UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

HOUSEHOLD MERIT, INC.	CASE NO. 94-62969
Debtor	Chapter 7

APPEARANCES:

DAMON & MOREY, LLP
Attorneys for Debtor
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Chapter 7 Trustee
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Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

MEMORANDUM-DECISION, FINDINGS OF FACT,
CONCLUSIONS OF LAW AND ORDER

The Court considers herein two applications for fees and expenses sought in the above referenced case originally filed pursuant to Chapter 11 of the Bankruptcy Code (11 U.S.C. §§101-1330)("Code") on October 31, 1994 and thereafter converted to a case pursuant to Chapter 7 of the Code on February 16, 1995.[1]

The first fee application was filed by Damon & Morey, LLP ("Damon"), Debtor's attorneys, on July 18, 1995, seeking a fee of $36,651.50 and reimbursement of expenses in the sum of $4,974.39

[1] Upon conversion of the case Paul M. Fischer, Esq. was appointed to act as Trustee.

covering the period September 1, 1994 through May 31, 1995. The second application was filed by Freed Maxick Sachs & Murphy, P.C. ("Freed"), Debtor's accountants, also on July 18, 1995, seeking a fee of $17,482.80 and reimbursement of expenses in the sum of $343.74 covering the period October 1, 1994 through January 31, 1995.

A hearing was held before this Court on both fee applications on August 8, 1995, with the United States Trustee ("UST") and the Chapter 7 Trustee ("Trustee") appearing in opposition. The Court granted all parties the option of filing memoranda of law not later than September 5, 1995. With the consent of the Court, the parties continued to submit memoranda of law through October 12, 1995.

JURISDICTIONAL STATEMENT

The Court has core jurisdiction of this contested matter pursuant to 28 U.S.C. §§1334(b), 157(a), (b)(1) and (2)(A) and (B).

DISCUSSION

Prior to the filing of the Chapter 11 case, Damon received a retainer from the Debtor in the sum of $35,800, of which $800 was applied to the case filing fee. In addition, Damon received the sum of $4,877.28 attributable to the services

allegedly rendered to the Debtor pre-petition.[2] As of the date of the filing of its fee application, Damon had not applied any portion of the $4,877.28 to its pre-petition services. (See Application of Damon & Morey, LLP For Allowance of Compensation and Reimbursement of Expenses dated July 13, 1995.)

A review of the docket of this Chapter 11 case indicates a filing date of October 31, 1994 and, thereafter, an Order by this Court sua sponte converting the case to Chapter 7 on February 16, 1995, following the initial status conference held by the Court. After conversion to Chapter 7, Debtor's major secured creditor succeeded in having the automatic stay vacated by Order dated February 23, 1995, thereby repossessing all of Debtor's inventory.[3]

The UST objects to the Damon fee application on several grounds: first, that it does not comply with the so-called UST Fee Guidelines promulgated pursuant to 28 U.S.C. §586(a)(3)(A); second, that the fee application seeks compensation for post-conversion services, other than services rendered by Damon in the preparation of the final report required by Federal Rule of Bankruptcy Procedure ("Fed.R.Bankr.P.") 1019; third, that Damon seeks compensation for travel time at its full hourly rate; fourth, and perhaps most significant, that Damon's services provided little benefit to the estate and may have been intended to advance the interest of Debtor's principal, William Baker ("Baker"), that the

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[2] UST asserts that Debtor's Statement of Financial Affairs discloses that Damon was paid $10,422.14 for pre-petition legal services.

[3] Damon seeks compensation for some 40.3 hours expended allegedly on Debtor's behalf post conversion.

Chapter 11 case had little chance of success, that, in fact, the "ultimate effect of the Chapter 11 case was to diminish what assets were available on the date of filing such that upon conversion there are no assets available for the unsecured creditors except for possible actions against the principals of the debtor corporation". (See Objection of the U.S. Trustee to Application of Damon & Morey, LLP, dated August 3, 1995, ¶7.)

The Trustee, while filing an Objection to both the Damon and Freed fee applications, acknowledges that he did receive Damon's cooperation in gathering documentation regarding Debtor's Chapter 11 operations to assist him in administering the Chapter 7 case. The Trustee asserts, however, the retainers being held by Damon and Freed, totalling approximately $50,000, will apparently be the only potential estate asset out of which Chapter 7 and 11 administration expenses can be paid. Thus, the Trustee contends that the retainers should be turned over to him for a pro rata distribution to all administrative claimants.[4] Additionally, the Trustee argues that any claim for pre-petition services interposed by Damon or Freed should be treated as a pre-petition unsecured non-priority claim.

Damon opposes the UST's Objection, asserting that it did not represent Debtor's principal, Baker, but that in fact he was represented by other counsel in negotiations with Debtor's primary secured lender, Marine Midland Bank ("MMB"), who ultimately repossessed all of Debtor's inventory and in turn sold it back to

[4] The Court notes that Code §726(b) grants priority to Chapter 7 administrative expenses over Chapter 11 administrative expenses in a converted case.

Baker post conversion. Damon contends that by virtue of Code §330 as amended by the Bankruptcy Reform Act of 1994 Pub.L.No. 103-394, the Court must examine factors other than solely results obtained in arriving at appropriate compensation utilizing the so-called "lodestar" test. Damon asserts that it need not guarantee a successful reorganization in order to earn its fees.

Turning to the objection of the Trustee, Damon argues that its retainer, and presumably that of Freed, is not property of the bankruptcy estate since it was accepted as "security for fees to be incurred in connection with Debtor's bankruptcy case and was deposited in Damon & Morey's attorneys' 'trust account' ("trust")." (See Response to Objection of Chapter 7 Trustee to the Application of Damon & Morey dated August 7, 1995, ¶5.)

Finally, Damon objects to the UST's criticism of billing its travel time at the full hourly rate, asserting that its blended billing rate for the case was approximately $100 per hour and was reasonable. Damon also takes issue with the UST criticism that the fee applications fail to comply with the newly promulgated "Fee Guidelines", contending that it had been advised by the UST that it would not apply those guidelines to cases filed prior to March 22, 1995.

Thus, the fee applications of Damon and Freed present two distinct issues for resolution by this Court. The first issue, which focuses primarily on the Damon fee application, is the reasonableness of the fee requested as determined in accordance with Code §330(a)(3)(A), while the second issue relates to the character of the retainers held by the professionals.

Addressing the first issue, the Court finds merit in the objection of the UST insofar as he challenges the benefit of Damon's services to the unsecured creditors of Debtor's estate. One need only review the docket of this case to realize that Debtor had little prospect of reorganization and that liquidation was apparently its only real option from the date of filing forward.[5] While the duration of a Chapter 11 case is not necessarily determinative of its initial viability, it may be some indication of a bad faith or inappropriate filing. See generally Matter of Little Creek Development Co., 799 F2d 1068, 1073 (5thCir. 1986). "Creditors should not be subjected to costs and delays of a bankruptcy proceeding if there is not a potential viable business in place worthy of protection. (citations omitted)."

The Chapter 11 case was filed on October 31, 1994 and less than four months later the case was converted to Chapter 7. In the intervening period, activity in the case was limited to a motion by Debtor to use cash collateral, a motion to conduct a sale of assets out of the ordinary course of business and approval of unsecured borrowing, a motion by two unsecured creditors to convert the case to Chapter 7, a motion by a secured creditor holding the security interest in cash collateral (MMB) to declare the cash collateral order in default or in the alternative lift the automatic stay, and motions by both Damon and Freed asking the Court to reconsider its Orders of Appointment pursuant to Code §327

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[5] A review of Debtor's pre-petition activity also lends support to the liquidation theory, Debtor having closed several of its stores prior to its Chapter 11 filing and effectuated the merger of two affiliates into the Debtor.

vis a vis the effective date of their respective appointments.[6]

While hindsight is almost always 20/20, it sometimes provides a valuable analysis of the futility that surrounds some debtors' excursions into bankruptcy generally or into particular chapters specifically. Damon defends its Chapter 11 advice to Debtor by contending that but for the failure of a "cash raising" sale timed to coincide with the return of troops from the U.S. Army's 10th Mountain Division from Haiti to the Watertown, New York (Fort Drum) area, Debtor's reorganization would have succeeded. Damon acknowledges that the failure of that sale mandated conversion to Chapter 7 for the Debtor.

