American Bankruptcy Institute Law Review

Volume 7 Number 1 Spring 1999

NOTE: THE DISINTERESTED STANDARD OF SECTION 327(a): APPLYING AN EQUITABLE SOLUTION FOR POTENTIAL CONFLICTS IN SMALL BANKRUPTCIES

Introduction

Section 327 of the Bankruptcy Code [1] is designed to protect debtors from employing attorneys whose own interests conflict with the interests of the bankruptcy estate. Unfortunately, the ambiguous statutory framework of section 327 does not provide adequate guidance to evaluate conflicts of interest in chapter 11 cases. Thus, courts are unable to apply section 327(a) uniformly when determining whether "actual" or "potential" conflicts should disqualify an attorney from representing the bankruptcy estate or parties relating thereto. Although a goal of section 327 is to protect debtors, the application of this provision may harm debtors who operate small business entities. In such cases, disqualification of the attorney may impose a greater financial burden than in large bankruptcies.

Part I of this Note discusses the traditional ethical codes of conduct and their shortcomings relating to conflicts of interest in bankruptcy. In Part II, this Note will analyze the statutory framework of section 327 concerning the employment of attorneys by the estate or parties relating thereto. Part III discusses the manner in which courts apply section 327(a) and the Model Code of Professional Responsibility to "actual" and "potential" conflicts of interest. Lastly, in Part IV, this Note suggests a *per se* disqualification approach for actual and potential conflicts in large chapter 11 cases in order to reconcile the varying applications of section 327(a) by the courts and proposes a new disinterested standard for attorneys representing parties in small bankruptcies.

I. Traditional Ethical Codes of Conduct as Applied in Bankruptcy

The Model Code of Professional Responsibility (the "Model Code") [2] and the Model Rules of Professional Conduct (the "Model Rules") [3] are considered ineffective in bankruptcy proceedings. [4] Conflicts of interest often arise in bankruptcy cases because multiple parties compete for access to a minimal amount of assets. [5] The Model Code and the Model Rules are suggestive guidelines and are inadequate in bankruptcy because they are overly broad and do not provide attorneys with guidance as to whether a particular conflict of interest requires disqualification. Thus, attorneys faced with potential conflicts must either discontinue employment, run the risk of having their fees disgorged, or be disqualified later without receiving payment for services rendered.

A. The Model Code of Professional Responsibility

The Model Code, which is comprised of the Canons, Ethical Considerations, and Disciplinary Rules, [6] provides professional ethical standards for practicing attorneys. The Canons [7] are suggestive guidelines for courts to use in evaluating an attorney's standard of conduct with respect to conflicts of interest. [8] Ethical Considerations are also suggestive guidelines [9] and "represent the objectives toward which every member of the profession should strive." [10] The Disciplinary Rules are mandatory standards that provide "minimum levels of conduct, the violation of which subjects the lawyer to disciplinary action." [11] Taken in its entirety, the Model Code does not provide a clear standard for conflicts of interest because it combines enforceable rules with unenforceable goals. [12] This confusing standard led to the abandonment of the Model Code, [13]

which was replaced by the Model Rules of Professional Conduct. [14]

B. The Model Rules of Professional Conduct

The American Bar Association adopted the Model Rules in 1983. [15] The Model Rules consist of both mandatory and permissive guidelines for ethical standards of professional conduct. [16] The Model Rules are designed to govern conflicts of interest stemming from client confidentiality, disclosure and disinterestedness. [17] One such rule commonly applied in bankruptcy cases is Model Rule 1.7(b). [18]

Model Rule 1.7(b) provides a two−part test which disqualifies counsel in cases where the estate's representation is or may be "materially limited by the lawyer's responsibilities to another client or to a third person, or by the lawyer's own interest." [19] However, an attorney is permitted to represent a client if the attorney "reasonably believes that the representation will not be adversely affected," and the "client consents after consultation." [20] Although the Model Rules combine these two factors and improve upon the Model Code, it is still inadequate for bankruptcy. [21] Attorneys find it difficult to determine which potential risks are temporary, minimal, or may never materialize, [22] and thus run the risk of disqualification after services have been rendered without receiving adequate compensation.

II. The Ethical Statutory Framework of the Bankruptcy Code

The Bankruptcy Code (the "Code") provides ethical guidelines for professionals, including attorneys, employed by the estate or parties relating thereto with conflicts of interest. [23] However, the Code's stringent requirements are inadequate because the ethical standards are ambiguous and the statutory framework is complex. [24] The statutory framework is comprised of sections 327(a) and 101(14) which, when considered together, create uncertainty in determining whether an attorney is disinterested. [25]

Section 327(a) sets forth a two−prong test for counsel retained by a trustee or debtor−in−possession. [26] The two−prong test requires that a trustee or debtor−in−possession [27] employ attorneys who (1) "do not hold or represent an interest adverse to the estate" and (2) are "disinterested." [28] Congress enacted section 327(a) to hold attorneys involved in the administration of the bankruptcy estate to strict ethical standards. [29]

Generally, the purpose of section 327(a) is to preclude a debtor from retaining a particular attorney in cases where the interest of such attorney is clearly adverse to the interest of the estate. [30] Section 327(a) also protects the bankruptcy estate by requiring prior court approval for the appointment of attorneys to guarantee that attorneys act with "undivided loyalty and exclusive allegiance," and that the fiduciary duty to the estate is "not compromised or eroded." [31] This section ensures that the retention of the attorney is necessary for the proper administration and management of the estate, and requires termination of employment that is considered unnecessary. [32]

Despite these safeguards, section 327(a) does not effectively protect the bankruptcy estate. The first prong of section 327(a) contains the term "adverse interest," yet the Code does not provide a definition. [33] Thus, courts have had the task of defining this term. The majority of courts follow *In re Roberts* [34] and define an "adverse interest" as any "economic interest" that negatively affects the estate or related parties, "thus creating either an actual or potential dispute," or "a predisposition or interest under circumstances that render such a bias" against the estate. [35]

The second prong of section 327(a) contains a "disinterested" standard, [36] which is defined by the Code in section 101(14). [37] Section 101(14)(E) defines a disinterested person as one who "does not have an interest materially adverse to the interest of the estate." [38] This "catch−all" phrase may disqualify any attorney with a remote interest in the estate, even though such interest would not affect the attorney's impartial advice and motivation. [39] Some courts interpret section 101(14)(E) to disqualify counsel representing the estate or related parties for both actual and potential conflicts of interest. [40] Yet, other courts apply a more permissive approach and only disqualify attorneys for actual conflicts of interest. [41]

As discussed, the definition of a "disinterested person" in section 101(14)(E) contains the same "adverse interest" requirement provided in the first prong of section 327(a). [42] However, the adverse interest requirement of section 101(14)(E) is less restrictive because it is modified by the term "materially." [43] Thus, an attorney who fails the disinterested requirement of section 101(14)(E) automatically fails the "no adverse interest" prong of section 327(a), whereas the reverse is not true. [44] As a result of the ambiguous terms and the differing use of this phrase within both provisions, courts have difficulty in determining whether to apply an adverse interest standard or to disqualify professionals who hold materially adverse interests. [45]

Most courts hold that the overlapping requirements of section 327(a) establish a one−prong test, and evaluate conflicts of interest under the disinterested standard of section 101(14)(E). [46] However, the National Bankruptcy Review Commission (the "Commission") recently adopted a strict disinterested standard [47] stating that an attorney is required to "show a lack of *any* interest adverse to the estate, *regardless* of materiality." [48] The Commission reasoned that a strict disinterested standard is necessary "in light of the unique nature of the bankruptcy process…to preserve public and judicial confidence in the bankruptcy system" [49] and to ensure that "ethical standards for bankruptcy practice [are] consistent with state ethical rules." [50]

III. Differing Views on the Types of Conflicts that Disqualify − Actual vs. Potential

Conflicts of interest are common in bankruptcy cases because the debtor's attorney may also have a fiduciary duty to another party whose interests conflict with that of the estate. [51] As a result of the various situations where conflicts may arise, courts are unable to formulate a universal standard to determine whether a specific conflict requires disqualification. [52] Thus, courts differ as to whether attorneys should be disqualified for only "actual" [53] conflicts rather than "potential" conflicts, [54] which do not presently exist but may in some circumstances become "actual." [55]

The differing views stem from the confusion surrounding section 327(c), [56] which mandates disqualification for "actual" conflicts resulting from an attorney representing both the bankruptcy estate and creditor. [57] Some courts rely on the term "actual" in section 327(c) to distinguish actual from potential conflicts of interest. [58] The distinction recognized between such conflicts has resulted in various interpretations concerning the character of conflict necessary for disqualification. [59] Some courts find that only actual conflicts of interest require disqualification. [60] Other courts recognize that potential conflicts may in some instances warrant disqualification but reject a *per se* rule for disqualification. [61] Under this line of cases, some courts [62] hold that a potential conflict is disqualifying *unless* (i) every competent attorney is already employed in the bankruptcy case; [63] or (ii) there is a slight chance that the potential conflict will become actual, and the necessity for the attorney's employment is compelling. [64] Lastly, numerous cases support a *per se* rule disqualifying attorneys for both actual and potential conflicts. [65]

A. Only Actual Conflicts of Interest Disqualify

Some courts interpret section 327(a) to disqualify employment only in cases where an actual conflict of interest exists. [66] For example, the court in *H & K Developers v. Waterfall Village of Atlanta, Ltd.* (*In re Waterfall Village of Atlanta, Ltd.*) [67] adopted a two−prong test [68] that was derived from the court's interpretation of Canon Nine of the Model Code, which states "[a] lawyer should avoid even the appearance of professional impropriety." [69] This test asks whether an actual conflict is present, and, if so, whether "public suspicion" caused by the conflict outweighs the interest of counsel in continuing with the representation of the debtor. [70] The *Waterfall* court found that a potential conflict existed and did not to proceed to the second prong of the test. [71] In effect, the court held that potential conflicts of interest do not require disqualification. [72] Also, the court in *In re Global Marine, Inc.*, [73] found that potential conflicts do not warrant disqualification. [74] The court concluded that "dormant" conflicts should be addressed when they materialize, rather than as a "pre−emptive" strike [75] because premature disqualification for potential conflicts would only result in unnecessary cost to the estate and further delay in the bankruptcy process. [76]

B. Potential Conflicts May Disqualify But Only in Some Circumstances

Some courts interpret section 327(a) to disqualify attorneys in certain cases where potential conflicts of interest exist. [77] However, courts in favor of this approach have refused to adopt a *per se* disqualification rule for potential conflicts. [78] In *In re Martin*, [79] the First Circuit held that actual conflicts require disqualification, yet potential conflicts alone do not warrant the same result. [80] The court stated that "horrible imaginings alone cannot be allowed to carry the day. Not every conceivable conflict must result in sending counsel away to lick his wounds." [81] Refusing to apply a *per se* disqualification rule for potential conflicts, the *Martin* court adopted a "balancing test." [82] The "balancing test" weighs various factors including (1) whether the arrangement is "reasonable;" (2) whether the parties have acted in "good faith;" (3) whether the arrangement is necessary for retaining "competent counsel;" and (4) the likelihood that the potential conflict will become an actual conflict. [83] The court reasoned that potential conflicts are merely factors in support of disqualification and do not necessarily nullify the attorney's appointment. [84]

