UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

THE LOST FORESTS, INC.,
d/b/a THE LOST FOREST — CASE NO. 93-63583

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 August l7, 1994, Costello, Cooney & Fearon ("CCF"), Debtor's counsel, appointed pursuant to an Order of this Court dated January l9, 1994, effective December 7, 1993, filed an Application for First Interim Allowance of Compensation ("Fee Application"). The Fee Application which covered the period December 7, 1993 through August l, 1994 seeks a fee of $45,898 plus expenses in the sum of $4,081.75 and appeared on the Court's motion calendar at Syracuse, New York on September 13, 1994. Argument on the motion was thereafter adjourned to October 4, 1994 on the consent of the parties.

The United States Trustee ("UST") filed an objection to the Fee Application on September 12, 1994 and a Supplemental Objection thereto on September 29, 1994.

On September 26, 1994, this Court entered a consensual order awarding CCF partial fees of $4,530.70 and reimbursement of expenses in the amount of $4,081.75.

Both parties were given until October 24, 1994 to file memoranda of law with regard to the balance of the Fee Application. On October 21, 1994, CCF filed a further Affirmation In Support of the Fee Application.

JURISDICTIONAL STATEMENT

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

FACTS

Debtor, a California corporation, filed a voluntary petition pursuant to Chapter ll of the Bankruptcy Code (11 U.S.C. §§101-1330)("Code") on December 2, 1993. Prior to, or at the time of filing, Debtor was involved in the operation of three retail stores, one located in Mall of America, Minneapolis, Minnesota, one located in Marketplace Mall, Rochester, New York and one located in Carousel Mall, Syracuse, New York. Of the three stores, it appears that only the Syracuse location was under the sole operation and control of the Debtor on the date of filing.

Between the date of filing and July 1994, the Debtor was a party to litigation in this Court involving all three store locations and by July 1994, Debtor had apparently ceased operations at all three locations.

During the course of the Chapter 11 case, the Debtor has filed neither a plan nor disclosure statement.[1]

ARGUMENTS

The UST contends generally that CCF should have realized as early as February 8, 1994 that Debtor's business was not reorganizable and at that point CCF should have embarked upon an orderly liquidation of the Debtor. As a result, the UST seeks to reduce the Fee Application for services rendered post February 1994 by 66%.

The UST also cites to CCF's representation of the Debtor between May and July 1994 in a contempt proceeding filed against the former landlord of the Rochester, New York store for an alleged intentional violation of the automatic stay. UST asserts that Debtor, presumably on CCF's advice, settled the contested matter for $7,500 which amount was further reduced by storage charges of $2,477 resulting in a net to the Debtor of $4,078.50 from which CCF seeks a fee of $3,421.50, leaving $657.00 for the Debtor's creditors. The UST posits that CCF should be denied all fees in

[1] On November 25, 1994, this Court entered an Order, on motion of the UST, converting the case to one filed pursuant to Chapter 7 and, thus, any fees awarded herein are subject to subordination in accordance with Code §726(b).

connection with the contempt motion.

The UST also criticizes CCF's handling of the Debtor's lease of the Syracuse store premises during the period December 1993 through March l994, asserting that initially Debtor "mounted a vigorous defense" of motions filed by the Syracuse landlord, then settled, vacated the premises and agreed to allow the landlord an administrative claim of approximately $10,000. (See UST's Supplemental Objection dated September 28, 1994, ¶l6)

Also of concern to the UST was what it characterizes as "an inordinate amount of time for research on basic principals (sic)" performed by a CCF associate (See UST's Supplemental Objection dated September 28, 1994, ¶17). The UST alleges an "administrative overkill" emanating from "internal review of work product or internal conferences" conducted by CCF (Id. at ¶18)

Lastly, the UST urges this Court to consider the "lack of positive result obtained, or benefit to the estate," in passing upon the Fee Application. (Id. at ¶20)

CCF disputes UST's allegations that Debtor was not reorganizable after February 8, 1994, asserting that Debtor's monthly operating reports were prepared on an accrual basis rather than a cash basis and thus reflected disbursements for which the Debtor was ultimately liable, but which were not actually paid.

CCF argues that initially Debtor's plan was "to stave off an eviction proceeding" at the Syracuse store location and "to gain control of the stores operated by Debtor's co-ventures in Minneapolis, Minnesota and Rochester, New York." (See Affirmation of Michelle C. Lombino, Esq., dated October 20, 1994, ¶3)

Following poor Christmas 1993 and January 1994 sales, CCF contends that Debtor decided to close the Syracuse store, but forged ahead with plans to regain control of the Minneapolis and Rochester stores. With regard to the Minneapolis store, Debtor was successful in regaining possession having commenced an adversary proceeding which ended in a Stipulation of Settlement on April 1, 1994. Likewise, the Debtor negotiated a Stipulated Settlement with its co-venturer for possession of the Rochester store.

CCF argues that its representation of Debtor in regaining possession of the Minneapolis and Rochester Stores resulted in desirable results since both stores had been profitable while in the operational control of Debtor's co-venturers. CCF also asserts that a Chapter 11 debtor's counsel is not guarantor of a Debtor's economic success and that if that were true a Chapter 11 debtor's counsel would rarely be compensated.

CCF defends its fee request as it relates to time consumed in conferencing by two or more of its attorneys, arguing that it was necessary that both Michael Religa, Esq. and Michelle Lombino, Esq. work on different aspects of the case and thus the need for frequent intra-office conferencing.

Finally, CCF suggests that if the UST did not feel that the Debtor's Chapter 11 case was viable, it should have sought to convert or dismiss the case in its initial stages.

