Representatives (Feb. 1990).

[10] "Failed Promises: Insurance Company Insolvencies," Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce, U.S. House of Representatives (Feb. 1990).

The NAIC ultimately responded to the report by initiating a number of reforms, including: adopting Risk-Based Capital Laws; adopting accreditation standards for departments of insurance; and creating a host of tools used by regulators to measure and monitor financial solvency). For example, the NAIC Insurance Regulatory Information System ("IRIS") identifies troubled insurers through a review of annual financial statements and examinations that assist in the measurement of the insurer's financial strength. The Financial Analysis Solvency Tools ("FAST") Scoring System assists regulators in determining which insurers should be reviewed as priorities because such insurers are considered to be "nationally significant" insurers writing premium in excess of certain thresholds. The higher the FAST score, the more immediate the review.

Cross References:

For further discussions of Risk-Based Capital Laws, see *Section 14.03* above; of IRIS Ratios, see *Section 14.04[3]*, of the Fast Scoring System, see *Section 14.04[4]*, and of early warning systems, see *Section 14.04[13]*, above.

Since the 1990s, the number of insolvencies has significantly decreased due to improved solvency regulation. Liquidations have diminished and rehabilitations and supervised run offs are more common. Today, regulators are more open to attempting to rehabilitate insurers than in the past, due in large part to early regulatory intervention, which provides a much better chance of the insurer's survival. Ultimately, the goal of conservation and rehabilitation is to protect the policyholders by ascertaining and managing the insurer's financial condition to afford payment of all of the policyholders' claims over time employing statutory receivership protections. Unfortunately, there likely will always be liquidations in those instances where bad actors have succeeded in mismanaging, stealing or looting an insurer's assets in such a way as to avoid detection by regulators until it is too late.

Cross References:

The regulation of insolvencies is discussed in *Chapter 98* below. Receiverships are discussed in *Chapter 99* below. The rehabilitation of insurer is discussed in *Chapter 100* below. The liquidation of insurance companies is discussed in *Chapter 101* below. The consequences of insurer insolvency are discussed in *Chapter 102* below. The special cases of insolvent foreign and multinational insurers are discussed in *Chapter 103* below. Case studies of insurer insolvencies are examined in *Chapter 104 below*.

[2] Relationship to Bankruptcy Law

Two of the most significant differences between bankruptcy and state insurance receivership are the court venues and the priorities of distributions to creditors. Typically, insurance receiverships are conducted in state chancery courts, while bankruptcies are before the Federal bankruptcy courts.[11] Additionally, state insurance receivership laws afford a higher level of priority to the claims of policyholders and insureds over those of most other creditors.[12] Generally, because insurance is affected with a public purpose and enforced through the

[11] *See, e.g.:*

US—*11 U.S.C. §§ 301*, *303*;

IL—*215 Ill. Comp. Stat. 5/188.1*, *5/189*, *5/190*.

[12] *See, e.g.:*

state's police powers, policyholders are treated more favorably than other unsecured creditors.[13] Bankruptcy law distinguishes between secured and unsecured creditors and does not afford favorable treatment to policyholders.[14]

Cross References:

For comprehensive discussion of the relationship of bankruptcy to insurance enterprises, see *Chapter 107* below. The effect of insurance as an asset in the bankruptcy estate is discussed in *Chapter 108* below. The impact of bankruptcy on insurance matters is discussed in *Chapter 109* below.

Chapter 110 below concludes this volume on insolvency and bankruptcy. It analyzes bankruptcy issues that arise in specific kinds of insurance, such as directors' and officers' insurance and professional liability insurance. It further addresses three specific types of bankruptcy cases and the insurance issues they have generated: law firm, automotive and asbestos cases. In addition, it analyzes three types of issues that often arise in general bankruptcy cases: environmental, self-insurance and arbitration.

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FL—*Fla. Stat. Ann. § 631.271*;

IL—*215 Ill. Comp. Stat. 5/205*.

[13] **US—***Paul v. Virginia, 75 U.S. 168, 183–185 (1869)*, *overruled on other grounds* by *Humana Inc. v. Forsyth, 525 U.S. 299 (1999)*.

[14] **US—***11 U.S.C. §§ 506*, ***507***.