Other courts addressing potential conflicts have applied a rebuttable presumption in favor of disqualification. [85] For example, the court in *In re BH & P, Inc.*, [86] held that a conflict can only overcome disqualification if: (1) the conflict is potential; [87] (2) the possibility of the conflict becoming actual is "remote;" [88] (3) the employment of the attorney is "compelling;" [89] and (4) another attorney could not adequately manage the case. [90] However, the court did not apply these factors because the conflict was considered actual. [91] On appeal, the Third Circuit reaffirmed the bankruptcy court's assertion that courts have the discretion to disqualify counsel for potential conflicts. [92]

C. Disqualifying for Both Actual and Potential Conflicts of Interest

A third line of cases disqualify attorneys for both actual and potential conflicts in accordance with Canon Nine of the Model Code. [93] Under this approach, courts hold that both types of conflicts require a *per se* rule in favor of disqualification based on the "appearance of impropriety." [94] In *Roger J. Au & Son, Inc. v. Aetna Insurance Co. (In re Roger J. Au & Son, Inc.)*, [95] the court disqualified an attorney for a potential conflict of interest where the attorney represented both the corporate debtor and the debtor's shareholder and principal officer. [96] The court reasoned that the possibility of a "shift in loyalty" and debtor's shareholder and principal officer furthering their own interests at the expense of the estate, violated both the "appearance of impropriety" standard of Canon Nine and the "disinterested" requirement of section 327(a). [97]

Subsequently, the court in *In re Kendavis Industries International, Inc.*, [98] addressed the applicability of section 327(a) to potential conflicts. [99] In interpreting section 327(a), the *Kendavis* court adopted an even narrower approach than the court in *Roger J. Au.* [100] The *Kendavis* court asserted that there is no such thing as a "potential conflict" and that the concept is a "contradiction in terms." [101] The court added that the "disinterested" requirement forbids the "appearance of impropriety" and that an attorney should be free from any personal interest that affects fair and impartial representation. [102] Under this analysis, an attorney will be held to have violated section 327(a) upon the commencement of the dual representation. [103]

IV. Proposed Model to Apply Section 327(A) in Large and Small Bankruptcies

This Note agrees with the courts' rationales in *In re Roger J. Au* and *In re Kendavis* which find that both actual and potential conflicts create an "appearance of impropriety" and violate section 327(a). [104] However, with regard to potential conflicts of interest, it is believed that a *per se* disqualification rule should only apply to attorneys representing large chapter 11 cases; whereas in small bankruptcies, potential conflicts should be evaluated in terms of equity and fairness. [105] This Note suggests that courts have the discretionary power to adopt an equitable solution for small bankruptcies pursuant to section 105 of the Code. [106] As in the case of *In re Martin*, [107] this evaluation should be fact−specific and factors in favor of disqualification should be weighed similarly to the "balancing test" applied in *In re BH & P*. [108] Finally, this Note proposes a set of factors for courts' consideration in weighing the equities to ensure that the goals of bankruptcy are equally

afforded to all chapter 11 debtors.

A. The Distinction Between Large and Small Bankruptcies

The Bankruptcy Reform Act of 1994 adopted a fast track approach for "small business "debtors to "enhance and preserve the value in the debtor's estate, reduce administrative costs, cut back on professional fees, and expedite the reorganization to a speedy and definitive conclusion." [109] A "small business" debtor, as defined in section 101(51C) of the Code [110] is "a person engaged in commercial or business activities . . . whose aggregate non−contingent liquidated secured and unsecured debts as of the date of the petition do not exceed $2,000,000." [111] Consistent with the rationale for a fast track approach, this Note suggests that courts use section 101(51C) to determine whether a bankruptcy is "small," thus deserving enhanced rights.

B. Maintaining a Strict Disinterested Standard for Large Bankruptcies

This Note supports the *per se* disqualification rule for actual conflicts in accordance with section 327(a), as such conflicts necessarily satisfy both the adverse interest and disinterested requirements. [112] Similarly, this Note proposes a *per se* disqualification for potential conflicts in large bankruptcies. [113] In accordance with the rationales advanced in *In re Kendavis* and *In re Roger J. Au*, this Note suggests the adoption of the "appearance of impropriety" standard of Canon Nine to determine whether a potential conflict should result in disqualification. [114] Although the strict "appearance of impropriety" standard will disqualify a significant number of representation arrangements, disqualification at the commencement of the case will decrease the likelihood of harm to the bankruptcy estate. [115]

This Note proposes that potential conflicts in large chapter 11 cases be held to Canon Nine's strict standard because such debtors often have access to a greater amount of assets, which may lessen the economic sting caused by requiring debtors to retain new counsel. [116] Furthermore, a strict disinterested standard, as adopted by the Commission, "prevent[s] even the emergence of a conflict" to guarantee that the interest of the estate is not compromised. [117] This standard for large bankruptcies protects both the estate and its creditors from the many types of conflicts which may arise from the multitude of parties, the greater amount of capital at stake, and the complexity of the business infrastructure. [118]

Further, this Note suggests that rather than waiting for a potential conflict to materialize into an actual conflict, it is more efficient to disqualify counsel at the beginning of the case. [119] This will ensure that debtors do not incur greater costs at the expense of the estate, by having their attorneys disqualified at a later point in the administration of the estate. [120] In such complex cases, the added costs and delay in acquainting a new attorney with the intricacies of the case do not warrant courts to stray from the express language of section 327(a) and traditional codes of ethics. [121] Also, placing the disqualification process for potential conflicts on hold in order to see if such conflicts become actual only frustrates the goals of bankruptcy by delaying disqualification. [122] This Note proposes that disqualification for both actual and potential conflicts of interest will resolve the inconsistent standards of review for disqualification of attorneys by providing a uniform standard for applying section 327(a) with respect to large bankruptcies.

C. Balancing the Equities in Small Chapter 11 Cases for Potential Conflicts

In small chapter 11 cases, this Note supports section 327(a)'s *per se* disqualification rule for actual conflicts to guarantee that the interest of the estate is not adversely affected. [123] In contrast, potential conflicts of interest should not be deemed *per se* disqualifying, [124] but rather, courts should use their discretionary power under section 105 of the Code [125] to provide equitable relief for debtors in particular circumstances. [126]

Section 105 provides courts with the discretionary power to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." [127] Courts are split on the issue of whether section 105 provides courts with the authority to deviate from requirements set forth in section 327(a). [128] Some courts have held that section 105 does not allow for the dilution of section 327(a). [129] In *Childress v. Middleton Arms, Ltd. Partnership (In re Middleton Arms, Ltd. Partnership)*, [130] the court reasoned that

bankruptcy courts "cannot use equitable principles to disregard unambiguous statutory language" and "whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code." [131] Other courts have held that the requirements of section 327(a) may be modified in cases where the interest of the estate is best served. [132] For example, in *United States Trustee v. PHM Credit Corp. (In re PHM Credit Corp.)*, [133] the court held that a bankruptcy judge may adopt "curative measures" if the employment is "important to the case's resolution, no actual impropriety or harm was alleged or shown," and the bankruptcy judge "carefully" balanced all competing interests. [134] This Note agrees with the latter view, and suggests that courts addressing potential conflicts in small bankruptcies have the authority under section 105 to dilute the disinterested standard of section 327(a). Courts should use this authority in small chapter 11 cases to "carry out" [135] the goals of bankruptcy [136] because such goals would be adversely affected if debtors were required to incur additional costs for finding new counsel for potential conflicts that will never materialize. [137]

Courts should use their discretionary power to adopt an equitable solution for potential conflicts in small bankruptcies because of the managerial and economic structure of small business entities. [138] Such entities often do not have the multitude of parties competing for the same assets, as encountered with large bankruptcies, thus potential conflicts seem less likely to turn into actual conflicts. [139] Also, because small bankruptcies are often not as complex as large chapter 11 cases, courts are able to oversee the managerial process, the economic issues, and the potential effect that a conflict may have on the administration of the estate. [140] As in the case of *In re Lee*, [141] the court used its discretionary power to adopt a less drastic approach for an attorney employed in a small bankruptcy. [142] Rather than disqualify the attorney from simultaneously representing both the corporate debtor and its sole shareholders, the court permitted the attorney to represent only one of the debtors. Thus, the *Lee* court seemed to have recognized that small business debtors may require special treatment in certain circumstances. [143]

In deciding whether to disqualify counsel for potential conflicts in small bankruptcies, this Note proposes a balancing test, and suggests a set of factors for courts' consideration. Courts should assess whether the potential conflict falls under the "materially adverse" standard of section 101(14)(E). As in the case of *In re Martin*, courts should apply a balancing test and determine whether the conflict is material. [144] Courts should then evaluate the adverse impact disqualification will have on the estate, as compared to allowing the representation to continue. [145] This proposed balancing test for potential conflicts should be tailored to the specific facts at issue [146] and judges, with their "experience, common sense, and knowledge," [147] should determine whether an attorney's disqualification will cause the estate to suffer undue delay and/or incur additional debt.

Courts have used different factors for evaluating potential conflicts. This Note combines these efforts to create helpful guidelines for judges and attorneys to determine disqualification for potential conflicts in small bankruptcies. In line with the court in *In re BH & P, Inc.*, [148] this Note suggests various factors including: (1) the entity's ability to reorganize the debt and maximize the return to creditors; [149] (2) the economic effect and delay caused by the retention of a new attorney at the onset as compared with allowing counsel to continue representation; [150] (3) the likelihood, whether more probable than not, that the conflict will materialize into an actual conflict; [151] (4) fairness and equity of the result; [152] and (5) the need for familiar counsel to continue representing the estate to enable the debtor to obtain a fresh start. [153] These proposed factors for evaluating potential conflicts are only suggestive guidelines for courts to consider and are "not designed to be all−inclusive." [154]

Additionally, this Note suggests that after the proposed balancing test is applied to a potential conflict, attorneys involved in the case should file with the court periodic statements concerning the status of the conflict. Such periodic disclosure statements will enable courts to evaluate the potential conflict in subsequent stages of the case to determine whether it has materialized into an actual conflict, thus requiring disqualification.

V. Conclusion

The purpose of section 327(a) of the Code is to ensure that debtors in pursuit of a fresh start are not manipulated by attorneys with interests adverse to the estate. Section 327(a) however, does not provide the bankruptcy courts with adequate guidance in dealing with the many complex issues that arise in the bankruptcy process. Consequently, courts have differed in the application of section 327(a) to conflicts of interest, thus failing to provide attorneys with proper guidelines for determining the types of conflicts that result in disqualification.

In light of the ambiguous statutory framework and inconsistent application of section 327(a), attorneys should be on guard that detecting conflicts of interest is similar to a "soldier on a minefield." [155] As a result of the apparent difficulty in detecting conflicts, this proposal will provide courts and attorneys with insight in determining disqualification in large and small chapter 11 cases.

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FOOTNOTES:

[1] *See* 11 U.S.C. § 327(a) (1994).

> 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.Back To Text

[2] Model Code of Professional Responsibility (1980) [hereinafter Model Code] (stating Model Code became effective in 1970); Regina Stango Kelbon et al., *Conflicts, The Appointment of "Professionals," and Fiduciary Duties of Major Parties in* Chapter 11, 8 Bankr. Dev. J. 349, 354 (1991) (noting that American Bar Association [hereinafter ABA] adopted Model Code in 1969); Nancy B. Rapoport, *Turning and Turning in the Widening Gyre: The Problem of Potential Conflicts of Interest in* Bankruptcy, 26 Conn. L. Rev. 913, 941 (1994) (stating ABA originally adopted Model Code in 1969, which became effective January 1, 1970).Back To Text

[3] Model Rules of Professional Conduct (1983) [hereinafter Model Rules] (providing standards of conduct for attorneys).Back To Text

[4] *See* Charles F. Cowley et al., *Employment of Professionals in* Bankruptcy Cases: A Practitioner's Guide, 31 Beverly Hills B.A. J. 61, 62 (1996) (discussing difficulties in applying Model Rules to bankruptcy cases because courts do not apply uniform approach to conflicts of interest); Peter E. Meltzer, *Whom Do You Trust?* Everything You Never Wanted To Know About Ethics, Conflicts and Privileges in the Bankruptcy Process, 97 Com. L.J. 149, 150 (1992) (stating Model Rules are not easily applied in bankruptcy because of multiple interests and parties).Back To Text

[5] *See* Marcia L. Goldstein et al., *Ethical Considerations For Bankruptcy Professionals: Disinterestedness, Conflicts of Interest, and Retainers*, C995 ALI−ABA 397, 399 (1995) (discussing how competing interests are intensified in multi−debtor cases); Robert J. Landry, III & James R. Higdon, *Ethical Considerations in* Appointment and Compensation of An Attorney for a Chapter 11 Debtor−in−Possession, 66 Miss. L.J. 355, 355 (1996) (describing parties involved in chapter 11 cases, including debtors, trustees, examiners and committees of equity security holders or creditors); Meltzer, supra note 4, at 150 (stating that multiple parties hold various interests which result in representation conflicts in bankruptcy).Back To Text

[6] *See* In re Glenn Elec. Sales Corp., 99 B.R. 596, 598 (Bankr. D.N.J. 1988) (noting Rules and Canons provide guidance in determining whether conflicts of interest exist in bankruptcy cases); In re Star Broad. Inc., 81

B.R. 835, 839 (Bankr. D.N.J. 1988) (stating Rules and Canons govern conduct of bar members practicing in federal courts); Rapoport, supra note 2, at 941 (observing Canons, Ethical Considerations and Disciplinary Rules are designed to guide attorneys in maintaining high ethical standards).Back To Text

[7] Three Canons often referred to include: Canon 4 which states: "A lawyer should preserve the confidences and secrets of a client;" Canon 5 which states: "A lawyer should exercise independent professional judgment on behalf of a client;" Canon 9 which states: "A lawyer should avoid even the appearance of professional impropriety." Model Code, supra note 2.Back To Text

[8] *See* Cowley, *supra* note 4, at 62 (stating that only Disciplinary Rules are mandatory, and Canons and Ethical Considerations are permissive guidelines); Rapoport, supra note 2, at 941 (providing that Canons and Ethical Considerations are not enforceable rules and only assist in interpretation of Disciplinary Rules which, if violated, require disciplinary actions against attorney); John D. Ayer, *The Responsibilities of the Lawyer in Bankruptcy Case*, Norton Bankr. L & Prac. Monograph No. 1 19, 58−59 (1988) (noting that Disciplinary Rules are mandatory). Back To Text

[9] *See* supra note 8 and accompanying text (discussing how Ethical Considerations, like Canons, are only suggestive guidelines and are not considered mandatory rules by courts).Back To Text

[10] Model Code of Professional Responsibility, Preliminary Statement (1981). *See* In re Consupak, Inc., 87 B.R. 529, 550 n.16 (Bankr. N.D. Ill. 1988) (quoting Preliminary Statement of Model Code); Frank v. Ducy, 1986 WL 1964, at *3 n.1 (N.D. Ill. 1986) (stating Ethical Considerations "are aspirational; they only provide guidance").Back To Text

[11] Frank, 1986 WL 1964, at *3 n.1. *See* H. Lowell Brown, *The Dilemma of Corporate Counsel Faced with Client Misconduct: Disclosure of Client Confidences or Constructive Discharge*, 44 Buff. L. Rev. 777, 795 n.62 (1996) (stating that Disciplinary Rules set forth minimum level of conduct for attorney, which if violated, subjects attorney to disciplinary action); Larry Schafer, Comment, Attorney and Client: Duty to Report Lawyer Misconduct, 67 N.D. L. Rev. 359, 362 (1991) (stating Disciplinary Rules "serve as guidelines for the minimum level of conduct a lawyer cannot fall below").Back To Text

[12] *See* supra note 8 and accompanying text (comparing permissive nature of Canons and Ethical Considerations with mandatory components of Disciplinary Rules).Back To Text

[13] *See* Joseph W. deFuria, Jr., A Matter of Ethics Ignored: The Attorney−Draftsman as Testamentary Fiduciary, 36 U. Kan. L. Rev. 275, 292 (1988) (noting that tripartite structure of Model Code, which is comprised of Canons, Ethical Considerations and Disciplinary Rules, did not hold up well when applied in practice); Hon. Abraham J. Gafni, Foreword: The Model Rules − A Practitioner's Guide to Avoiding Malpractice, 61 Temp. L. Rev. 1045, 1046 (1988) (criticizing both content and tripartite form that made Model Code unworkable); Rapoport, *supra* note 2, at 949 (stating that confusing manner of Model Code led to development of Model Rules).Back To Text

[14] *See* Model Rules, supra note 3 (providing standards of conduct for attorneys); Edmund B. Spaeth, Jr., *To What Extent Can a Disciplinary Code Assure the Competence of Lawyers?*, 61 Temp. L. Rev. 1211, 1219−20 (1988) (recognizing new black−letter approach by Model Rules as major difference from Model Code); Rapoport, *supra* note 2, at 949 (discussing Model Rules' more direct approach as compared to Model Code).Back To Text

[15] *See* Cowley, *supra* note 4, at 62 (stating that ABA adopted Model Rules, which was later adopted by thirty−three states in some form); Eugene R. Gaetke, Kentucky's New Rules of Professional Conduct for Lawyers, 78 Ky. L.J. 767, 770 (1990) (discussing ratification of Model Rules in many states); Kelbon, supra note 2, at 354 (stating Model Rules were adopted in 1983).Back To Text

[16] *See* Model Rules, supra note 3 (providing ethical standards of conduct for attorneys); Erwin Chemerinsky & Laurie Levenson, The Ethics of Being a Commentator, 69 S. Cal. L. Rev. 1303, 1319 n.40 (1996) (comparing distinctions in format and accessibility to required standards of conduct found in Model Code and Model Rules); Rapoport, supra note 2, at 950 (stating that Model Rules only provide guidance and attorneys are not obligated to comply). Back To Text

[17] *See* supra note 5 and accompanying text (discussing existence of conflicts of interest); *see* infra note 18 (providing Model Rule 1.7(b) and requirements for disqualification).Back To Text

[18] *See* Model Rules of Professional Conduct Rule 1.7(b) (1998) [hereinafter Model Rule 1.7(b)] providing that:

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 interest, unless:

> a. the lawyer reasonably believes the representation will not be adversely affected; and
>
> b. the client consents after 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.

Id.; *See also* Bagdan v. Beck, 140 F.R.D. 650, 658−59 (D.N.J. 1991) (emphasizing that one outcome of Model Rule 1.7(b) is to protect debtor by avoiding conflicts of interest when special counsel represents both bankruptcy trustee and individual claimants); Cowley, *supra* note 4, at 62 (stating that Model Rules govern an attorney's duty to avoid conflicts as provided for in Rule 1.7(b)).Back To Text

[19] *See* Model Rule 1.7(b), supra note 18 (discussing Rule 1.7(b) with respect to attorneys' ethical standards regarding conflicts of interest).Back To Text

[20] Id.Back To Text

[21] *See* In re Roberts, 75 B.R. 402, 405 (D. Utah 1987) (noting "complexity" of bankruptcy law).Back To Text

[22] *See* Model Rule 1.7 cmt. at 11 (stating that conflicts of interest may be difficult to assess in areas outside of litigation); In re Olsen Indus., 222 B.R. 49, 56−7 (Bankr. D. Del. 1997) (agreeing with and quoting *Leslie Fay* court); In re Leslie Fay Cos. Inc., 175 B.R. 525, 532 (Bankr. S.D.N.Y. 1994) (recognizing difficulty in assessing conflicts of interests when conflict has not yet emerged, and finding disqualification not warranted when facts indicate conflict is merely "hypothetical or theoretical").Back To Text

[23] *See* 11 U.S.C. § 327 (1994) (setting forth guidelines for employment of professionals, namely, attorneys administering bankruptcy cases); 11 U.S.C. § 101(14)(E) (1994) (defining "disinterested person" as one with no interest materially adverse to interest of estate); In re Star Broad. Inc., 81 B.R. 835, 838−39 (Bankr. D.N.J. 1988) (discussing Code's method of dealing with conflicts of interest); Kelbon, supra note 2, at 353 (stating that Code contains provisions governing attorney's duties with respect to avoiding conflicts); Meltzer, supra note 4, at 151 (stating that various sections of Code pertain to types of professionals employed by debtor and set forth ethical standards for conflicts arising in such employment).Back To Text

[24] *See* Leslie Fay, 175 B.R. at 532 (stating that Code's ethical standards create confusion when applied to bankruptcy conflicts); Larry E. Prince & Robert A. Faucher, Ethical Issues Facing Idaho Bankruptcy Practitioners, 34 Idaho L. Rev. 309, 311 (1998) (stating most ethical obligations of attorneys are subject to non−bankruptcy laws because Code addresses narrow class of obligations); R. Craig Smith, Conflicts of Interest Under the Bankruptcy Code: A Proposal to Increase Confidence in the Bankruptcy System, 8 Geo. J. Legal Ethics 1045, 1049 (1995) (stating that Congress set forth special conflict rules for bankruptcy attorneys); Christopher M. Ashby, Comment, *Bankruptcy Code Section 327(A) and Potential Conflicts of*

Interest – Always or Never Disqualifying?, 29 Hous. L. Rev. 433, 437 (1992) (stating that §§ 327(a) and 101(14) provide ambiguous standard for testing disqualification).Back To Text

[25] *See* Firm Not Automatically Disqualified From Representing Debtor, 9 No. 12 Inside Litig. 16, 16 (stating that courts "rigidly apply" § 327 standards if attorney is covered by § 101(14) disinterestedness requirements); Prince & Faucher, supra note 24, at 333 (stating that §§ 327(a) and 101(14) taken together are unclear); Ashby, supra note 24, at 437 (stating that uncertainty is created by determining disinterestedness under §§ 327(a) and 101(14)). Back To Text