The UST concedes that while a debtor's attorney in a Chapter 11 case is not required to guarantee a successful reorganization as a condition precedent to the approval of its fees, failure of a reorganization is a significant factor to be considered, citing In re Lederman Enterprises, Inc., 143 B.R. 772, 775 (D.Colo. 1992) aff'd 997 F.2d 1321 (10th Cir. 1993). In the Lederman case, the district court, citing to In re Offield, 128 B.R. 548 (Bankr. W.D.Mo. 1991), clearly articulated a standard that bankruptcy courts need not approve attorney compensation for services which do not benefit the estate. "Chapter 11 cases which lack viable chances of reorganization may place fees of counsel at risk." Id. at 550. However, both the Lederman and Offield decisions were rendered prior to the 1994 amendments to Code §330

[6] On April 14, 1995, the Court issued its Memorandum-Decision, Findings of Fact, Conclusions of Law and Order denying the motion of Damon and Freed to reconsider its prior Orders and make both professionals appointment nunc pro tunc to the date the Chapter 11 case was filed.

which are applicable to these fee applications.

It is worthy of note that amended Code §330(a)(3)(C) rejects to a large extent the "hindsight" analysis of benefit to the estate by providing that services had to have been "beneficial at the time at which the service was rendered". Thus, if Damon's services rendered in fall of 1994 were arguably beneficial as judged by the status of the case at the time, they appear to pass muster pursuant to Code §330(a)(3)(C). Damon's assertion that the Debtor's "cash raising" sale, scheduled to coincide with the return of the U.S. Army troops to the Watertown, New York area in early January 1995, was the linchpin of its ability to reorganize is somewhat suspect. It is all the more suspect when one considers that rather than conducting the so-called "cash raising" sale itself, the Debtor employed the services of a liquidator. This Court reaches the conclusion that Debtor's Chapter 11 case was probably intended to be a liquidation from the date of filing forward, regardless of the outcome of the so-called "cash raising" sale. While the Court acknowledges that a liquidating Chapter 11 is clearly permissible and, in some instances, may result in a greater return to unsecured creditors than a Chapter 7 liquidation, this particular liquidation resulted in little or no benefit to unsecured creditors and appears to have benefitted only the Debtor's principal. This lack of benefit was the result of the secured creditor's vacating of the automatic stay, and its repossession and resale of the inventory to Debtor's principal, Baker and Baker's subsequent unauthorized use of the jurisdiction

of this Court to continue or re-start the "cash raising" sale. [7] The UST, in fact, asserts that in reality Damon sought to protect the best interests of Baker rather than adequately representing the Debtor.

While Damon disputes the UST's assertion of a conflict of interest, a review of the time records may not fully support Damon's opposition. For example, on January 23, 1995, Damon's time records indicate that it was conferencing with Baker regarding "exit strategy" and on the same date, they discussed a "buy out" of the Marine note. Between January 25, 1995 and January 26, 1996, Damon was conferring with Marine's attorneys and Samuel Hester, Esq. ("Hester") allegedly Baker's personal attorney, regarding a buy-out of Marine's interest in Debtor's former assets. Again in February 1995, Damon was negotiating with attorneys for Marine and, ostensibly, Baker regarding Marine's lift stay motion and the ultimate disposition of the repossessed inventory to Baker personally. It is difficult for the Court to conclude that any of these services benefitted the creditors of the Debtor's estate at the time they were rendered, whether or not Damon was engaged in an alleged conflict of interest.

