

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF ALABAMA

IN RE:

GREAT AMERICAN AMUSEMENT,
INC.,
Debtor.

CASE NO. 99-11060-WSS
Chapter 7

IRVIN GRODSKY, P.C.,
Plaintiff

v.

ADV. PROC. NO. 01-1169

LYNN HARWELL, Chapter 7 Trustee,
ELMER L. COOK, II,
Defendants.

ORDER ON COMPLAINT AND COUNTERCLAIM

Irvin Grodsky, Attorney for the Plaintiff
Lionel Williams, Attorney for the Trustee
Lynn Harwell Andrews, Trustee

This matter is before the Court on the Plaintiff's complaint to determine the validity, priority, or extent of a lien, and the Defendant's counterclaim to invalidate a lien and turnover funds. The Court has jurisdiction to hear this matter pursuant to 28 U.S.C. §§ 157 and 1334 and the Order of Reference of the District Court. This matter is a core proceeding pursuant to 28 U.S.C. §157(b)(2).

FINDINGS OF FACT

The Debtor, Great American Amusement Inc. ("Great American"), filed a Chapter 11 petition on March 22, 1999, and the Court approved the Plaintiff, Irvin Grodsky, P.C. ("Plaintiff"), as counsel for Great American under a general retainer agreement. Great American paid the Plaintiff a retainer of \$1,000.00.

The Court approved two of the Plaintiff's applications for allowance of interim compensation. As of August 7, 2001, Great American owed the Plaintiff \$27,914.47 in approved fees and costs for immediate payment, and \$1,430.00 in approved fees and costs for deferred payment. The total of approved costs and fees is \$29,344.47.

The funds at issue are connected with the confirmation of the Debtor's third amended plan. The terms of its third amended required Great American to make substantial payments on the confirmation date to the first mortgage holder, Kennedy Funding, Inc. ("Kennedy"), and to pay real property and ad valorem taxes. To show the feasibility of the plan, the Court required Great American to have all monies payable on the confirmation date placed in the Plaintiff's trust account on or before the February 20, 2001 confirmation hearing.

On February 16, 2001, Elmer Cook Construction ("Cook Construction") transferred \$55,000.00 to the Plaintiff's trust account for the required payments under the third amended plan. No documentation authorizing the transfer of the funds or the use of the funds by the Debtor was ever presented to or obtained from the Court. Joseph Morgan, a principal of the Debtor, represented that the funds from Cook Construction were actually loaned to Sunshine Properties, Inc. ("Sunshine"), a company owned by the principals of the Debtor. Sunshine allowed the Debtor to use the funds.

The following payments were made from the deposited funds:

3-7-2001	\$27,151.25	Kennedy
3-7-2001	\$3,000.00	Sunshine Prop.
3-30-2001	\$10,000.00	Sunshine Prop.
6-6-2001	\$7,100.00	Kennedy
7-19-2001	\$7,100.00	Kennedy

The payments to Kennedy were made pursuant to an adequate protection agreement approved by the

Court. The Court did not approve Sunshine's receipt of the funds and was not asked to approve transfer of the funds. The first payment of \$7,100.00 to Kennedy was replaced by a check from the Debtor's DIP account on July 6, 2001. The balance in the trust account on July 19, 2001 was \$7,697.50.

It was intended that the Debtor would replace the July 19, 2001 payment of \$7,100.00 to Kennedy before the adjourned confirmation hearing set on August 7, 2001. Prior to the August 7th hearing, the Debtor had a check drawn on its DIP account for \$7,100.00 payable to the Plaintiff's trust account. At the August 7, 2001 hearing, the Debtor's case was converted to a Chapter 7 case by the Court. Immediately after the hearing, the Plaintiff received the \$7,100.00 check described above, cashed it and obtained a cashier's check with the proceeds payable to the Plaintiff's trust account. The cashier's check was then delivered to counsel for the Trustee. At the time that the Debtor's case was converted from a Chapter 11 to a Chapter 7 proceeding, the Plaintiff had \$7,697.50 in its trust account for the Debtor and then delivered the \$7,100.00 cashier's check.

CONCLUSIONS OF LAW

The Plaintiff asks the Court to find that the Plaintiff has a valid retaining lien on the \$7,697.50 held in its trust account pursuant to Ala. Code §34-3-61(a) (1975), and that the funds can be applied to the unpaid balance of previously awarded fees and expenses. The Trustee asserts that the Bankruptcy Code does not allow postpetition retaining liens, and that the lien is invalid because the Plaintiff's legal services are unrelated to the creation of the funds at issue. The Trustee also maintains that even if the lien is valid, it can be avoided under 11 U.S.C. §545(a).

The Court first must address the Trustee's objection that the Plaintiff does not have a retaining lien under Alabama law because the Plaintiff's services rendered to the Debtor did not generate the funds at issue. The Plaintiff disagrees, and asserts that the monies were placed in its trust account to

fund a plan negotiated and prepared by the Plaintiff. Without the Plaintiff's work on the plan, there would have been no funds deposited with the Plaintiff. From the Court's perspective, the chapter 11 plan devised by the Plaintiff did not call for the Debtor to make deposits to be held by the Plaintiff. The Court required the deposits to be made as a condition of confirmation because there was no direct evidence that the Debtor had the funds to make the payments called for in the plan. The Plaintiff would not have had the funds in its trust account but for the Court's condition of confirmation. Therefore, it is difficult to find that the funds at issue were generated by the Plaintiff's services to the Debtor. Section 34-3-61(a) is usually applied when an attorney brings an action on behalf of a client and generates a pool of funds to which the attorney's lien can attach. This is not the present situation. While it is true that the Plaintiff performed valuable services for the Debtor in devising the plan, the Plaintiff's work did not result in a monetary award for the Debtor. However, the language of §34-3-61(a) is broad: "Attorneys-at-law shall have a lien on all papers and money of their clients in their possession for services rendered to them, in reference thereto. . .". On its face, the Plaintiff can technically argue that the funds in its possession are for services rendered to the Debtor. Therefore, the Court will assume, but will not decide, for the sake of this decision only, that the Plaintiff has a valid retaining lien under §34-3-61(a).

The primary issue before the Court is whether an attorney's postpetition retaining lien created under state law can attach to funds held by the Debtor's attorney. As the Plaintiff points out, the Bankruptcy Code does not address this issue. Postpetition retaining liens are neither prohibited or allowed under the Bankruptcy Code. Courts that have considered whether retaining liens can be imposed for postpetition services have generally held that the liens are not allowed under the Bankruptcy Code or that they are preempted by the Bankruptcy Code's provisions for the award of attorney fees. The bankruptcy court in *In re Printcrafters, Inc.*, 208 B.R. 968 (Bankr. D. Colo. 1977)

dealt with a prepetition fee retainer still held by the debtor's counsel at the time of conversion from chapter 11 to chapter 7. In determining whether an administrative expense claim could be secured with a postpetition attorney's fee retaining lien, the court stated:

Considering the Code as a whole and the policies behind it, this Court is convinced that recognition of the Colorado retaining lien for postpetition services rendered to a trustee or debtor-in-possession is incompatible with and superseded by bankruptcy law. . . . Secret, automatic liens which prime other administrative expense claims are inconsistent with the Code's elaborate priority scheme and with the requirement that creditors be given notice of and an opportunity to object to the creation of postpetition liens under §§363 or 364.

Printcrafters, 208 B.R. at 978. Similarly, the court in *In re Sea Catch, Inc.*, 36 B.R. 226, 235 (Bankr. D. Alaska 1983) noted that: "Pursuant to the Supremacy Clause of the Constitution, specific Bankruptcy Code and corresponding rule provisions regarding the award of attorney fees [including §§ 327, 328, 330 and 1107] cannot be superseded by an attempt to give a post-petition effect to a state created lien as far as post-petition services are concerned." A bankruptcy court within the Eleventh Circuit has also address the issue of postpetition liens. In *In re Studebaker's of Fort Lauderdale*, 104 B.R. 411 (Bankr. N.D. Fla. 1989), special counsel approved to pursue a state court action on the debtor's behalf requested a charging lien under Florida law against the proceeds from the action. The debtor's bankruptcy petition was originally a chapter 11 case and was later converted to chapter 7. The parties agreed that the special counsel was entitled to the fees approved by the court; however, the Trustee objected to special counsels request for a charging lien to guarantee payment of the fee. The Trustee argued that the fees were an administrative expense and should be paid under §507 of the Code dealing with priorities. *Studebaker's* 104 B.R. at 412. The bankruptcy court found no authority for allowing a post-petition charging lien to set aside the priorities of §507, and went on to reason:

“Indeed, good sense and the plain language of the Bankruptcy Code advise otherwise. The Code clearly contemplates the payment of expenses incurred in collecting and distributing the assets of the bankruptcy estate. Congress specifically set forth in Section 507 the priority by which those expenses should be paid.” *Studebaker’s*, 104 B.R. at 413.

Based on case law outlined above, this Court finds that the Plaintiff cannot assert a postpetition retaining lien against the funds held in its trust account. The Plaintiff has an administrative expense which must be paid according to the priority set out by the Bankruptcy Code. The Court finds that the relief sought in the Plaintiff’s complaint should be denied, and the funds held by the Plaintiff should be turned over to the Chapter 7 Trustee as property of the estate. It hereby

ORDERED that the relief sought in the Plaintiff’s complaint is **DENIED**, and the funds held by the Plaintiff shall be turned over to the Chapter 7 Trustee within 7 days of the date of this order.

Dated: August 9, 2002