[26] *See* In re Prudent Holding Corp., 153 B.R. 629, 631 (Bankr. E.D.N.Y. 1993) (recognizing that § 327 provides two−prong test for employment of attorney in bankruptcy proceeding); Lillian E. Kraemer, *Ethical Issues Involving Case Professionals and Other Court−Appointed Parties in Chapter 11 Proceedings*, CA46 ALI−ABA 1, 10 (1995) (asserting that § 327(a) provides two−prong test which courts apply simultaneously); Robin E. Phelan & John D. Penn, *Bankruptcy Ethics, an* Oxymoron, 5 Am. Bankr. Inst. L. Rev. 1, 15 (1997) (stating that § 327(a) contains "two−part test" for determining whether attorney may represent debtor); Patti Williams, Comment, Bankruptcy Code Section 327(a) − New Interpretation Forces Attorneys to Waive Fees or Wave Good−Bye to Clients, 53 Mo. L. Rev. 309, 311 (1988) (noting that two−prong test must be met under § 327(a) before attorney may be retained to represent bankruptcy estate).Back To Text

[27] Section 327(a) expressly provides that a professional retained by a "trustee" be disinterested. The term "debtor−in−possession" is omitted from section 327(a), however section 1107(a) of the Code states that a "debtor−in−possession" has the same rights and obligations as a trustee. In light of this, courts have held that section 327(a) is not limited to the trustee, and that counsel retained by the "debtor−in−possession" must also satisfy the disinterested requirements. *See* 11 U.S.C. § 1107(a) (1994) providing that:

> subject to any limitations on a trustee serving in a case under this chapter, and to such limitations or conditions as the court prescribes, a debtor in possession shall have all the rights, other than the right to compensation under section 330 of this title, and powers, and shall perform all the functions and duties, except the duties specified in sections 1106(a)(2), (3), and (4) of this title, of a trustee serving in a case under this chapter).

Id.; *See also* In re Covey, 57 B.R. 665, 666 (D.S.D. 1986) (recognizing that § 327(a) is silent as pursuant to § 1107(a)); to employment of professionals by debtor−in−possession, yet § 1107(a) extends § 327(a)'s requirements to debtor−in−possession); In re Watervliet Paper Co., 96 B.R. 768, 770 (Bankr. W.D. Mich. 1989) (stating that while § 327(a) speaks of employment by trustee, its standards are equally applicable to debtor−in−possession; Williams, supra note 26, at 309 (stating that § 327(a) applies to debtor−in−possession through § 1107(a)); Karen J. Brothers, Comment, *Disagreement Among the Districts: Why Section 327(a) of the* Bankruptcy Code Needs Help, 138 U. Pa. L. Rev. 1733, 1735 (1990) (discussing how § 1107(a) makes § 327(a) applicable to debtors−in−possession).Back To Text

[28] *See* supra note 1 and accompanying text (providing express language of § 327(a)); *see also* John D. Ayer, *Professional Responsibility in Bankruptcy Cases*, SB37 ALI−ABA 1, 32 (1997) (stating requirements for disinterestedness are often confused by courts although two requirements are distinguishable); Harvey R. Miller, *The Chapter 11 Players in Contemporary Bankruptcy Practice: Roles, Obligations, and Ethical Considerations of Debtors in Possession, Trustees, Examiners and Committees*, 630 PLI/Comm 401, 443 (1992) (stating that upon court's approval, trustee may employ disinterested attorneys without adverse interest to represent parties in bankruptcy).Back To Text

[29] *See* In re Envirodyne Indus., 150 B.R. 1008, 1016 (Bankr. N.D. Ill. 1993) (stating that Congress intended "adverse interest" and "disinterested person" to be strict limitations concerning professional's fiduciary duty); Prudent Holding Corp., 153 B.R. at 631 (describing § 327(a) as providing for undivided loyalty to bankruptcy estate); Kraemer, supra note 26, at 12 (stating that Congress' intent was to hold professionals to strict standards).Back To Text

[30] *See* 11 U.S.C. § 327(a) (1994) (mandating use of "disinterested persons" in executing bankruptcy); In re River Ranch, Inc., 176 B.R. 603, 604 (Bankr. M.D.Fla. 1994) (stating that § 327 forbids representation by professionals whose interest are "patently and obviously adverse to the interest of the estate and . . . the interest of a debtor."); Bankruptcy Litigation Report, 11 No. 5 Inside Litig. 16, 16 (1997) (stating that Code does not define "adverse interest" but applies and defines "disinterested" rigidly).Back To Text

[31] Prudent Holding Corp., 153 B.R. at 631. *See* 11 U.S.C. § 327(a) (stating that other professionals' employment in bankruptcy case is subject to court approval); In re That's Entertainment Mktg. Group, Inc., 168 B.R. 226, 229 (N.D. Cal. 1994) (stating court approval is necessary to serve estate's interest).Back To Text

[32] *See* In re Cormier, 35 B.R. 424, 425 (D. Me. 1983) (stating § 327(a) requires court's advance approval to guarantee that "employment is necessary" and in estate's best interest); Kraemer, supra note 26, at 13 (stating that reasonable necessity governs employment of professionals in bankruptcy cases); supra notes 28−31 and accompanying text (discussing purposes of Code's provisions with respect to employment of professionals).Back To Text

[33] *See* Bankruptcy Litigation Report, supra note 30, at 16 (stating that Code does not define meaning of "adverse interest"); Court Upholds Concurrent Committee Representation of Economic Competitors, 10 No. 4 Inside Litig. 11, 11 (1996) (noting that Code does not provide a definition of "adverse interest"). *But see* Edwin E. Smith & Peter C.L. Roth, *Ethical Standards in Bankruptcy Contexts: Disinterestedness*, 769 PLI/Comm 249, 252 (1998) (stating that case law defines "adverse interest"). Back To Text

[34] 46 B.R. 815 (Bankr. D. Utah 1985), *aff'd in part, rev'd in part*, In re Roberts, 75 B.R. 402 (D. Utah 1987). The District Court reversed the Bankruptcy Court on the grounds that the principles as applied to the specific facts at issue did not warrant disqualification. However, the District Court supported the Bankruptcy Court's proposed rationale in determining whether a conflict should result in disqualification for the representing attorney. Roberts, 75 B.R. at 413. *See generally* In re Crivello, 134 F.3d 831, 835−36 (7th Cir. 1998); Rome v. Braunstein, 19 F. 3d 58 n.1 (1st Cir. 1994); In re CF Holding Corp., 164 B.R. 799, 806 (Bankr. D. Conn. 1994); In re Envirodyne Indus., 150 B.R. 1008, 1016−17 (Bankr. N.D. Ill. 1993); In re American Printers & Lithographers, Inc., 148 B.R. 862, 864 (Bankr. N.D. Ill. 1992); In re Tinley Plaza Assoc., 142 B.R. 272, 276−77 (Bankr. N.D. Ill. 1992); In re Al Gelato Continental Desserts, Inc., 99 B.R. 404, 407 (Bankr. N.D. Ill. 1989); In re Glenn Elec. Sales Corp., 99 B.R. 596, 601 (D.N.J. 1988); In re Leypoldt, 1995 WL 562183, at *4 (Bankr. D. Idaho 1985) (following "adverse interest" definition set forth in *In re Roberts*).Back To Text

[35] The court in *Roberts*, defines 'to hold an adverse interest' as:

> (1) to possess or assert mutually exclusive claims to the same economic interest, thus creating either an actual or potential dispute between the rival claimants as to which, if any, of them the disputed right or title to the interest in question attaches under valid and applicable law; or (2) to possess a predisposition or interest under circumstances that render such a bias in favor or against one of the entities.

Roberts, 46 B.R. at 826−27. *See* Kelbon, supra note 2, at 357 (reiterating *Roberts*' definition of "adverse interest"); 3 Collier On Bankruptcy ¶ 327.04[2][a], at 327−27 (Lawrence P. King eds., 15th ed. rev. 1996) (defining adverse interest as "any economic interest that would tend to lessen the value of the bankruptcy estate or that would create either an actual or potential dispute," or "a predisposition under circumstances that render such bias against the estate.").Back To Text

[36] *See* supra notes 1 and 28 and accompanying text (defining disinterested standard contained in § 327(a)).Back To Text

[37] *See* 11 U.S.C. § 101(14) (1994) defining "disinterested person" as one who:

> (A) is not a creditor, an equity security holder, or an insider;
>
> (B) is not and was not an investment banker for any outstanding security of the debtor;
>
> (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 investment banker in connection with the offer, sale, or issuance of a security of the debtor;
>
> (D) is not and was not, within two years before the date of the filing of the petition, a director, officer, or employee of the debtor or of an investment banker specified in subparagraph (B) or (C) of this paragraph; and
>
> (E) 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 specified in subparagraph (B) or (C) of this paragraph . . . .

Id.; *See also*, 3 Collier, supra note 35, ¶ 327.04[3][a], at 327−30 (stating that courts differ in applying § 101(14) test for disinterestedness); Phelan & Penn, supra note 26, at 15−16 (stating that disinterestedness as defined by § 101(14) does not mean professional is "bored with the representation"). Back To Text

[38] 11 U.S.C. § 101(14)(E) (1994).Back To Text

[39] *See* Ashby, supra note 24, at 441 (quoting 2 Collier On Bankruptcy, ¶ 323.03, at 327−38).Back To Text

[40] *See* In re TMA Assocs., 129 B.R. 643, 645 n.5 (Bankr. D. Colo. 1991) (refusing to recognize difference between actual and potential conflicts of interest); In re Codesco, 18 B.R. 997, 1000 (Bankr. S.D.N.Y. 1982) (recognizing that potential conflicts are disabling); R. Craig Smith, supra note 24, at 1063 (noting that both "actual and potential conflicts" are "disabling"). Back To Text

[41] *See* H & K Developers v. Waterfall Village of Atlanta, Ltd. (In re Waterfall Village of Atlanta, Ltd.), 103 B.R. 340, 345 (Bankr. N.D. Ga. 1989) (representing an example of permissive interpretation of allowing only actual conflicts); In re Stamford Color Photo Inc., 98 B.R. 135, 138 (Bankr. D. Conn. 1989) (observing that potential conflicts alone are not enough to warrant disqualification); In re Global Marine, Inc., 108 B.R. 998, 1004 (Bankr. S.D. Tex. 1987) (noting that only actual, not potential conflicts, are disqualifying under § 327(a)).Back To Text

[42] *See* supra notes 33−41 and accompanying text (discussing § 327(a) as applied in conjunction with § 101(14)(E)). **Back To Text**

[43] *See* Ayer, supra note 28, at 33−38 (discussing courts' confusion regarding disinterestedness framework); Ashby, supra note 24, at 437 (stating that uncertainty regarding test for disqualification arises when § 327(a) is considered with § 101(14)); supra note 25 and accompanying text (discussing lack of clarity resulting from interplay of §§ 327(a) and 101(14)).Back To Text

[44] *See* In re Star Broad., Inc., 81 B.R. 835, 838 (Bankr. D.N.J. 1988) (asserting that when counsel is disinterested, both prongs of § 327(a) are met); Roger J. Au & Son, Inc. v. Aetna Ins. Co. (In re Roger J. Au & Son, Inc.), 64 B.R. 600, 604 (N.D. Ohio 1986) (stating that both prongs of § 327(a) are satisfied upon finding counsel to be non−disinterested); Ashby, supra note 24, at 439 (contending that attorney who satisfies "disinterested" prong also fulfills "no adverse interest" prong). Back To Text

[45] *Compare* In re Martin, 817 F.2d 175, 180 (1st Cir. 1987) (noting § 327(a) sets forth one−prong test), *with* In re Leslie Fay Cos., Inc., 175 B.R. 525, 531 (Bankr. S.D.N.Y. 1994) (stating that § 327(a) provides two requirements that need to be satisfied to avoid disqualification); *see also* Goldstein, supra note 5, at 444

(stating that upon existence of conflicts, some courts require demonstration of "materiality" of adverse interests); Kraemer, *supra* note 26, at 10 (stating that some courts recognize redundancy of language in § 327(a) and have collapsed requirements into one−prong test); Ashby, supra note 24, at 440 (explaining courts' disagreement as to type of conflict that will disqualify attorneys, as result of Code's lack of guidance).Back To Text

[46] *See* Martin, 817 F.2d at 180 (stating that "the twin requirements of disinterestedness and lack of adversity telescope into what amounts to a single hallmark"); Waterfall Village of Atlanta, Ltd., 103 B.R. at 343 (stating that two prongs overlap); Stamford Color Photo, Inc., 98 B.R. at 137 (noting that both prongs of § 327(a) appear to overlap); Star Broad. Inc., 81 B.R. at 838 (stating that two prongs are satisfied upon showing of disinterestedness); Roger J. Au, 64 B.R. at 604 (recognizing both prongs are satisfied when disinterested prong is met).Back To Text

[47] *See* Nat'l Bankr. Rev. Comm'n, Bankruptcy: The Next Twenty Years, Final Report 871 (1997) [hereinafter Commission Report] (retaining strict disinterested standard). Back To Text

[48] Id. at 872−73.Back To Text

[49] Id. at 873−74 (quoting In re Consolidated Bancshares, Inc., 785 F.2d 1249, 1256 n.6 (5th Cir. 1986)).Back To Text

[50] Commission Report, supra note 47, at 874. Back To Text

[51] *See* Karen Gross & Jeanne M. Weisneck, Selected Bibliography on Ethics for Bankruptcy Professionals, 68 Am. Bankr. L.J. 419, 422 (1994) (stating wide range of conflicts may arise in bankruptcy context); G. Ray Warner, Of Grinches, Alchemy and Disinterestedness: The Commission's Magically Disappearing Conflicts of Interest, 5 Am. Bankr. Inst. L. Rev. 423, 427 (1997) (discussing current laws prohibiting conflicts of professionals employed by estate or entities relating thereto); Joseph D. Vaccaro & Marc R. Milano, Note, *Section 327(a): A Statute in Conflict: A Proposed Solution to Conflicts of Interest in Bankruptcy, 5 Am. Bankr. Inst. L. Rev. 237, 237−38 (1997) (stating fiduciary obligations involving both creditors and estate create conflicts which bankruptcy courts have legitimate interest).Back To Text*

[52] *Compare* H & K Developers v. Waterfall Village of Atlanta, Ltd. (In re Waterfall Village of Atlanta, Ltd.), 103 B.R. 340, 345 (Bankr. N.D. Ga. 1989) (advocating *per se* prohibition against actual conflicts of interest), *with* In re Kelton Motors, Inc., 109 B.R. 641, 650 (Bankr. D. Vt. 1989) (stating that courts must balance number of factors in conflict cases); *see also* Meltzer, *supra* note 4, at 170−71 (addressing various courts' determinations of disqualification, whether case−by−case approach or *per se* disqualification rule); Ashby, supra note 24, at 462 (discussing inconsistent application of § 327(a) to conflicts of interest). Back To Text

[53] *See* In re American Printers & Lithographers, Inc., 148 B.R. 862, 865−66 (Bankr. N.D. Ill. 1992) (finding that continued representation created actual conflict of interest); In re Diamond Mortgage Corp. of Illinois, 135 B.R. 78, 90 (Bankr. N.D. Ill. 1990) (defining "actual conflict" as two active and competing interests); Kraemer, *supra* note 26, at 23 (stating "actual conflict" is not defined by Code, but derived meaning from bankruptcy case law).Back To Text

[54] *See* In re Dynamark, Ltd., 137 B.R. 380, 381 (Bankr. S.D. Cal. 1991) (finding that remoteness of conflict plays factor in determining whether conflict is considered actual or potential); In re BH & P, Inc., 103 B.R. 556, 563 (Bankr. D.N.J. 1989) (defining "potential" as dormant, but may become actual); William I. Kohn & Michael P. Shuster, *Deciphering Conflicts of Interest in* Bankruptcy Representation, 98 Com. L.J. 127, 143 (1993) (stating that some courts find appearance of impropriety as potential conflict and enough to justify disqualification).Back To Text

[55] *See* Brothers, supra note 27, at 1744−45 (stating courts disagree as to whether conflicts must be actual to warrant disqualification); Kohn & Shuster, supra note 54, at 139 (recognizing some courts analyze potential

conflicts with case−by−case approach while other courts apply *per se* disqualification rule); Smith & Roth, supra note 33, at 255 (describing § 327(a) as "minefield" for attorneys because of courts' inconsistent application regarding actual or potential conflicts).Back To Text

[56] *See* 11 U.S.C. § 327(c) (1994):

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

Id.Back To Text

[57] *See* id. (requiring disqualification in case where attorney represents estate and creditor if "actual conflict" exists); Kohn & Shuster, supra note 54, at 143 (stating § 327(c) specifically prohibits simultaneous representation of both estate and creditors of estate); Daniel C. Stewart, *Ethical Considerations Arising in the Representation of a Debtor and its Affiliates*, 449 PLI/Comm 59, 79 (1988) (interpreting Code to deny compensation for conflicts of interest).Back To Text

[58] *See* In re N.S. Garrott & Sons, 63 B.R. 189, 192 (Bankr. E.D. Ark. 1986) (stating that attorneys may have conflicts recognized under § 327(c) that are non−disqualifying); In re Roberts, 46 B.R. 815, 838−39 (Bankr. D. Utah 1985) (recognizing disqualification for actual conflicts, but not precluding disqualification for potential conflicts).Back To Text

[59] *See* Fund of Funds, Ltd. v. Arthur Andersen & Co., 567 F.2d 225, 227 (2d Cir. 1977) (noting that on deciding question of ethics, people will often reach different conclusions); In re Grabill Corp., 113 B.R. 966, 970 (Bankr. N.D. Ill. 1990) (noting split among courts as to whether courts should distinguish between actual and potential conflicts of interest); Waterfall Village of Atlanta, Ltd., 103 B.R. 340, 343 (observing split in authority in connection with testing for disqualification).Back To Text

[60] *See* In re BH & P, Inc., 949 F.2d 1300, 1316 (3d Cir. 1991) (stating that under § 327(c), disqualification is mandatory for actual conflicts of interest); 2 Collier, supra note 35, ¶ 327.04, at 327−29, 327−30 (noting that courts generally agree that §§ 327 and 101(14)) prohibit actual conflicts of interest); Ashby, supra note 24, at 441 (recognizing that some courts only prohibit actual conflicts of interest). Back To Text

[61] *See* In re Federated Dep't Stores, Inc., 44 F.3d 1310, 1319 (6th Cir. 1995) (reiterating that actual conflict is not required for disqualification); In re Martin, 817 F.2d 175, 182−83 (1st Cir. 1987) (holding some potential conflicts disabling but refusing to apply *per se* rule); R. Craig Smith, supra note 24, at 1058 (stating that some courts use a permissive approach, while others hold potential conflicts to be disabling).Back To Text

[62] *See* In re BH & P, Inc., 103 B.R. 556, 572 (D.N.J. 1989) (applying rebuttable presumption against allowing potential conflicts); Gill v. Sierra Pac. Constr., Inc. (In re Parkway Calabasas Ltd.), 89 B.R. 832, 835 n.3 (Bankr. C.D. Cal. 1988) (adopting presumption against potential conflicts in bankruptcy proceeding); R. Craig Smith, supra note 24, at 1059 (noting that some courts have adopted presumption against potential conflicts of interest).Back To Text

[63] *See* BH & P, Inc., 949 F.2d at 1316 (stating that "competent attorney" prong was originally proposed for large cases where "every competent professional in a particular field is already employed by a creditor or party in interest").Back To Text

[64] *See* id. at 1305 (illustrating presumption against potential conflicts of interest); R. Craig Smith, supra note 24, at 1065−69 (discussing intricacies of *In re BH & P* regarding presumption against potential conflicts of interest as not applying to actual conflicts); Vaccaro & Milano, supra note 51, at 246−47 (recognizing courts' application of rebuttable presumption pertaining to conflicts of interest).Back To Text

[65] *See* In re Kendavis Indus. Int'l, 91 B.R. 742, 754 (Bankr. N.D. Tex. 1988) (finding all conflicts actual and that potential conflicts do not exist); In re Roger J. Au & Son, Inc., 64 B.R. 600, 605 (N.D. Ohio 1986) (finding both actual and potential conflicts to be disqualifying); R. Craig Smith, supra note 24, at 1063−65 (discussing case law holding both actual and potential conflicts as violating § 327).Back To Text

[66] *See* R. Craig Smith, supra note 24, at 1059−61 (noting that some courts use permissive interpretation of Code and find only actual conflicts disabling); Ashby, *supra* note 24, at 449 (observing precedent supporting permissive construction of § 327(a)); Vaccaro & Milano, *supra* note 51, at 246−47 (recognizing that some courts take view that only actual conflicts are disqualifying). Back To Text

[67] 103 B.R. 340 (Bankr. N.D. Ga. 1989). The court found that prior representation of debtor on unrelated matters did not warrant disqualification for potential conflict. The court recognized that the case was a one asset case with a small number of creditors, a majority of the debt was held by secured creditors that were represented by counsel, and there was no "appearance of impropriety" to outweigh the debtor's right to retain counsel of choice.Back To Text

[68] *See* id. at 344 (applying flexible two−prong test to interpret Canon 9); *see also* Kleiner v. First Nat'l Bank of Atlanta, 751 F.2d 1193, 1210 (11th Cir. 1985) (adopting two−prong test for attorney disqualification); Woods v. Covington County Bank, 537 F.2d 804, 813 n.12 (5th Cir. 1976) (announcing two−prong test for attorney disqualification).Back To Text