Finally, in analyzing the Fee Application, the UST objects to Damon's fee request for services rendered post-conversion to Chapter 7 except to the extent that they complied with Fed.R.Bankr.P. 1019. In that regard, the Chapter 7 Trustee does acknowledge that he received significant assistance from Damon

[7] Following repossession of Debtor's inventory and resale to Debtor's principal, Baker continued to advertise the liquidation sale as being pursuant to an order of this Court.

in performing his fiduciary duties.[8]

Keeping the foregoing in mind, the Court has analyzed Damon's Fee Application in three components. The first component covers the pre-petition period (9/24/94 through 10/31/94). The Court will make no adjustments to the fee requested for that period. The second component is the post-petition, post-appointment period (11/7/94-2/16/95).[9] A review of the time records during this period supports the assertion of the UST that Damon was at least in part providing services that could only have benefitted Baker, Debtor's president, in connection with his purchase of Debtor's inventory from MMB following its modification of the stay and repossession of its collateral. The Court will, therefore, disallow 7.4 hours attributable to William Savino, Esq. ("Savino"), billed at $175 per hour and 11.6 hours attributable to Henry Gitter, Esq. ("Gitter") billed at $100 per hour. The third component is the post-conversion period (2/16/95-5/18/95). During this latter period the Court has approved a fee only for hours which were expended in directly assisting the Trustee. Therefore, the Court will disallow 1.9 hours attributable to Savino; 21.2 hours attributable to Gitter; 1.5 hours to Daniel Brown, Esq.; and 4.9 hours attributable to Patricia M. Christ, a paralegal.

Additionally, the Court notes that Damon has billed its

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[8] Both the UST and Damon reference the recent decision of In re Friedland, 182 B.R. 576 (Bankr. D.Colo. 1995) which interpreted new Code §330(a)(4)(B), as prohibiting compensation to a Chapter 7 debtor's counsel. However, since both concede that Damon is entitled to compensation for services rendered directly to the Trustee the Court will not discuss Friedland herein.

[9] While Damon's time records reflect post-petition pre-appointment hours, no fee is claimed for that period.

travel time at its full hourly rate, a practice not permitted by this Court except in very limited circumstances not present here. Accordingly, the Court will adjust 34 hours of travel time attributable to Gitter between October 11, 1994 and February 15, 1995, which results in a further reduction of the fee request by $1,646. Finally, the Court will not approve the estimated fee of $600 for future services included in the Fee Application.

The foregoing adjustments result in a total reduction of Damon's fee request by $7,688.50.

A review of Damon's request for reimbursement of expenses meets with the approval of this Court with the exception of "overtime work expenses" totalling $200.81. Thus, the Court will authorize reimbursement of expenses of $4,773.58.

Turning to the Fee Application of Freed, the Court notes at the outset that while the Fee Application references a $15,000 pre-petition retainer, no mention was made of the retainer in Freed's Application for Appointment approved by this Court on December 30, 1994. The failure to disclose said retainer violates Fed.R.Bankr.P. 2014(a) and Rule 214.1 of Local Rules of this Court.

In addition, the Freed Fee Application seeks compensation for some 29 hours expended between the date of filing (10/31/94) and the effective date of Freed's appointment (12/1/94), which will be denied in accordance with the "per se" rule which this Court believes still prevails in this Circuit. See In re Household Merit, Inc., Case No. 94-62969, (April 14, 1995, Gerling, C.J.).

An examination of Freed's time records leads the Court to conclude that in many instances they do not comply with Local Rule

216.1(3) of the Local Rules of the Court which were in effect at the time the Freed Application was filed.[10] There are numerous time entries for Howard A. Rein, CPA, a Director of Freed, which state simply "Telephone discussions with W. Baker regarding current financial affairs". Thus, the Court will disallow an additional 5.5 hours expended between 12/2/94 and 1/3/95 subject to further explanation. Finally, the Court will disallow 3 hours of secretarial time which is appropriately included in Freed's overhead.

Making adjustment for the total hours disallowed, the Court will reduce Freed's Fee Application by $4,064.50.[11] The Court will make no adjustment to Freed's request for disbursements.

The final issue raised by these Fee Applications requires this Court to examine the nature of the retainers paid to Damon and Freed, respectively, prior to the filing of Debtor's petition. Both professionals contend that the retainers paid to them pre-petition were in the nature of advanced payment or security retainers which they allege did not become property of Debtor's estate and, therefore, no portion of the retainers need be turned over to the Trustee. Damon argues that the nature of the retainers is to be determined by state not federal law and that if the Court rejects the advance payment theory, then it must conclude that both

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[10] It likewise does not appear that the time records would have complied with former Local Rule 17, which Rule was in effect as of the date Freed was appointed.

[11] Freed's time records total $21,485.80, though its fee request is limited to $17,482.80, since it apparently concedes that it was not entitled to its post-petition pre-appointment hours. The Court has made its adjustment to the total of Freed's time records.

Damon and Freed possess security interests in the retainers which preclude disgorgement for payment of either Chapter 11 or Chapter 7 administrative claims..

Both the UST and the Trustee agree that state law controls the nature of the retainer being reviewed by a federal bankruptcy court. Both urge the Court to reject the professionals argument that their retainers are in the nature of advanced payment retainers and, therefore, fully earned pre-petition, thus, not becoming property of the estate. Rather the UST and the Trustee argue that, at best, the retainers herein are security retainers which do constitute property of the Debtor's estate subject to the rights of the secured creditors, i.e. Damon and Freed. The UST carries its analysis one step further and urges the Court to address an issue arguably of first impression, to wit: whether a security retainer secures only pre-petition services, not post-petition services and, thus, the latter services are not to be considered in analyzing the amount of the secured claim pursuant to Code §506(a). The UST contends that the professionals claim to fees for post-petition services are, at best, an administrative expense pursuant to Code §503(a)(2) and if earned only in the Chapter 11 case, are subordinate to Chapter 7 administrative expenses pursuant to Code §726(b).

The Court begins its analysis with the nature of the retainers paid herein to Damon and Freed, respectively. It appears that all parties are in agreement that the Court need only focus its attention on two types of retainers. The first is an "advance payment retainer" defined by the bankruptcy court in In re McDonald

Bros. Const., Inc., 114 B.R. 989, 1000 (Bankr. N.D.Ill. 1990) as a pre-petition payment made for future post-petition services which is considered fully earned upon receipt, is non-refundable and is not property of the bankruptcy estate. The second is a "security retainer", likewise defined in McDonald Bros. Const. Inc., supra, as a pre-petition payment for services to be rendered post-petition; however, the retainer even though held by the professional in escrow constitutes property of the estate subject to the professional's security interest. Id at 999.

At the outset, the Court will examine New York law vis a vis non-refundable retainers. The leading case appears to be Matter of Cooperman, 83 N.Y.2d 465, 633 N.E.2d 1069, 611 N.Y.S.2d 465 (N.Y. 1994), in which the New York Court of Appeals held that special advance payment non-refundable retainer agreements are unenforceable and may subject the attorney to professional discipline because these fee agreements compromise the client's right to terminate the unique fiduciary attorney-client relationship. Id. at 471. The Court stated, "Moreover, we intend no effect or disturbance with respect to other types of appropriate and ethical fee agreements (See Brickman and Cunningham Non-refundable Retainers Revisted, 72 N.C.L. Rev. 1, 6 [1993]). Minimum fee arrangements and general retainers that provide for fees, not laden with the nonrefundability impediment irrespective of any services, will continue to be valid and not subject in and of themselves to professional discipline." Id. at 476.

In urging the Court to reach the conclusion that they were the recipients of advance payment retainers, Damon & Freed

argue for the Court's reliance upon McDonald Bros., supra, 114 B.R. at 1000, and the conclusions of the late Bankruptcy Judge Howard Schwartzberg in In re D.L.I.C., Inc., 120 B.R. 348 (Bankr. S.D.N.Y. 1990).

In re D.L.I.C. Inc., supra, is of questionable precedent for Damon & Freed's advance payment retainer argument since Judge Schwartzberg, in reliance on New York law, simply acknowledged the existence of such a retainer and that it would not become property of the debtor's estate but concluded that the objecting creditors had failed to present sufficient facts from which the Court could determine the nature of the retainer. Further, Judge Schwartzberg's conclusion was reached prior to the Cooperman decision that advance payment non-refundable retainers were not permissible in New York State. It is not clear that he would have reached the same conclusion had he had the benefit of Cooperman.

The Court believes that the better view is that enunciated by Bankruptcy Judge E. Stephen Derby in In re Printing Dimensions, Inc., 153 B.R. 715 (Bankr. D.Md. 1993) where he was confronted with facts similar to the matter sub judice and was asked to determine the nature of a $20,000 pre-petition retainer. Counsel for debtor in that case argued that what it had received pre-petition was an engagement retainer earned upon receipt and, therefore, not property of the estate. The Court disagreed concluding that the retainer was in the nature of an advance payment and while acknowledging what the Court characterized as a minority view that advance payment retainers do not constitute property of the estate, concluded that the concept of earned

retainers is contrary to the whole concept of Chapter 11 reorganizations and the bankruptcy court's role in approving professional compensation. Relying on both Maryland law and the bankruptcy court's rationale in In re NBI, Inc., 129 B.R. 212 (Bankr. D.Colo. 1991), Judge Derby concluded that the retainer was property of the debtor's estate and that application of the retainer to services rendered was subject to bankruptcy court approval.

The alternative argument of Damon and Freed that their retainers were in the nature of security for future payment of their fees appears to be the more tenable position. Clearly, however, a security retainer constitutes property of the estate. See S.E.C. v. Towers Financial Corp., 1993 WL 276935 (S.D.N.Y. 1993), In re Interstate Department Stores Inc. , 128 B.R. 703 (Bankr. N.D.N.Y. 1991); and McDonald Bros., supra, 114 B.R. at 999. As the Chapter 7 Trustee points out, the very language of the retainer agreements executed by Damon and Freed make reference to the retainers as being "security".

There is significant authority that to the extent the professional holds a security interest in the retainer it is not subject to the pro rata payment of other administrative claimants as the Trustee suggests. See Printing Dimensions, supra, 153 B.R. at 719; and Interstate Department Stores, supra, 128 B.R. at 706. The UST, while assuming arguendo that Damon and Freed hold security retainers, asserts that the security interest must be limited only to the value of the services rendered pre-petition. To hold otherwise contends the UST would place the professional with a

security retainer in a better position than other secured creditors who are secured only to the extent of their allowed claim on the date of filing.

The UST acknowledges the existence of several cases which hold that a security retainer secures both pre and post-petition services. See In re Matthews, 154 B.R. 673, (Bankr. W.D.Tex. 1993); In re Viscount Furniture Corp., 133 B.R. 360 (Bankr. N.D.Miss. 1991); Interstate Department Stores, supra, 128 B.R. at 706; Matter of K & R Min., Inc., 105 B.R. 394 (Bankr. N.D.Ohio 1989); In re Burnside Steel Foundry Co., 90 B.R. 942 (Bankr. N.D.Ill. 1988) and In re Kinderhaus Corp., 58 B.R. 94 (Bankr. D.Minn. 1986), but see contra In re Rittenhouse, 76 B.R. 610 (Bankr. S.D.Ohio 1987). The UST argues, however, that none of these cases with the exception of Burnside, actually analyze their conclusions, and he suggests that Burnside's analogy of the professional's security retainer to the security deposit of a landlord, to insure payment of future rents is flawed because a lease rejection claim of a landlord which arises post-petition is actually "transformed" into a pre-petition claim by virtue of Code §502(g). No such comparable provision "transforms" a post-petition claim for attorney's fees into a pre-petition debt.[12]

