

**UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF FLORIDA
TAMPA DIVISION**

In re:

Case No. 8:04-bk-20591-PMG
Chapter 11

FINAO CORPORATION,
d/b/a Memorial Sleep Center,
d/b/a Memorial Hospital Sleep Center,
_____ Debtor.

**ORDER ON MOTION TO DISQUALIFY
DEBTOR'S COUNSEL**

THIS CASE came before the Court for hearing to consider the Motion to Disqualify Debtor's Counsel filed by Thomas J. Wiedel and Thomas M. Schuetter (the Movants).

In the Motion, the Movants request that the Court enter an Order disqualifying the law firm of Trenam, Kemker, Scharf, Barkin, Frye, O'Neill, & Mullis, P.A. (Trenam) as counsel for the Debtor, Finao Corporation, in this chapter 11 case. Generally, the Movants assert that Trenam represents an interest adverse to the estate, and is not a disinterested party, because it previously represented two shareholders in a dispute regarding ownership of the Debtor's stock. Consequently, the Movants contend that Trenam's employment is prohibited by §327(a) of the Bankruptcy Code.

Background

The Debtor, Finao Corporation, has operated a diagnostic sleep center in Tampa, Florida, since 2002.

The initial shareholders of the Debtor were Terry E. Leapaldt and Trudy K. Leapaldt (the Leapaldds). Additionally, Terry Leapaldt was the president of the Debtor, and Trudy Leapaldt was the vice president of the Debtor and the manager of its day-to-day operations.

Trenam represented the Leapaldds in connection with the Debtor's formation, and has provided general business advice to the Leapaldds regarding the Debtor's operations. (Doc. 15, Amended Affidavit of Richard J. McIntyre, p. 4).

Prior to January 24, 2004, the Leapaldds entered into negotiations with the Movants pursuant to which the Movants proposed to infuse certain capital into the Debtor in exchange for fifty percent (50%) of the Debtor's stock. According to the Movants, Trenam prepared a proposed Stockholders Agreement that was intended to document their acquisition of the stock. (Doc. 36, Motion to Disqualify Debtor's Counsel, p. 2). A dispute arose concerning the transaction, however, and no written agreement was ever signed to document the Movants' entitlement to the stock. The parties agree, however, that the Movants had advanced more than \$150,000.00 to the Debtor by the time that the dispute arose. (Transcript, pp. 6, 25).

On January 24, 2004, the Movants filed an action in the Circuit Court of Hillsborough County, Florida, styled Thomas J. Wiedel, Thomas M. Schuetter, and Pacific Island Medical, Inc. v. Finao Corporation, Terry E. Leapaldt and Trudy K. Leapaldt, Case No. 04-606. The Movants assert that the purpose of the action was to "determine the ownership interests and relative rights of the shareholders in the company." (Doc. 36, Motion to Disqualify Debtor's Counsel, pp. 1-2).

In the state court litigation, the Movants contend that they purchased fifty percent (50%) of the Debtor's stock, and also contend that they are the vice president and treasurer of the Debtor. (Doc. 36, Motion to Disqualify Debtor's Counsel, p. 1).

The Debtor disputes the claim that the Movants are stockholders and officers of the Debtor, and asserts that the parties had failed to reach a meeting of the minds regarding fundamental elements of the stock agreement. (Transcript, pp. 19-21). The Debtor acknowledges, however, that the Movants are unsecured creditors of the Debtor by virtue of their loans to the company. (Transcript, pp. 25-26).

Trenam represented the Leapaldds and the Debtor in the state court action. (Doc. 15, Amended Affidavit of Richard J. McIntyre, p. 4).

The Debtor filed a chapter 11 petition on October 21, 2004, five days before a scheduled hearing in the state court action.

Trenam is the Debtor's counsel of record in its chapter 11 case.

On November 12, 2004, the Movants filed the Motion to Disqualify Debtor's Counsel that is currently at issue. The heart of the Motion appears in Paragraph 6, in which the Movants allege as follows:

6. Trenam represents the Leapaldds and the Debtor in the State Court Action. Trenam's resulting conflict of interest in this case is apparent: Trenam must take direction regarding the Debtor's affairs from its officers, directors, and shareholders, but Trenam has in this regard adopted its clients' (the Leapaldds') position that Movants are not existing shareholders or officers of the Debtor. If truly representing the Debtor, Trenam cannot take a stake in the private dispute among the officers and shareholders as to ownership and control of the Debtor.

(Doc. 36, Motion to Disqualify Debtor's Counsel, p. 2).

Trenam asserts that it has terminated its representation of the Leapaldds in the state court action. (Doc. 50, Debtor's Response to Motion to Disqualify Debtor's Counsel, pp. 3, 6).

Discussion

The Movants contend that "Trenam is not 'disinterested' under the Bankruptcy Code." (Doc. 36, Motion to Disqualify Debtor's Counsel, p. 3). Section 327(a) of the Bankruptcy Code provides:

11 USC §327. Employment of professional persons

(a) 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.

11 U.S.C. § 327(a)(Emphasis supplied). The term "disinterested person" is defined in §101(14) of the Bankruptcy Code to mean a person that "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." 11 U.S.C. §101(14).

An attorney's representation of the shareholders of a corporate debtor does not necessarily constitute the representation of an interest adverse to the estate under §327(a). Instead, for an attorney to be disqualified, the party objecting to the representation must demonstrate some additional conflict between the shareholders and the debtor. In re Huntco Inc., 288 B.R. 229, 234 (Bankr. E.D. Mo. 2002).

A determination as to whether an attorney represents an interest adverse to the estate involves a fact-specific analysis. In the case-by-case analysis, the court should determine whether there is an existing conflict of interest, and should also determine whether it is likely that any potential conflict will ripen into an actual conflict. In re Huntco, 288 B.R. at 234.

Further, by its terms, §327 only prohibits an attorney from representing a debtor if he currently represents an interest adverse to the estate. The attorney is not necessarily disqualified solely because he represented an adverse interest in the past. Id. at 236.

Finally, an attorney represents an interest adverse to the estate under §327(a) "only if the issues on which it represented the interest holder is [sic] somehow germane to the issues involved in the bankruptcy." Id.

Application

The Court finds that significant factual questions exist in this case regarding the actual or potential conflict alleged by the Movants, and that an evidentiary hearing should therefore be conducted so that the Court can complete its fact-specific analysis under §327(a).

The Movants contend, for example, that Trenam is not disinterested within the meaning of §327 (1) because the Debtor (Trenam's current client) may hold claims against the Leapaldds (Trenam's former clients) arising from the Leapaldds' personal use of corporate funds; (2) because the attorney at Trenam who handled the negotiations between the Movants and the Leapaldds is a material witness in the resolution of the stockholder dispute; and (3) because Trenam is taking direction from the Leapaldds, who constitute only one faction of the competing shareholder interests. (Transcript, pp. 11-13).

It appears, therefore, that the Movants' argument is premised on their assertion that the Leapaldds own only fifty percent of the Debtor's stock, and that the Movants are entitled to receive the balance of the stock once the stockholders dispute is resolved.

The Debtor disputes the Movants' contention in this regard, however, and contends that the parties never reached a final agreement as to the Movants' acquisition of the Debtor's stock. The Debtor claims, for example, that the parties failed to reach agreement on such essential terms as (1) whether the Movants would be repaid an amount equal to their investment in the Debtor, in addition to receiving fifty percent of the Debtor's stock, as consideration for the transaction, and (2) whether Mrs. Leapaldd would continue to operate the daily affairs of the Debtor if Mr. Leapaldd died. Since there was no agreement on these key terms, the Debtor claims that the deal unraveled and was never binding on any of the parties. (Transcript, pp. 20-21).

Consequently, the Debtor contends that no stock was ever issued to the Movants, and that the Leapaldds remained the sole shareholders and officers of the Debtor. (Transcript, p. 22).

The Court finds that a threshold issue raised by the Motion to Disqualify Debtor's Counsel is whether the Movants are entitled to fifty percent of the

Debtor's stock as a result of their dealings with the Debtor and the Leapaldds. The issue of whether the Movants are entitled to such an interest, or whether the Leapaldds remain the sole shareholders and officers of the Debtor, relates directly to whether Trenam's prior representation of the Leapaldds created an actual or potential conflict between the interest of the individuals and the interest of the Debtor.

Given the factual issues described above, however, the Court finds that these matters cannot be resolved on the basis of the statements and proffers by the parties' attorneys, and that an evidentiary hearing should be conducted on the Motion to Disqualify Debtor's Counsel.

Accordingly:

IT IS ORDERED that a Final Evidentiary Hearing on the Motion to Disqualify Debtor's Counsel filed by Thomas J. Wiedel and Thomas M. Schuetter will be conducted on February 18, 2005, at 9:00 a.m. in Courtroom 8A, Sam M. Gibbons United States Courthouse, 801 N. Florida Avenue, Tampa, Florida, before the Honorable Paul M. Glenn, Chief Bankruptcy Judge.

DATED this 26th day of January, 2005.

BY THE COURT

/s/ Paul M. Glenn
PAUL M. GLENN
Chief Bankruptcy Judge