[69] *See* Model Code Canon Nine (1980).Back To Text

[70] *See* Waterfall Village, 103 B.R. at 344 (stating that although there need not be proof of actual wrongdoing, "there must be at least a reasonable possibility that some specifically identifiable impropriety did occur" and "a court must also find that the likelihood of public suspicion or obloquy outweighs the social interest which will be served by a lawyer's continued participation in a particular case"); Kraemer, supra note 26, at 40 (discussing two−prong test used by *Waterfall Village* court: (1) whether actual conflict occurred, and (2) likelihood of public suspicion outweighing counsel's interest in representing debtor); R. Craig Smith, supra note 24, at 1061 (discussing two−prong inquiry of (1) whether an actual conflict occurred, and (2) whether likelihood of public suspicion outweighed interest of attorney representing debtor).Back To Text

[71] *See* Waterfall Village, 103 B.R. at 346 (finding no actual conflict to exist and disregarding second inquiry); R. Craig Smith, supra note 24, at 1060−61 (addressing courts' application of two−prong test and how such test was applied in *In re Waterfall*); Ashby, supra note 24, at 450 (stating that *Waterfall* court did not evaluate under second prong of test because no actual conflict existed); Vaccaro & Milano, supra note 51, at 246 (noting *Waterfall Village* court did not find actual conflict).Back To Text

[72] *See* Waterfall Village, 103 B.R. at 345 (stating that potential conflict of interest insufficient to disqualify counsel).Back To Text

[73] 108 B.R. 998 (Bankr. S.D. Tex. 1987). The court in *In re Global Marine* found that representation of corporate debtor and its subsidiaries, having common core interests, result in potential conflicts in every such case. However, this type of arrangement does not warrant disqualification. Disqualification would only result in an increase in cost for parties having to seek new attorneys to handle each multiple party, and negatively affect the time−management of the case by causing prematurely the hiring of new counsel. Id. at 1004.Back To Text

[74] *See* id.Back To Text

[75] *See* id. (asserting that potential conflicts do not warrant disqualification); Kelbon, supra note 2, at 371 (discussing contention by court in *In re Global Marine* that potential conflicts do not require disqualification); R. Craig Smith, supra note 24, at 1059−60 (recognizing *In re Global Marine* as case standing for proposition that only actual conflicts are disabling).Back To Text

[76] *See* supra note 73 and accompanying text (discussing facts and rationale of *In re Global Marine* court).Back To Text

[77] *See* In re Diamond Mortgage Corp., 135 B.R. 78, 91 (Bankr. N.D. Ill. 1990) (recognizing that some courts deal with potential conflicts on case−by−case basis); In re Oliver's Stores, Inc. 79 B.R. 588, 595 (Bankr. D.N.J. 1987) (asserting potential conflicts are not grounds for *per se* disqualification of counsel); R. Craig Smith, supra note 24, at 1061−63 (recognizing existence of line of cases that do not consider potential conflicts to be *per se* invalid). Back To Text

[78] *See* R. Craig Smith, supra note 24, at 1061−63 (noting cases where courts have disqualified attorneys for potential conflicts of interest without applying *per se* disqualification rule).Back To Text

[79] 817 F.2d 175 (1st Cir. 1987). The court found that a security mortgage on debtor's property used as attorney's retainer was not "*per se* invalid" as a potential conflict. Rather, the court remanded lower court's holding that such mortgage was *per se* disqualifying, and recommended a more flexible standard of inquiry concerning potential conflicts of interest. Id. at 183.Back To Text

[80] *See* Martin, 817 F.2d at 183 (holding potential conflicts not *per se* prohibited under § 327(a)); Meltzer, supra note 4, at 156 (discussing *Martin* line of cases as proposing that potential conflicts alone are not sufficient to warrant disqualification); Vaccaro & Milano, supra note 51, at 246 (discussing First Circuit's test considering actual conflicts to be disqualifying, where potential conflicts are not).Back To Text

[81] Martin, 817 F.2d at 183.Back To Text

[82] *See* id. at 182 (stating that potential conflict disqualification inquiry must be "case−specific" and take into consideration all relevant facts of particular case); R. Craig Smith, supra note 24, at 1059 (discussing courts' application of "balancing test").Back To Text

[83] *See* Martin, 817 F.2d at 182.Back To Text

[84] *See* id. (recognizing potential conflicts as one of many factors in courts' determination of disqualification of counsel); In re Gilmore, 127 B.R. 406, 408−09 (Bankr. M.D. Tenn. 1991) (adopting balancing approach set forth in *Martin*, and rejecting *per se* disqualification); R. Craig Smith, supra note 24, at 1062 (discussing *Martin* court's assertion that potential conflicts are only one of multitude of factors in determining whether to disqualify counsel).Back To Text

[85] *See* In re BH & P, Inc., 103 B.R. 556, 572 (Bankr. D.N.J. 1989) (establishing rebuttable presumption against simultaneous representation); In re Lee, 94 B.R. 172, 172 (Bankr. C.D. Cal. 1988) (applying rebuttable presumption against potential conflicts if trustee represents two or more related bankruptcy matters); Gill v. Sierra Pac. Constr., Inc. (In re Parkway Calabasas, Ltd.), 89 B.R. 832, 832 (Bankr. C.D. Cal. 1988) (applying rebuttable presumption that potential conflicts are disqualifying). *See generally*, R. Craig Smith, supra note 24, at 1065−69 (noting cases supporting presumption against disqualification for potential conflicts).Back To Text

[86] 103 B.R. 556 (Bankr. D.N.J. 1989) The court concluded that a trustee representing the estate could not serve as trustee for shareholders' estate because such trustee, in representing the debtor's estate, would become a creditor of shareholders. Id. at 573.Back To Text

[87] Id.Back To Text

[88] Id.Back To Text

[89] Id.Back To Text

[90] *See* BH & P, 103 B.R. at 573 (discussing potential conflicts as merely same as actual conflicts, just at different stages of development); Miller, supra note 28, at 473 (discussing courts' application of rebuttable presumption pertaining to simultaneous representation and illustrating *In re BH & P*'s conclusion that "actual" and "potential" conflicts are merely "different stages in the same relationship"); R. Craig Smith, supra note 24, at 1066 (providing various courts' applications of rebuttable presumptions against potential conflicts); Vaccaro & Milano, supra note 51, at 247 (noting courts' application of rebuttable presumptions).Back To Text

[91] *See* BH & P, 103 B.R. at 573.Back To Text

[92] *See* R. Craig Smith, supra note 24, at 1068 (discussing rebuttable presumption as applying to potential conflicts of interest framed on argument that becoming actual conflict is remote); supra note 85 (stating that rebuttable presumptions apply to potential conflicts of interest).Back To Text

[93] *See* Model Code Canon 9 (providing that "a lawyer should avoid even the appearance of professional impropriety."); R. Craig Smith, supra note 24, at 1057 (discussing courts' application of Canon 9 together with Code's "catch−all" provision which broadens courts' reach to apply to both actual and potential conflicts); Stewart, supra note 57, at 66 (discussing Canon 9 as protection against potentially conflicting arrangements).Back To Text

[94] *See* Stewart, supra note 57, at 66 (defining Canon 9 and its application to bankruptcy conflicts); S.E.C. v. ESM Group, Inc. (In re ESM Gov't Secs., Inc.), 66 B.R. 82, 84 (S.D. Fla. 1986) (holding attorney and her firm disqualified from representing parties with adverse interest under Code and Canon 9); Cowley, supra note 4, at 63 (stating that Code incorporates considerations equivalent to Canon 9's "appearance of impropriety" standard).Back To Text

[95] 64 B.R. 600 (N.D. Ohio 1986). Back To Text

[96] *See* id. at 606 (holding potential conflict worthy of disqualification); Smith, supra note 24, at 1063 (discussing *Roger J. Au & Son* and disqualification of attorney for potential conflicts of interest).Back To Text

[97] *See* supra notes 93−94 and accompanying text (defining Canon 9 and discussing disinterestedness under § 327(a)); *see also* Roger J. Au & Son, 64 B.R. at 605−06 (finding that appearance of impropriety sufficiently fulfilled § 327(a)'s "disinterested" requirement). Back To Text

[98] 91 B.R. 742 (Bankr. N.D. Tex. 1988). The court in *In re Kendavis* held that the representation of the debtor and principals of the debtor violated section 327 because the services of counsel furthered the interests of the principals and not the interests of the estate. Id. at 742. The court deemed this representation to be an actual conflict based on the belief that "a 'potential conflict' is a contradiction in terms." Id. at 744.Back To Text

[99] *See* id. at 753 (stating that once conflict is apparent it is deemed actual); In re Marine Power & Equip. Co., 67 B.R. 643, 653 (Bankr. W.D. Wash. 1986) (stating public policy is to avoid potential conflicts); Brenda Hacker Osborne, *Attorneys' Fees in Chapter 11 Reorganizations;* A Case for Modified Procedures, 69 Ind. L. J. 581, 586 (1994) (discussing *Kendavis'* bright−line rule for interpreting conflicts resulting in disqualification under § 327).Back To Text

[100] *See* Kendavis, 91 B.R. at 754 (stating court's more restrictive view scorning concept of potential conflicts); Roger J. Au. & Son, 64 B.R. at 605 (stating that "appearance of impropriety" in simultaneous representation provides requisite for lack of disinterestedness); Smith, supra note 24, at 1063 (comparing Code's eligibility standard in *In re Roger J. Au* with *In re Kendavis* where court followed more restrictive approach).Back To Text

[101] Kendavis, 91 B.R. at 753 (stating that conflict, either actual or potential, is considered conflict); *see also* In re TMA Assocs. Ltd., 129 B.R. 643, 645 n.5 (Bankr. D. Colo. 1991) (asserting no distinction between actual and potential conflicts of interest); In re Grabill Corp., 113 B.R. 966, 970 (Bankr. N.D. Ill. 1990)

(adopting *Kendavis* court's reasoning that potential conflicts do not exist).Back To Text

[102] *See* Kendavis, 91 B.R. at 753 (determining conflict by applying Canon 9 standard); *see also* H & K Developers v. Waterfall Village of Atlanta, Ltd. (In re Waterfall Village of Atlanta, Ltd.), 103 B.R. 340, 344 (Bankr. N.D. Ga. 1989) (construing *Kendavis* finding as "step further" than *Roger J. Au* holding); Smith, supra note 24, at 1064 (discussing potential conflicts restrictively interpreted by *Kendavis* court under application of Canon 9 of Model Code).Back To Text

[103] *See* Kendavis, 91 B.R. at 754 (extending § 327 to disqualify all attorneys simultaneously representing debtor and creditor, regardless of actual conflict); *In re* A.H. Robbins, Co., No. 85−1307−R, slip. op. (Bankr. E.D. Va. 1986) (holding simultaneous representation of debtor and debtor's second largest creditor which was unrelated to bankruptcy matter, as impermissible conflict of interest); Smith, supra note 24, at 1064 (discussing *Kendavis* court's construction of *per se* rule requiring disqualification for any conflict).Back To Text

[104] *See* Kendavis, 91 B.R. at 753−57; In re Michigan Gen. Corp., 78 B.R. 479, 484 (Bankr. N.D. Tex. 1987); In re Roger J. Au & Son, Inc., 64 B.R. 600, 606 (N.D. Ohio 1986) (recognizing that both actual and potential conflicts of interest violate § 327).Back To Text

[105] *See* In re Roberts, 75 B.R. 402, 405 (D. Utah 1987) (stating that as applied to potential conflicts of interest, courts "cannot paint with broad strokes" and conclusions can only be reached after "painstaking analysis" because "in deciding questions of professional ethics men of good will often differ in their conclusions."); Arnold M. Quittner, *Employment of Professionals and Compensation*, 418 PLI/Comm 173, 252, 530 (1987) (discussing courts' ethical principles should be applied according to facts at issue); Ashby, supra note 24, at 462 (stating that courts must evaluate conflicts of interest to determine disqualification under § 327(a)). Back To Text

[106] 11 U.S.C. § 105(a) (1994):

> The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.