Additionally, the UST suggests that such an

[12] The Chapter 7 trustee in K & R Min., Inc., supra, 105 B.R. at 397-98, actually advanced the very same argument as the UST advances herein regarding extension of the security retainer to post-petition services. While the Court rejected the trustee's argument, it did so by seemingly straining to conclude that to the extent Code §364 might be applicable to post-petition services, creditors had sufficient notice of the retainer arrangement constituting a security interest.

interpretation significantly erodes the concept of Code §503(b)(2) by which Congress granted "administrative" not "secured" status to post-petition professional fees. Finally, the UST opines that embracing the concept that a pre-petition retainer secures payment of post-petition services prejudices the unsecured creditors in many ill-fated Chapter 11 cases such as this one that had no reasonable prospect of reorganization.

Acknowledging that it is contrary to the weight of current authority, this Court finds merit in the UST's argument. While Code §506(a) does not limit an "allowed claim" to one existing only pre-petition, it appears that absent an exercise of rights pursuant to Code §362, 363, 364 or 365, a creditor's secured claim is fixed as of the date of filing. So too argues the UST, must the claim of a professional to the extent that it is secured by a retainer, be limited to amount due on the date of filing. The balance of any security retainer in excess of the allowed pre-petition fee claim renders the professional oversecured and presumably entitled to the benefits of Code §506(b). To create, however, a special class of secured creditors whose secured claim continues to increase in amount post-petition to the detriment of other creditors, both priority unsecured and non-priority unsecured, seems to fly in the face of the general scheme of payment established by Congress, especially the scheme of payment mandated by Code §§503(b)(2), 507(a)(1) and 726(b).

While a professional holding a pre-petition security retainer would undoubtedly argue that unlike other pre-petition secured creditors, it continues to render services post-petition in

reliance upon the existence of the security retainer, that reliance may not be either reasonable nor justified given the clear language of Code §§503(b), 507(a)(1) and 726(b).

In a somewhat analogous situation, this Court in In re French, 111 B.R. 391, 393 (Bankr. N.D.N.Y. 1989) held that a specific section of New York State law which conferred lien status on an attorney who rendered pre-petition services to a debtor that directly resulted in a post-petition recovery did not serve as the basis for approving payment post-petition absent an appointment pursuant to Code §327(a).

Following the majority view under the facts of this case clearly points out the fundamental unfairness that is visited upon other administrative creditors who have dealt with the Chapter 11 debtor post-petition. Their claims will go largely unpaid in this case while the Debtor's professionals retain approximately $50,000 which will be applied to full payment of their pre and post-petition claims. Perhaps even more significant is the possibility that the Trustee in the converted case, whose administrative expenses (the so called "burial expenses") are given priority under Code §727(b), may also remain partially unpaid.[13]

Thus, this court is compelled to reach the conclusion urged by the UST and the Trustee that while Damon and Freed possess security retainers, those retainers are security only to the extent of services performed pre-petition. As to the balance of the

[13] The Court estimates that if Damon and Freed are paid 100% of the Fee & Disbursement Request approved by the Court, the estate will be left with a balance of unused retainers totalling approximately $7,000.

retainers, they are to be turned over to the Trustee for application in accordance with Code §726, specifically §726(b).

Based upon the foregoing, it is

ORDERED that Damon is awarded fees in the total sum of $28,963.56 and disbursements of $4,773.58 and shall be paid immediately the secured portion of said fee award in the sum of $7,467.00 and the secured position of said disbursements in the sum of $1,520.06, and it is further

ORDERED that Freed is awarded fees in the sum of $17,421.30 and disbursements of $343.74 and shall be paid immediately the secured portion of said fee award in the sum of $13,577.50 and the secured portion of said disbursements in the sum of $343.74, and it is finally

ORDERED that the balance of any retainers being held by Damon and/or Freed shall be paid over to the Trustee within twenty (20) days of the date of this Order and shall be subject to a further order of this Court.

Dated at Utica, New York
this day of February 1996

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STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge