

07-3058-bk (L)

07-3213-bk-(CON)

IN THE
United States Court Of Appeals
FOR THE SECOND CIRCUIT

In Re: D.A. Elia Construction Corp., Debtor.

D.A. ELIA CONSTRUCTION CORP.,

Debtor-Appellant,

vs.

DAMON & MOREY, LLP,

Defendant-Appellee,

ON APPEAL FROM THE ORDER OF THE UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF NEW YORK
JUDGE RICHARD J. ARCARA, AT DOCKET NUMBERS:
06-MC-71, BK NUMBER: 94-10866-K

BRIEF FOR DEBTOR-APPELLANT
D.A. ELIA CONSTRUCTION CORPORATION

Respectfully submitted,
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THE DISTRICT COURT ABUSED ITS DISCRETION BY ENTERING A JUDGMENT IN AN AMOUNT DIFFERENT THAN THAT ORDERED BY THE BANKRUPTCY COURT AND SUBSEQUENTLY AFFIRMED BY THE DISTRICT COURT AND MANDATE OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

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PRELIMINARY STATEMENT

This is an appeal from the July 2, 2007 Decision and Order of the Honorable Richard J. Arcara granting judgment to the Appellee Damon & Morey, LLP (“Damon & Morey”) in the amount of three hundred forty two thousand, five hundred and eighteen dollars and forty nine cents (\$342,518.49).

JURISDICTIONAL STATEMENT

The United States District Court for the Western District of New York had jurisdiction over this matter pursuant to 28 U.S.C. §158. The Court of Appeals has jurisdiction over this matter pursuant to 28 U.S.C. §1291. The Order being appealed from was entered on July 2, 2007 and a timely Notice of Appeal was filed on July 13, 2007.

STATEMENT OF ISSUES PRESENTED FOR REVIEW

The issue on appeal is whether the District Court abused its discretion by not following the Mandate of the Second Circuit by entering judgment in an amount different from that granted by the Bankruptcy Court Judge and subsequently affirmed.

STATEMENT OF THE CASE

The Judgment in issue arises from Damon & Morey’s representation of the Debtor as a result of and pursuant to the Motion of Damon & Morey (D 17) to be

employed as attorneys for the Debtor (D 32) in connection with Debtor's March 30, 1994 filing for Protection in the United States Bankruptcy Court for the Western District of New York. On June 15, 1994, the Court was persuaded by "...proposed safeguards [against representation that might result in conflicts of interest] placed on the record by Damon & Morey" and approved Damon & Morey's employment "over the good and valid objections of the United States Trustee" (D-36).

All sums claimed by the Appellee are memorialized in their six Fee Applications dated September 1, 1994, August 25, 1995, September 8, 1998, August 11, 1999, August 17, 2000 and June 29, 2004.

Damon & Morey's First Fee Application was filed on September 1, 1994 (D 76) and requested a total of forty six thousand, three hundred fifty eight dollars and two cents (\$46,358.02) for fees and disbursements. The U.S. Trustee's Office objected to same on the grounds that Damon & Morey sought payment for time and expenses from prior to its appointment as General Counsel for the Debtor in Possession and for lack of specificity in its itemizations. The objections were addressed in a hearing on September 21, 1994 (D 85). On September 29, 1994, the Court issued an Order approving thirty one thousand, eight hundred twenty nine dollars and ninety seven cents (\$31,829.97) in fees and disbursements, subject to a holdback in the amount of nine thousand seven hundred and ninety seven dollars

(\$9,797.00), thereby impliedly disapproving of the four thousand, seven hundred thirty one dollars and five cents (\$4,731.05) remainder (D-88).

Damon & Morey filed its Second Fee Application on August 25, 1995 (D 166), requesting thirty five thousand, seven hundred forty seven dollars and thirteen cents (\$35,747.13) in fees and disbursements. The U.S. Trustee objected (D-176), for various reasons, including suspect billing practices, an apparent lack of billing judgment, an apparent lack of benefit to the estate for time billed and for duplicative billing. The Bankruptcy Court's September 27, 1995 Order on the Second Fee Application approved a draw down of twenty three thousand, one hundred seventy dollars and three cents (\$23,170.03) without prejudice to the reassertion of these objections at the time of the Final Fee Application (D-182).

Damon & Morey filed its Third Fee Application on September 8, 1998 (D 395). The fee application requested two hundred seventy three thousand, seven hundred forty seven dollars and thirty three cents (\$273,747.33) in fees and disbursements, including distribution of the holdbacks from prior applications. By Order dated September 28, 1998, the Bankruptcy Court denied discovery in connection with the fee application and allowed one hundred fifty four thousand, seven hundred thirty eight dollars and twenty three cents (\$154,738.23) of which four thousand, seven hundred thirty eight dollars and twenty three cents

(\$4,738.23) represented disbursements. At that time, the Court confirmed that the fees would be subject to disgorgement, reexamination and adjustment (D-424).

Damon & Morey filed its Fourth Fee Application (D 598) on August 11, 1999 requesting two hundred seventy two thousand, ninety one dollars (\$272,091.00). The Bankruptcy Court's September 22, 1999 Order (D-607) adjourned Damon & Morey's Fourth Fee Application with no decision being made at all as to the merits of said application and went on to order, *inter alia*, that Debtor can (and/or shall) remit to Damon & Morey's no more than two hundred thousand dollars (\$200,000) subject to disgorgement.

Damon & Morey's Fifth Fee Application, dated August 17, 2000 (D 677) sought allowance of fees for work done since the previous application and for all "holdbacks" from each of the previous applications, for a total of one hundred fifty three thousand, nine hundred ninety four dollars and forty two cents (\$153,994.42). The Bankruptcy Court allowed a payment of thirty thousand dollars (\$30,000.00) and deferred, without prejudice, ruling on the balance of the Fee Application.

Since Damon & Morey, Debtor's actual Attorney of Record to this day, refused to file the Final Report, on February 12, 2004 Debtor filed the same sua sponte. The Bankruptcy Court considered this report a "nullity" since it was not signed by the Attorney of Record. Thereafter, on June 29, 2004 Damon & Morey filed its Sixth and Final Fee Application ("Final Fee Application") (D-713)

seeking payment for all hold backs and additional fees and disbursements in the amount of eighty seven thousand, six hundred seventy one dollars and twenty cents (\$87,671.20).

On September 1, 2004, the Debtor filed Objections to the Final Fee Application (D-728). On September 7, 2004, Damon & Morey filed its Response to the Objections (D-729). By Affidavit dated October 18, 2004, David Elia, C.E.O. of the Debtor, filed a Reply (D-734) to Damon & Morey's Response.

On October 19, 2004, the Bankruptcy Court denied the Debtor's Objections and its request for further discovery and an evidentiary hearing. Instead, the Court approved in full every penny of every fee application of Damon and Morey, including all holdbacks and unapproved fees (D-735). On October 26, 2004, the Debtor filed a Notice of Appeal from the October 19, 2004 Order (D-738). On June 19, 2006, the District Court by Decision and Order (D-770) fully affirmed the decision of the Bankruptcy Court. Thereafter, on Appeal to the Second Circuit, the District Court Decision was affirmed by Summary Order.

RELEVANT FACTS

The amount of the July 2, 2007 Decision and Order (A-5) is inexplicably in a different amount from that requested by Damon & Morey (A-48), approved by the Bankruptcy Court Judge (A-22) and subsequently mandated by this Court. It is

apparent that the lower Courts improperly adjusted the Damon & Morey fee award on account of errors that were never adjudicated.

It is undisputed that Damon & Morey labored under a series of conflicts of interest during its representation of the Debtor. As a result, Damon & Morey did not meet the requirement that counsel for the debtor remain “disinterested” as it also represented the Lead Creditor of the Creditors’ Committee against the Debtor. The breadth of the conflict remains unknown as Damon & Morey failed to disclose the conflict to the Bankruptcy Court or the Debtor until forced to do so because of the malpractice action of Construction Pacesetters against it. Even after discovery, the Appellee has continued to conceal the nature and extent of its digressions to the Court.¹

SUMMARY OF ARGUMENT

The District Court improperly entered judgment in favor of Appellant(A-10) by failing to make any findings of fact as to how it arrived at an amount different than that approved by the Bankruptcy Court(A-22) and affirmed on appeal. The failure of the District Court to make findings of fact relative to its entry of

¹ Filed contemporaneously with Debtor’s Brief is a Motion to Supplement the Record to include the Debtor’s Motion recently filed in the United States Bankruptcy Court seeking to vacate this judgment and set it aside in light of recently discovered documents that confirm further undisclosed indiscretions of Damon & Morey with regard to its conflicts of interest, including engaging in a contingency fee agreement in the Construction Pacesetters action against Debtor and accepting fees in violation of the Bankruptcy Code.

Judgment in an amount different than that Ordered by the Bankruptcy Court and Mandated by this Court is an abuse of discretion and requires this Court to vacate the District Court's Decision and Order(A-5) and Judgments (A-9, A-10) and remand for further proceedings.

ARGUMENT

The District Court abused its discretion by entering a judgment in contravention of the amount approved by the Bankruptcy Court and mandated by the United States Court of Appeals in and for the Second Circuit. The Appellee by and through its Sixth and Final Fee Application requested the amount of three hundred fifty eight thousand, seven hundred fifty six dollars and sixty two cents (\$358,756.62) as and for the final balance due and owing for its representation of the Debtor (A-25).

Prior to this Sixth and Final Fee Application, the Debtor had already paid to the Appellee approximately four hundred thousand dollars (\$400,000), subject to disgorgement, and Judge Kaplan Ordered "holdbacks" of approximately three hundred eighty five thousand dollars (\$385,000)(D-88, D-182, D-424, D-607, D-677). Thereafter, a series of appeals were taken resulting in the Second Circuit affirming the request of three hundred fifty eight thousand, seven hundred fifty six dollars and sixty two cents (\$358,756.62) as and for the final balance due Damon

& Morey based upon full allowance of their Sixth and Final Fee Application and all previous hold backs.

Thereafter, without explanation, the District Court entered Judgment (A-9) and Amended Judgment (A-10) upon the motion of Damon & Morey (A-11) in the amount of three hundred forty two thousand, five hundred eighteen dollars and forty nine cents (\$342,518.49), an amount sixteen thousand, two hundred thirty eight dollars and thirteen cents (\$16,238.13) less than that requested by Damon & Morey in their Fee Application (A-25) and Mandated by this Court. This discrepancy is a result of the Appellee's admission that it was not entitled to a portion of those fees that were approved due to billing errors and its conflicted representation. (A-11)

Thereafter, the Debtor discovered that not only did the Appellee charge for fees that it was not entitled to as a result of conflicted representation, but also that it had entered into a Contingent Fee Agreement with the Lead Creditor, Construction Pacesetters, against the Debtor during the course of its representation of the Debtor. Upon information and belief, Damon & Morey was paid one third of improperly obtained funds, seventy five thousand dollars (\$75,000), that but for the malfeasance of Damon & Morey (while acting in its conflicted capacity advancing the interests of the Lead Creditor against the Debtor), would have gone into the Debtor's estate. Also, contrary to the representations made to the Court

and Debtor that only one (1) “rogue” partner and an associate were involved in the conflicted representation, at least four (4) Damon & Morey attorneys plus two (2) other law firms were hired and paid by Damon & Morey to represent the Lead Creditor against the Debtor. Finally, to conceal this wrongful conduct, Damon & Morey set up files in the names of the principals of the Lead Creditor while actually working for the Lead Creditor against the Debtor. (See Appellants Motion to Supplement the Record Dated September 28, 2007).

The Debtor has maintained throughout these proceedings that the improper conduct of the Appellee has caused it pecuniary losses and, in addition, has prevented the Debtor from resuming its business.

The admission of Damon & Morey that it was not entitled to the full amount of the fees it requested, coupled with the additional discovery that proves the active concealment by the Appellee of its fraudulent conduct, require that this Court vacate the Judgment of the District Court and Order and order an inquest into the misconduct of Damon & Morey. The Court has the authority to modify or vacate any judgment as may be just under the circumstances pursuant to 28 U.S.C. § 2106.

The record establishes, by the Appellee’s own admission, that it has impermissibly charged fees that the Bankruptcy Code does not allow and that are violative of the Code of Professional Responsibility and the Bankruptcy Court

Rules that apply to attorneys. More importantly, vital public policy issues at stake are paramount because the Bankruptcy Court, as the gate keeper of fee applications by professionals, should always require reasonableness, even in rare “surplus” cases. If allowed, debtors’ counsel in surplus cases can comfortably plunder the estates because of the courts’ and trustees’ apparent lack of interest and attention when the debtors live up to their promises and pay all creditors. The precedent set by this case will be that “success” fees are appropriate and misconduct will be overlooked so long as there are no creditors left to protect.

A review of the record in this case confirms that Judge Kaplan was sufficiently concerned with the handling of the prior fee application’s that he Ordered holdbacks of money on each of Damon & Morey’s requests, subject to future review and disgorgement. Moreover, Justice Kaplan was aware that the parties recognized that there were “issues” with regard to the performance of Debtor’s Counsel since it sanctioned mediation in an effort to come to an agreement as to what, if anything, was owed Damon & Morey.

Indeed, the Appellee’s failure to file fee applications for years at a time warranted enhanced scrutiny of the Bankruptcy Court, yet, no comment or attention was afforded despite prejudice to Debtor in clear violation of the Bankruptcy Rules and the Order Approving Employment of Damon & Morey. How can almost three and four years pass without a fee application? How can

admitted conflicts resulting in pecuniary loss to the Debtor be allowed without redress? How can Debtor's Counsel get paid under such circumstances with impunity? The entry of an amended and modified judgment in contravention of the mandate to the District Court is not permissible and is an abuse of discretion. *See, e.g., Briggs v. Pennsylvania R. Co., 334 U.S. 304; Scientific Anglers, Inc. v. B.F. Gladding & Co., 260 F.2d 662 (6th Cir. 1958).*

The Court has inherent power to correct violations of the law and equitable powers to prevent injustice; this particular case cries out for this Court to intervene to assure that there is a review of the fee applications of Appellee in light of its misconduct to assure the integrity of the Bankruptcy Court.

This Court must exercise its' inherent power and recall the mandate to avoid injustice. Absent such action by this Court, there is no way to determine the correct award to which the Appellee is entitled, if any, and the scope and effect of its admitted violations of the Bankruptcy Code and abrogation of duties owed its Debtor client. The Court cannot allow Debtor's counsel to escape accountability for its misconduct merely because there is money left over in this bankruptcy reorganization.

Had there been creditors remaining in this matter, the Court would have continued to scrutinize Damon & Morey's bills and, without a doubt, reduced the fee application of the Debtor's counsel and addressed this misconduct and resultant

pecuniary losses, as it would be required to determine if Damon & Morey should be surcharged for the actual losses caused to the estate by its misconduct. This is without regard to its fee claims, where as here, the malpractice of Debtor's Counsel and its conflicted Representation cost the Debtor Estate unrecovered monies due to it.

This is further underscored by the fact that the District Court entered judgment in an amount different than that mandated by the Second Circuit and the Bankruptcy Court. This confirmation of the error of the Bankruptcy Court Judge in awarding fees that the Appellee has admitted they are not entitled to requires that the Court make findings as to how those amounts were arrived at and, after appropriate inquiry, determine what further and other information must be developed in order to confirm the reasonable fee due to Appellee.

CONCLUSION

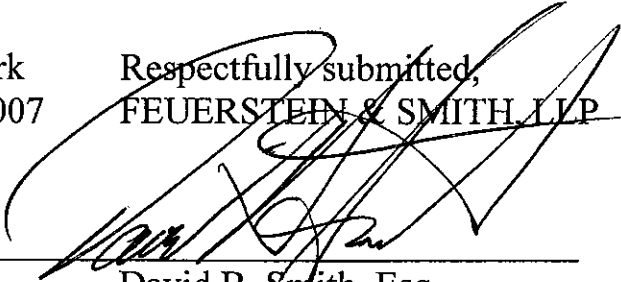
The entry of Judgment against the Debtor Appellant must be vacated and the matter remanded to the Bankruptcy Court for further proceedings to address the misconduct of Damon & Morey, and, to conduct an inquest into the reasonableness of its claimed fees so that a proper Judgment may be entered.

DATED:

Buffalo, New York
September 20, 2007

Respectfully submitted,
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