Id.Back To Text

[107] *See* infra note 146−147 and accompanying text (recommending case−by−case analysis as applied in *In re Martin*).Back To Text

[108] *See* supra notes 86−92 and accompanying text (discussing balancing test and factors used in *In re BH & P*).Back To Text

[109] Myron M. Scheinfeld, Small Business and Single Asset Real Estate Bankruptcies, 41 No. 6 Prac. Law. 17, 18 (1995).Back To Text

[110] 11 U.S.C. § 101(51C) (1994).Back To Text

[111] Id. "Small business" was originally defined as part of a proposed new chapter 10 dealing with small business bankruptcies. S.1985, 102d Cong. § 205 (1992). This chapter was part of a comprehensive bill, which included the creation of the National Bankruptcy Review Commission and numerous commercial and consumer amendments. The American College of Real Estate Lawyers ("ACREL") objected strenuously to the new chapter 10 because it would have permitted a bankruptcy court to "disregard" the mortgagee's lien if it "finds the plan is equitable and fair." Letter from Richard R. Goldberg, President and Professor Walter J.

Taggart, Chair of the Bankruptcy and Creditor's Rights Committee of ACREL, to Hon. Howell Heflin, Chairman, Subcommittee on Courts and Administrative Practice, Committee on the Judiciary, February 14, 1992 (available in the Bankruptcy Research Library, Legislative History Collection, St. John's University, School of Law). In response to this criticism, the clause excepting real estate from the business that may be covered by the proposed chapter was inserted, thus removing formidable opposition to the bill. *See* S.1985, 102d Cong. § 205(a) (1992). The chapter itself was never enacted. However, some of the less controversial time saving provisions of chapter 10 applicable to small businesses were retained in the bill, which eventually became the Bankruptcy Reform Act of 1994, Pub. L. No 103−394 (1994). Perhaps inadvertently, the exception for real estate businesses was never deleted when the objectionable provisions of the proposed chapter 10 were eliminated. For this reason, this Note recommends the removal of the exclusion for real estate businesses from the definition of "small business" in § 101(51C).Back To Text

[112] *See* Goldstein, supra note 5, at 128 (noting Third Circuit's *per se* disqualification rule for actual conflicts of interest); Kraemer, supra note 26, at 34 (recognizing express language of § 327 prohibits representation in circumstances where actual conflicts of interest exist); R. Craig Smith, supra note 24, at 1052 (stating that courts disagree as to whether actual, present conflicts always violate Code); Vaccaro & Milano, supra note 51, at 241 (noting actual conflicts are universally disqualifying).Back To Text

[113] *See* supra section IV(a) (discussing distinction between large and small bankruptcies); *see also* H & K Developers v. Waterfall Village of Atlanta, Ltd. (In re Waterfall Village of Atlanta, Ltd.), 103 B.R. 340, 344 (Bankr. N.D. Ga. 1989) (construing *Kendavis* as expanding *Roger J. Au* holding to provide for *per se* disqualification rule); In re Kendavis Indus. Int'l, 91 B.R. 742, 751 (Bankr. N.D. Tex. 1988) (implementing *per se* disqualification rule based on actual and potential conflicts); Ashby, supra note 24, at 444 (discussing how *Kendavis* court expanded holding of *Roger J. Au* to permit disqualification based merely on potential conflicts of interest).Back To Text

[114] *See* Kendavis, 91 B.R. at 753 (stating that counsel is disqualified for representing parties in bankruptcy proceeding solely because of "appearance of impropriety"); In re Guy Apple Masonry Contractor, Inc., 45 B.R. 160, 168 (Bankr. D. Ariz. 1984) (providing that "[v]iolations of Canon 9 have served as the basis for disqualification of counsel."); Kohn & Shuster, supra note 54, at 142 (recognizing that some courts hold that potential conflicts or appearances of impropriety disqualify attorneys from representing parties involved in bankruptcy).Back To Text

[115] *See* In re Martin, 817 F.2d 175, 180−81 (1st Cir. 1987) (stating that "[s]ection 327 is intended . . . to address the appearance of impropriety as much as its substance, to remove the temptation and opportunity to do less than duty demands."); Monon Corp. v. Wabash Nat'l Corp., 764 F. Supp. 1320, 1322 (N.D. Ind. 1991) (allowing disqualification of attorney in reliance on Canon 9 standards of "appearance of impropriety"); In re Glenn Elec. Sales Corp., 99 B.R. 596, 601 (D.N.J. 1988) (stating that Code's disqualification measures are similar to Canon 9); In re B.E.T. Genetics, Inc., 35 B.R. 269, 271 (Bankr. E.D. Cal. 1983) (indicating courts' ability to disqualify based solely on Canon 9 standards); Kelbon, supra note 2, at 354 (recognizing Bankruptcy Code's adoption of strict measures initiated in Canon 9); Ashby, supra note 24, at 447−48 (stating that Congress intended disqualification to ensure that counsel best serves interest of estate).Back To Text

[116] *See* 11 U.S.C. § 327(a) (1994); Martin, 817 F.2d at 180 (providing that "[t]he duty explicitly imposed on the bankruptcy court by § 327 . . . demands that the court root out all impermissible conflicts of interest between attorney and client"); In re Roger J. Au & Son, Inc., 65 B.R. 322, 335 (Bankr. N.D. Ohio 1984) (holding that past representation of debtor's sole shareholder and principal officer disqualified counsel and firm because both were no longer disinterested); Susan Pace Hamill, The Limited Liability Company: A Catalyst Exposing the Corporate Integration Question, 95 Mich. L. Rev. 393, 411 (1996) (recognizing that smaller corporations have lower rate of return as compared to larger firms); Elizabeth Warren, The Untenable Case for Repeal of Chapter 11, 102 Yale L.J. 437, 442 (1992) (recognizing large corporations' ability to hire team of qualified attorneys to handle bankruptcy, whereas smaller companies do not have this luxury).Back To Text

[117] *See* Commission Report, supra note 47, at 874.Back To Text

[118] *See* Christopher W. Frost, *Running the Asylum: Governance Problems in* Bankruptcy Reorganizations, 34 Ariz. L. Rev. 89, 131 (1992) (discussing courts' recognition of complexity of business judgments and requirement that decision−maker be free of conflict); Harvey R. Miller, The Changing Face of Chapter 11: A Reemergence of the Bankruptcy Judge As Producer, Director, and Sometimes Star of the Reorganization Passion Play, 69 Am. Bankr. L.J. 431, 449 (1995) (recognizing complexity of reorganization cases which often involve hundreds of parties in interest); Smith, supra note 24, at 1046 (discussing large scale bankruptcies which often involve hundreds of parties with diverse interests resulting in increase of potentially conflicting interests).Back To Text

[119] *See* In re Leslie Fay Cos., Inc., 175 B.R. 525, 537 (Bankr. S.D.N.Y. 1994) (stating that law firm's failure to disclose actual and potential conflicts of interest cost company heavy financial burden); In re Michigan Gen. Corp., 77 B.R. 97, 106 (Bankr. N.D. Tex. 1987) (stating possibility of conflict may justify disqualification and any doubts relating thereto shall result in disqualification); Phelan & Penn, *supra* note 26, at 19 (recognizing importance of immediate action and disclosure rather than waiting for actual conflicts to arise). Back To Text

[120] *See* Shaw & Levine v. Gulf & Western Indus., Inc. (In re Bohack Corp.), 607 F.2d 258, 263 (2d Cir. 1979) (stating generally, courts loathe to separate clients from attorneys where there is no prejudice since such dismissal can lead to delay and expense); Michigan Gen. Corp., 77 B.R. at 103 (stating that estate should not be burdened with cost incurred in maintaining employment of attorney when there is no "concomitant benefit").Back To Text

[121] *See* supra notes 119−20 and accompanying text (discussing that delay in disqualifying attorneys may result in economic hardships).Back To Text

[122] *See* Pierson v. Creel (In re Consolidated Bancshares, Inc.), 785 F.2d 1249, 1256 n.6 (5th Cir. 1986) (noting that strict disinterested standard is required to preserve judicial and public confidence in bankruptcy system); Bohack, 607 F.2d at 263 (discussing how integrity of judicial process can outweigh delay and expenses brought on by attorney replacement); In re Lee Way Holding Co., 100 B.R. 950, 958 (Bankr. S.D. Ohio 1989) (recognizing that court should scrutinize disinterested standard to ensure integrity of bankruptcy process and to maintain confidence in bankruptcy system); In re Philadelphia Athletic Club, Inc., 20 B.R. 328, 334 (Bankr. E.D. Pa. 1982) (stating that strict disinterested standard should be applied to preserve confidence in bankruptcy process); *see also* infra notes 119 and 136 (comparing economic hardships and delay with goals of bankruptcy).Back To Text

[123] *See* In re F.M. Station, Inc., 169 B.R. 502, 502 (Bankr. D.R.I. 1994) (denying fees where conflicting interest of counsel produced negative effect on estate); In re Kendavis Indus. Int'l, 91 B.R. 742, 748 (Bankr. N.D. Tex. 1988) (disqualifying attorney because actual conflict resulted in attorney not acting in best interest of estate).Back To Text

[124] *See* In re Martin, 817 F.2d 175, 181−82 (1st Cir. 1987) (rejecting *per se* disqualification in case of potential conflicts); In re Diamond Mortgage Corp., 135 B.R. 78, 91 (Bankr. N.D. Ill. 1990) (distinguishing between actual and potential conflicts); Kelbon, supra note 2, at 353 (recommending adoption of pragmatic approach for conflicts as opposed to *per se* disqualification rule); Ashby, supra note 24, at 456 (proposing that potential conflicts are not *per se* disqualifying). Back To Text

[125] *See* supra note 106 (providing full text of § 105(a)).Back To Text

[126] *See* Elizabeth H. Winchester, Note, Expanding the Bankruptcy Code: The Use of Section 362 and Section 105 to Protect Solvent Executives of Debtor Corporation, 58 Brook. L. Rev. 929, 939 (1992) (noting that § 105 grants bankruptcy courts discretionary power to enjoin conduct which adversely affects debtor). *See generally* David A. Brenningmeyer, Comment, The Limited Power of Federal Bankruptcy Courts to Stay

Enforcement of State Environmental Regulations, 44 Me. L. Rev. 485, 505−06 (1992) (discussing discretionary power granted to courts under § 105 of Code); James O. Johnston, Jr., Note, The Inequitable Machinations of Section 362(a)(3): Rethinking Bankruptcy's Automatic Stay Over Intangible Property Rights, 66 S. Cal. L. Rev. 659, 678−79 (1992) (discussing equitable power granted to courts through § 105).Back To Text

[127] 11 U.S.C. § 105(a) (1994).Back To Text

[128] *See* Smith & Roth, supra note 33, at 258−59 (discussing split among courts as to whether discretionary power under § 105 can be used by courts to ignore or modify § 327(a) when employment is in best interest of estate).Back To Text

[129] *See* Archambault v. Hershman (In re Archambault), 174 B.R. 923, 928 (W.D. Mich. 1994) (recognizing that court cannot use equitable power of § 105 to override clear directives of Code); Childress v. Middleton Arms, Ltd. Partnership (In re Middleton Arms, Ltd. Partnership), 119 B.R. 131, 134 (M.D. Tenn. 1990) (reversing bankruptcy court for overstepping equitable jurisdiction conferred by § 105 for failure to apply requirements of § 327(a)); Warner, supra note 51, at 443 n.41 (stating that court cannot use § 105 to circumvent § 327(a)).Back To Text

[130] 119 B.R. 131 (M.D. Tenn. 1990). The court held that a disinterested real estate broker under § 327(a) could not be employed under the court's discretionary authority set forth in § 105 even though the employment would only have a beneficial affect on the parties (security holders).Back To Text

[131] Middleton Arms, Ltd., 119 B.R. 124, 134 (M.D. Tenn. 1990) (quoting *In re* C−L Cartage Co., 899 F.2d 1490 (6th Cir. 1990) and Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 206 (1988), respectively).Back To Text

[132] *See* United States Trustee v. PHM Credit Corp. (In re PHM Credit Corp.), 110 B.R. 284, 288 (E.D. Mich. 1990) (stating § 105 grants courts power to adopt curative measures addressing concerns with regard to requirements of § 327); In re Flanigan's Enterps., 70 B.R. 248, 253 (Bankr. S.D. Fla. 1987) (applying modified test for employment).Back To Text

[133] 110 B.R. 284 (E.D. Mich. 1990). Back To Text

[134] *See* id. at 286, 289.Back To Text

[135] *See* 11 U.S.C. § 105(a) (1994).Back To Text

[136] *See* United States v. LTV Corp. (In re Chateaugay Corp.), 944 F.2d 997, 1002 (2d Cir. 1991) (noting Code's aim to provide reorganizing debtors with fresh start); Internal Revenue Service v. Energy Resources, Co. (In re Energy Resources Co.), 871 F.2d 223, 230 (1st Cir. 1989) (discussing reorganization goals of ensuring payment to creditors and providing debtors with opportunity to make fresh start); Michelle M. Arnopol, *Including Retirement Benefits in a* Debtor's Bankruptcy Estate: A Proposal for Harmonizing ERISA and the Bankruptcy Code, 56 Mo. L. Rev. 491, 501 (1991) (stating that goals of federal bankruptcy system are to provide honest debtor with fresh start and to ensure equitable distribution of assets to creditors); Susan Block−Lieb, *Fishing in Muddy Waters: Clarifying the Common Pool Analogy as Applied to the Standard for Commencement of a* Bankruptcy Case, 42 Am. U. L. Rev. 337, 429 (1993) (asserting that purpose of chapter 11 reorganization includes maximization of distributions to creditors and providing debtor with fresh start); Gary M. Roberts, Note, Bankruptcy and the Union's Bargain: Equitable Treatment of Collective Bargaining Agreements, 39 Stan. L. Rev. 1015, 1025 (1987) (recognizing that bankruptcy law allows creditors to collect debt effectively and efficiently); Daniel J. Von Weihe, Note, *Necessary or Excessive: The Standard of "Reasonably Necessary" in* Chapter 13 Bankruptcy, 17 J. Corp. L. 639, 639 (1992) (providing that Code permits debtor to obtain fresh start in exchange for equitable return to creditor).Back To Text

[137] *See* In re American Printers & Lithographers, Inc., 148 B.R. 862, 866−67 (Bankr. N.D. Ill. 1992) (disqualifying law firm based on finding of high likelihood that potential conflict would become actual); In re Roberts, 46 B.R. 815, 823 (Bankr. D. Utah 1985) (stating that disqualification should not apply to theoretical or hypothetical conflicts, rather only where actual conflicts are present); 2 Collier, supra note 35, ¶ 327.03, at 327−42 (asserting that remote relationships should not serve as basis for disqualification); Ashby, supra note 24, at 454 (recognizing that courts do not have to disqualify for every potential conflict); *see also* Goldstein, supra note 5, at 482 (recognizing that cost of retaining new attorney is costly and time−consuming and may jeopardize reorganization process); infra note 138 and accompanying text (weighing value of disqualification against goals of bankruptcy law).Back To Text

[138] *See* H & K Developers v. Waterfall Village of Atlanta, Ltd. (In re Waterfall Village of Atlanta, Inc.), 103 B.R. 340, 344 (Bankr. N.D. Ga. 1989) (stating that court must weigh debtor's interest in obtaining counsel of choice with "likelihood of public suspicion" when determining whether conflict should be disqualifying); Warner, supra note 51, at 426 (recognizing equitable considerations in determining whether conflicts should be waived); Ashby, supra note 24, at 454−55 (stating that courts should compare likelihood of injury to integrity of bankruptcy system with regard to particular conflict at issue); *see also* Jeff Bohm & David B. Young, *Small Business and Single Asset Real Estate Reorganizations and the Bankruptcy Reform Act of 1994*, 753 PLI/Comm 465, 471 (1997) (recognizing unique problems characteristic to small companies which require different treatment than larger publicly held corporations).Back To Text

[139] *See* In re BH & P, Inc., 103 B.R. 556, 562 (Bankr. D.N.J. 1989) (noting that in large cases, it is difficult to find qualified counsel without conflict); In re O.P.M. Leasing Servs., Inc., 16 B.R. 932, 932 (Bankr. S.D.N.Y. 1982) (stating that in large bankruptcies, courts must carefully scrutinize disqualification due to complex nature of such cases); 2 Collier, supra note 35, ¶ 101.14, at 101−31 (stating that in large cases, it is more difficult to retain qualified counsel who does not represent shareholders or creditors of debtor).Back To Text

[140] *See* Frost, supra note 118, at 132 (recognizing that large bankruptcy estates have high likelihood of multiple creditors with claims that warrant managerial analysis, and pressures from shareholders make large bankruptcies more difficult to manage); Warner, supra note 51, at 441 (recognizing key distinctions between large complex companies as compared to smaller corporate entities, resulting from managerial component and infrastructure).Back To Text

[141] 94 B.R. 172 (Bankr. C.D. Cal. 1989).Back To Text

[142] *See* id. at 180 (declining to impose "drastic remedy" on attorney representing corporate debtor and sole shareholders).Back To Text

[143] *See* id. at 179 (noting "[c]ourt has the power to reduce the compensation awarded to professionals, or to deny it altogether" for conflicts, however, court used discretionary authority to only disqualify attorney in one case).Back To Text

[144] *See* In re Martin, 817 F.2d 175, 182 (1st Cir. 1987) (stating that for conflict to be disabling, it must carry sufficient threat of material adversity to warrant disqualification); In re Guy Apple Masonry Contractors, Inc., 45 B.R. 160, 166 (Bankr. D. Ariz. 1984) (recognizing that proper inquiry is whether conflict is materially adverse to estate, not merely whether conflict exists); Smith, supra note 24, at 1053 (noting that some courts require showing of "sufficient threat of material adversity" for disqualification).Back To Text

[145] *See* id. (discussing courts' focus on how estate is affected by disqualification or continued representation).Back To Text

[146] *See* Martin, 817 F.2d at 182 (noting court's application of balancing inquiry is "case−specific"); Pierson v. Creel (In re Consolidated Bancshares), 785 F.2d 1249, 1256 (5th Cir. 1986) (noting Fifth Circuit's "painstaking analysis of the facts and precise application of precedent" when determining whether conflict is disqualifying); In re Hoffman, 53 B.R. 564, 566 (Bankr. W.D. Ark. 1985) (noting that in testing whether

conflict requires disqualification, conflict "must be considered in light of the particular facts of each case.").Back To Text

[147] Martin, 817 F.2d at 182.Back To Text

[148] 103 B.R. 556 (Bankr. D.N.J. 1989). Back To Text

[149] *See* In re Energy Resources Co., 871 F.2d 223, 230 (1st Cir. 1989) (recognizing Code's goal is to ensure payment to creditors); Arnopol, supra note 136, at 501 (providing that bankruptcy attempts to apply equitable distribution of assets to creditors); Kelbon, supra note 2, at 371 (noting courts' interest in economy of estate in evaluating whether conflict warrants disqualification).Back To Text

[150] *See* Rome v. Braunstein, 19 F.3d 54, 59 n.3 (1st Cir. 1994) (noting court's determination whether potential impairment will be "outweighed by impracticability of disentangling multiple interests 'without unreasonable delay'"); In re Caldor, Inc., 193 B.R. 165, 177 (Bankr. S.D.N.Y. 1996) (recognizing that conflicts can be outweighed by costs and delay to litigation upon disqualification of professionals); Rapoport, supra note 2, at 937 (discussing that delay is fatal to process of reorganization and retention of new counsel requires time to become familiar with case). Back To Text

[151] *See* In re Oliver's Stores, Inc., 79 B.R. 588, 594 (Bankr. D.N.J. 1987) (noting that disqualification is warranted by establishing that conflict is likely to arise); In re O'Connor, 52 B.R. 892, 897 (Bankr. W.D. Okla. 1985) (stating that proper test is not whether "hypothetical or theoretical conflict is present" but whether "a potential actual conflict" exists); Ashby, supra note 24, at 457 (stating that based on facts of particular case, courts should consider likelihood potential conflict will evolve into disabling actual conflict).Back To Text

[152] *See* In re Stamford Color Photo, Inc., 98 B.R. 135, 137 (Bankr. D. Conn. 1989) (stating that court must consider "interest of justice" as factor to be weighed); Brothers, supra note 27, at 1743 (recognizing that some courts hold that "interest of justice" should be considered in determining whether or not to disqualify professional). Back To Text

[153] *See* In re Federated Dept. Stores, Inc., 114 B.R. 501, 506 (Bankr. S.D. Ohio 1990) (recognizing importance of retaining counsel familiar with affairs of debtor); In re Heatron, Inc. 5 B.R. 703, 705 (Bankr. W.D. Mo. 1980) (refusing to disqualify attorney with conflict because of value afforded by attorney's experience and familiarity with debtor); Brothers, supra note 27, at 1735−36 (discussing importance of debtor retaining counsel familiar with case which will save time and cost in best interest of estate).Back To Text

[154] In re Martin, 817 F.2d 175, 182 (1st Cir. 1987).Back To Text

[155] *See* Smith & Roth, supra note 33, at 255 (asserting that § 327(a) creates a "minefield for lawyers to determine in which situations a court may find a lack of disinterestedness or the holding of an adverse interest").Back To Text