DISCUSSION

The fee application and the objection of the UST presents

the Court with a dilemma which is not easily resolved. Reduced to its simplest form, it requires the Court to invoke 20/20 hindsight in determining whether CCF is entitled to the fees and disbursements it seeks.

As CCF appropriately points out, a Chapter 11 debtor's attorney need not guarantee a successful reorganization as a condition precedent to payment of its fees. Conversely, a debtor's counsel should not necessarily be fully compensated for hours consumed in what becomes a futile exercise ultimately ending in conversion to Chapter 7 where the futility should be recognized by counsel well in advance of the actual conversion. See In re Vines, Inc., 159 B.R. 381 (Bankr. D.Mass. 1993)

The instant Chapter 11 case was filed on December 2, 1993. It involved a flurry of litigation very early in its pendency, and then slipped slowly under the wave of Chapter 7 conversion less than a year later never having spawned a plan of reorganization or liquidation.

The UST argues that as early as February 8, 1994, CCF should have determined that the Debtor was not reorganizable and promptly proceeded with a plan of liquidation. The UST points to the Debtor's monthly operating reports and its deteriorating negotiations with Debtor's landlords at its three mall stores as proof that in February CCF should have counselled the Debtor to liquidate. Having failed to so counsel the Debtor, posits the UST, CCF should suffer a 66% reduction in fees sought by CCF after February 8th. See In re Old South Transp. Co., Inc., 134 B.R. 660, 662 (Bankr. M.D.Ala. 1991)

The Court cannot agree with the UST's contention that CCF should be penalized to the extent of denying 66% of its requested fee because it did not insist that the Debtor liquidate on or after February 8, 1994. CCF argues that it was able to accomplish the Debtor's two immediate goals, the first being to stave off its eviction from the Syracuse store at least until after Christmas 1993 and the second being to regain control of its Rochester and Minneapolis stores from its co-venturers.

CCF suggests, and the Court concurs, that in the early stages of any Chapter 11 case, particularly one where the debtor is a tenant, simply avoiding lease termination and eviction is a debtor's paramount concern. It is a rare debtor, indeed, who will be in a position within the first month or so of its Chapter 11 case to make a well reasoned business decision as to the feasibility of assuming or rejecting the lease of its retail premises. In fact, Code §365(d)(4) automatically grants a debtor at least 60 days in which to move to assume non-residential leases. While it appears to be true that the Debtor was experiencing serious difficulties at all three of its retail locations pre-petition, that is insufficient to charge Debtor's counsel with incompetence in failing to recommend liquidation to its client approximately two months post-filing.

What is somewhat perplexing to the Court, however, is why the Debtor so actively pursued the ouster of its co-venturers in both Rochester and Minneapolis, only to apparently discover that upon gaining singular control of the stores' operations, in one case Debtor was locked out and in the other Debtor succumbed to a

consensual order lifting the stay, leading to its eviction by June 1994. The Court further questions the propriety of the settlement of the contempt litigation against the Rochester landlord for an intentional violation of the stay at $7,500 if in fact the Debtor was "cash poor" at the time of settlement. CCF seeks a fee of $3,421.50 for the hours expended in effectuating the settlement. This fee request represents approximately 45% of the recovery and the Court will reduce that fee to 25% or $1,875, thus, disallowing $1,546.50.

The Court finds persuasive the UST's criticism of CCF incurring significant time researching issues of law. In spite of the apparent fact that some of CCF's representation of Debtor involved interpretation of non-bankruptcy law, attorneys will not be allowed to educate themselves with regard to Title 11 of the United States Code at a significant expense to a debtor's creditors. Thus, the Court will allow a fee of $1,000 for services devoted to legal research and disallow the balance of $3,393.25. See In re. S.T.N. Enterprises, Inc., 70 B.R. 823, 837 (Bankr. D.Vt. 1987)

Likewise, and in spite of CCF's explanation that the case required two attorneys' direct involvement, thus necessitating numerous intra-office conferences, the Court will disallow all but $2,000 of the $4589.00 devoted to said conferencing. See In re Adventist Living Centers, Inc, 137 B.R. 692, 697 (Bankr. N.D.Ill. 1991)

Finally, while the UST's criticism of CCF's overall representation of this Debtor does have merit, the Court's

familiarity with the case suggests that CCF was laboring under some difficulty in dealing with a Debtor whose principal was not readily accessible being a foreign national as well as a Debtor which was already embroiled in significant disputes with its creditors when it sought to reorganize under Chapter 11. As CCF points out in its responsive papers, it was not obligated to guarantee the Debtor's successful reorganization and while the "results obtained" in terms of benefit to the Debtor's creditors is not clearly discernible at this point, the Court will approve CCF's fees as follows:

Fee Requested	$45,898.00
Adjustment for settlement of contempt motion	-1,546.50
Adjustment for legal research	-3,393.25
Adjustment for intra-office conferencing	-2,589.80
Fee Approved	$38,368.45
Minus portion of Retainer applied pursuant to Order of Court dated 9/26/94	-4,530.70
	$33,837.75

CCF's request for disbursements in the sum of $4,081.75 was previously approved by Order of the Court dated September 26, 1994.

In light of the conversion of this case to Chapter 7 by Order dated November 25, 1994, the fees awarded herein will be subordinated to any administrative expenses incurred in the Chapter 7 case. See Code §726(b).

Thus, CCF is directed to immediately turn over to the Chapter 7 Trustee, Allan Bentkofsky, Esq., the balance of funds, if any, being held in its escrow account on behalf of Debtor as

designated in the Fee Application at ¶35.

IT IS SO ORDERED.

Dated at Utica, New York

this day of January 1995.

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STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge