UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

HOUSEHOLD MERIT, INC. — CASE NO. 94-62969

Debtor — Chapter 11

APPEARANCES:

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Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

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

On January 17, 1995, the Debtor moved this Court for an order reconsidering its prior Order of December 30, 1994, appointing Freed, Maxick, Sachs & Murphy ("Freed Maxick") as Debtor's accountants effective December 1, 1994, as well as its prior Order of December 7, 1994 appointing Damon & Morey, Esqs. ("Damon") as Debtor's attorneys effective November 7, 1994.

The motion was argued at a motion term of this Court held at Utica, New York on January 31, 1995. The motion was partially opposed by the United States Trustee ("UST") and following oral

argument, the Court reserved decision.

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).

FACTS

Debtor, which operated retail furniture stores in Watertown and Potsdam, New York, filed a voluntary petition pursuant to Chapter 11 of the Bankruptcy Code (11 U.S.C. §§101-1330) ("Code") on October 31, 1994.

On November 7, 1994, Debtor submitted an Application and proposed order appointing Damon as Debtor's counsel to the UST for its review. The Court, pursuant to the comments of the UST noting certain deficiencies, returned the Application and proposed order to Damon on November 17, 1994. Damon resubmitted the Application and proposed order to the UST on November 25, 1994. The Application and proposed order were then approved by the UST on December 7, 1994 and, thereafter, the Court executed an Order on the same date, appointing Damon as Debtor's attorney effective November 7, 1994.

Similarly, on December 1, 1994, Debtor submitted an Application and proposed order seeking the appointment of Freed Maxick as Debtor's accountant. That Application and proposed order were, likewise, returned to the Debtor by the UST for revision on

December 8, 1994, then resubmitted on December 19, 1994 and ultimately approved by the UST on December 28, 1994. An Order was executed by the Court on December 30, 1994, appointing Freed Maxick as Debtor's accountants, effective December 1, 1994.[1]

ARGUMENTS

Debtor argues that the Court should reconsider its Orders of Appointment pursuant to Federal Rule of Bankruptcy Procedure (Fed.R.Bankr.P.) 9024 and make the appointment of both Damon and Freed Maxick retroactive to October 31, 1994, the date Debtor's Petition was filed.

In support of that relief, Debtor acknowledges that bankruptcy courts generally require the appointment of a professional pursuant to Code §327 prior to the professional being eligible for any compensation. However, Debtor asserts that this so-called "*per se*" rule is no longer rigidly applied by bankruptcy courts in the Second Circuit because, *inter alia*, it is allegedly a trap for the unwary.

Additionally, the Debtor contends that Damon and Freed Maxick were relying on the local practice of the U.S. Bankruptcy Court for the Western District of New York where a professional who seeks appointment pursuant to Code §327 and files an application

[1] On February 16, 1995, following a status conference, this Court ordered the conversion of Debtor's case to one pursuant to Chapter 7 of the Code. Thus, any future compensation awarded to Damon or Freed Maxick in connection with services to be rendered to the Chapter 11 Debtor will be subordinated to the administrative claims incurred in the present Chapter 7 case. See Code §726(b).

for appointment within 30 days following the filing of a petition will be appointed retroactive to the date of filing.

Finally, Debtor asserts that Freed Maxick is an innocent third party in that it relied on Damon to obtain its appointment and that it rendered valuable services in reliance upon its reasonable belief that it would be appointed in a timely manner.

The UST contends that the "*per se*" rule still applies in the Second Circuit and that the only exception to it is a finding of excusable neglect. The UST points out that the local rules of the Western District of New York regarding appointment of professionals do not contain provisions similar to those of the Northern District of New York and Debtor should have been aware of the lack of any 30 day grace period in the local rules of this District.

The UST does not, however, oppose the motion for reconsideration insofar as it applies to Damon, since in spite of its reliance on a local rule having no application in this District, the Debtor did file its application for appointment of Damon within approximately one week of the filing of Debtor's petition. However, the UST opposes any reconsideration of the Freed Maxick appointment Order upon the ground that even if the Debtor correctly relied on the 30 day reach back period employed in the Western District of New York, it did not file its application for Freed Maxick's appointment until more than 30 days post filing. The UST can find no basis to employ an excusable neglect exception

to the *per se* rule.[2]

DISCUSSION

The subject of *nunc pro tunc* appointment of professionals in bankruptcy cases has been at the heart of a great deal of case law since the adoption of the Bankruptcy Reform Act of 1978. It can be said with a degree of certainty that within the Second Circuit, the so-called " *per se*" rule, which is generally the antithesis of *nunc pro tunc* appointment, has been applied fairly consistently. In re Rogers-Ryatt Shellac Co., 51 F.2d 988 (2d Cir. 1931), In re Progress Lektro Shave Corp. 117 F.2d 602 (2d Cir. 1941), In re Sapphire S.S. Lines, Inc. 509 F.2d 1242 (2d Cir. 1975). There is little argument that the " *per se*" rule, which denies compensation to a professional who renders pre-appointment services to a debtor, is a harsh rule. However, this Court is not prepared to concede that it is likewise a trap for the unwary.

The "*per se*" rule recently came under scrutiny by the U.S. Bankruptcy Court for the Western District of New York in the case of In re Piecuil, 145 B.R. 777 (Bankr. W.D.N.Y. 1992). In that case, Chief Bankruptcy Judge Michael Kaplan analyzed the history of the *per se* rule in the Second Circuit and concluded that "it can still be said today, as it was in 1983, that 'It is fair to note... that in most of these decisions some additional reason for

[2] The Court notes that the Debtor also sought an order shortening the time to 60 days within which it could make an interim fee application pursuant to Code §331. The UST did not oppose that relief, however, it became moot upon the conversion of the case to Chapter 7.

disallowing payment of fees is shown absent the mere failure to secure a prior order, a reason that would have precluded proper issuance of the order authorizing the employment.'" Id. at 783, quoting In re Triangle Chemicals, Inc., 697 F.2d 1280 (5th Cir. 1983). It is, thus, Judge Kaplan's view that while the *per se* rule may still have relevance in the Second Circuit, it has been misconstrued by some bankruptcy courts as being grounded solely on the failure to secure timely appointment, when in fact in almost every early Second Circuit decision out of which the rule grew, there were other reasons to deny appointment of the professional even if timely appointment had been sought.

This Court is likewise of the opinion that the *per se* rule need not be mechanically applied in every case where the professional fails to seek timely appointment, however, it does hold the view that the only recognized exception to the rule is excusable neglect and that exception should not be expanded to the point where it subsumes the rule itself. See In re Robotics Resources R2, Inc., 117 B.R. 61, 62 (Bankr. D.Conn. 1990); In re French, 111 B.R. 391, 394 (Bankr. N.D.N.Y. 1989).

In the instant case, Damon, a firm with a substantial business and litigation practice, as well as expertise in representing Chapter 11 debtors, assisted the Debtor in the filing of its voluntary Chapter 11 petition on October 31, 1994. (See Declaration of William Savino, Esq. dated November 4, 1994, filed in support of Debtor's Application for employment of Damon.) It did not, however, submit its application for appointment to the UST until November 7, 1994. The only significant reason given for

its delay of one week was that it believed it was entitled to rely on the local rules of bankruptcy practice for the Western District of New York when it could find no local rules of practice in this District on point and since it was unaware of any specific prohibition against retroactive appointments. (See the undated Declaration of Henry Gitter, Esq. at paragraphs 4-9, submitted in support of the instant motion.) This Court is unable to find excusable neglect in such an explanation by Damon. In fact, the Court did appoint Damon retroactive to November 7, 1994, the date on which it filed its Application initially, even though the Application had to be revised due to the UST's Objection and was re-submitted to the Court a month later on December 7, 1994.

Turning to the Application of Freed Maxick, the Court notes that Debtor's Application seeking its appointment as accountant was dated November 29, 1994 and was first submitted to the UST for review on December 1, 1994. Even assuming Debtor was entitled to rely on the local rules of the Western District of New York, it did not follow the 30 day retroactivity rule with regard to the Freed Maxick Application for appointment.

Debtor asserts that Freed Maxick is an innocent third party which relied upon Damon to prepare its application for appointment much the same as the accounting firm had done in Piecuil, supra 145 B.R. at 783. While there is merit to that argument and this Court has been persuaded on prior occasions to view the plight of the non-attorney professional seeking appointment in a more favorable light, particularly where it is apparent that the non-attorney has executed the necessary documents

in the good faith belief that they will be presented to the Court in due course, the facts presented here do not provide a basis for such persuasion.

The moving papers contain the Affidavit of Howard Rein, CPA, a director of Freed Maxick, which simply parrots the explanation of Debtor and Damon, that he was unaware of the lack of a retroactivity rule similar to that prevailing in the Western District of New York and that Freed Maxick relied in good faith on Damon to have a knowledge of the local rules and procedures. It is not apparent, however, that Rein is contending that he executed the necessary application for appointment of Freed Maxick significantly prior to December 1, 1994, at or about the time of Debtor's filing, and that thereafter he relied in good faith on Damon's assertions that it would process the Application forthwith.[3]

As in the case of Damon, the Court did appoint Freed Maxick effective the date the Application was first received by the UST, namely December 1, 1994, even though the proposed order and revised Application in proper form did not reach the Court until December 28, 1994.

Based upon all of the foregoing, the Court sees no reason to modify the Orders of December 7, 1994 and December 30, 1994, appointing Damon and Freed Maxick, respectively. Thus, Debtor's motion for reconsideration will be denied.

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[3] The Court notes that Rein's Declaration in support of the appointment of Freed Maxick was executed on December 15, 1994, though it is apparent that this was the second such Declaration executed by Rein.

IT IS SO ORDERED.

Dated at Utica, New York

this 14th day of April 1995

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge