

UNITED STATES BANKRUPTCY COURT  
WESTERN DISTRICT OF TENNESSEE

IN RE  
XL SPORTS, Ltd.,  
Debtor.

Case No. 97-37119-WHB  
Chapter 11

XL SPORTS, Ltd.,  
Plaintiff,

v.

Adv. Proc. No. 97-1431

JERRY LAWLER,  
Defendant.

**See attached appeal at end of opinion**

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ORDER ON DEFENDANT'S MOTION TO DISMISS COMPLAINT

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In this adversary proceeding, the defendant filed his motion to dismiss or, in the alternative, to strike certain paragraphs of the complaint as immaterial. The defendant filed a supporting memorandum, and the plaintiff filed responses, to which the defendant further responded. The motion was argued on February 2, 1998. The Court will conditionally deny the motion to dismiss, subject to the plaintiff's amendment to the complaint by March 2, 1998.

There were arguments raised, both in the written memoranda and in oral argument, that are not supported by evidence. Basically, at this early stage of the proceeding, there is no evidence before the Court. While the Court appreciates the defendant's references to contracts and to allegations of the author of those contracts, the Court has resisted the temptation to rely upon documents that are not yet formally before the Court. The Court is aware that a motion to dismiss which brings in matters outside the pleadings shall be considered as a motion for summary judgment, FED. R. CIV. P. 12(b); however, this proceeding is at too preliminary a stage to consider granting

summary judgment.

The heart of the motion to dismiss is that the complaint falls to state the bare allegations of fraud with sufficient particularity to enable the defendant to file a responsive pleading. The Court agrees. Based upon statements of all counsel at the hearing on this motion, the plaintiff has had ample opportunity to discover enough about this complaint to form a more particular complaint. The Court understands that there is judicial authority for the concept that FED. R. CIV. P. 9(b) is somewhat relaxed in bankruptcy proceedings where, for example, the plaintiff is a bankruptcy trustee who lacked first hand knowledge of the underlying facts. Ahern and MacLean, *BANKRUPTCY RULES MANUAL* § 7009.03 (citing, e.g., *In re Hollis & Co.*, 83 B.R. 588 (Bankr. E.D. Ark. 1988)). “A persuasive reason to permit this relaxation is the trustee’s inevitable lack of knowledge concerning acts of fraud previously committed against the debtor, a third party.” *COLLIER ON BANKRUPTCY* 15<sup>th</sup> Ed. Rev’d., ¶ 7009.03, at 7009-4. A debtor in possession is the statutory equivalent of a trustee, holding the trustee’s avoidance powers. 11 U.S.C. § 1107(a). It does not follow, however, that a debtor in possession has the same relaxed standard for pleading fraud.

This debtor in possession is not a distant third party. Rather, this debtor in possession has been involved in the contracts and transactions that are the subject of this complaint, and the debtor in possession has had an opportunity through similar litigation in Ohio to discover some of the facts from the defendant. Moreover, counsel for the defendant has stated that the plaintiff filed a similar complaint in Ohio, to which a similar motion to dismiss was pending when the plaintiff voluntarily dismissed that complaint. This complaint is filled with general allegations and comments that do not refer to specific facts of who, what, when, where, why, and how. It is obvious that more particular facts exist, as the plaintiff’s counsel stated in court that he was preparing a more specific

complaint against this defendant on legal grounds other than fraudulent transfer avoidance. This debtor in possession is not a distant third party; rather, this debtor in possession is in a position to plead the alleged fraud with sufficient particularity to enable the defendant to respond to the allegations.

That does not mean that the plaintiff must exhaustively plead “unnecessary details of evidentiary matter.” A more particular complaint does not necessarily mean a lengthy complaint. “Facts with respect to false misrepresentations, including time and place and content of the misrepresentations, should be pleaded, as should facts with respect to the consequences of the fraud.” COLLIER ON BANKRUPTCY ¶ 7009.03 at 7009.03.

The complaint as written also leaves doubt as to the relief sought. In court, plaintiff’s counsel stated that this was a § 548 complaint relying both upon actual and constructive fraud. If those are the causes of action, they should be more directly stated in the complaint.

The motion also seeks dismissal for failure of the complaint to join an indispensable party or parties. It is clear from the oral argument that the plaintiff takes the position that it can invoke avoidance of a transfer or sale between Jerry Lawler and one Jerry Jarrett, and that such a transfer was void ab initio. Without regard to whether the plaintiff is correct in that position, it is apparent that the failure to include Jerry Jarrett, and perhaps others involved as either principals or victims in what the plaintiff alleges to have been a fraudulent scheme, leaves this Court with an inability to reach a just and complete adjudication of this dispute. If, for example, the plaintiff is unable to persuade the Court that it can “void” the transaction between Mr. Lawler and Mr. Jarrett, the result of this litigation would simply be further litigation. Moreover, a judgment in this proceeding would be prejudicial to Mr. Jarrett if, in fact, the transaction between him and Mr. Lawler was void ab

initio. He might have, for example, tax consequences that would flow from such a judgment. The futility of proceeding without necessary parties is illustrated by the holding that a failure to join an indispensable party may be raised at any stage of the proceeding, including after the entry of a judgment. *Provident Tradesmens Bank & Trust Co. v. Patterson*, 390 U.S. 102, 88 S.Ct. 733, 19 L.Ed. 2d 936 (1968). The Court agrees with the defendant Lawler that this complaint has failed to name one or more parties who are known to the plaintiff to have been involved in the transactions underlying this complaint; at least, that is correct if the plaintiff chooses to continue to rely upon actual fraud in this complaint and upon the position that the transactions between Mr. Lawler and Mr. Jarrett were void ab initio. If, on the other hand, the plaintiff elects to proceed only on a constructive fraud theory that it did not receive reasonably equivalent value for what it transferred to Mr. Lawler, other parties may or may not be necessary.

The motion to dismiss raises other alleged defects in the complaint. The Court will not attempt to address the remaining alleged defects; rather, the Court will await the plaintiff's amended, and hopefully clearer, complaint.

The granting of a motion to dismiss for failure to plead fraud with particularity is typically coupled with an opportunity for the plaintiff to amend the complaint. *Luce v. Edelstein*, 802 F.2d 49, 56 (2d Cir. 1986). This is not surprising in view of applicable Rule 9(b)'s absence of a sanction for failure to so plead. Ahern and MacLean, *BANKRUPTCY RULES MANUAL* § 7009.04. This Court concludes that an appropriate remedy for the motion to dismiss is to give the plaintiff a reasonable opportunity to amend the complaint, with a failure to so amend to result in dismissal of this complaint.

IT IS THEREFORE ORDERED that the motion to dismiss is conditionally denied; however,

the plaintiff is to file an amended complaint and serve it upon the defendant and his counsel by March 2, 1998. The plaintiff may, of course, be required to serve any other parties named in the amended complaint. The amended complaint shall more particularly plead the allegations of fraud; the complaint shall make it clear whether the plaintiff is relying upon actual fraud or constructive fraud or both under § 548; and the complaint shall name all indispensable parties, including Mr. Jarrett. After filing and service of the amended complaint, the defendant and any other parties named shall have the opportunity permitted by the Rules of Civil and Bankruptcy Procedure to respond. The Court will conduct a status and scheduling conference in this proceeding after the amended complaint is at issue.

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UNITED STATES BANKRUPTCY JUDGE

Dated: February 3, 1998

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IN THE UNITED STATES DISTRICT COURT  
FOR THE WESTERN DISTRICT OF TENNESSEE  
WESTERN DIVISION

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IN RE: XL SPORTS, LTD., LLC, )  
Debtor. )  
)  
JERRY LAWLER, )  
)  
Appellant, )  
)  
V. ) NO. 98-2720-TUV  
)  
)  
XL SPORTS, LTD., LLC, )  
)  
Appellee. )

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ORDER ON BANKRUPTCY APPEAL

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This is an appeal from a bankruptcy court order approving debtor's application to employ attorney Larry E. Parrish nunc pro tunc.<sup>1</sup>

I. STANDARD OF REVIEW

A district court reviews the bankruptcy court's conclusions of law de novo. Wesbanco Bank Barnesville v. Rafoth (In re Baker & Getty Fin. Servs., Inc.), 106 F.3d 1255, 1259 (6th Cir.) (citing Bankruptcy Rule 8013), cert. denied, 118 S. Ct. 65 (1997). When reviewing a "bankruptcy court's retention and compensation orders, [a district court's review] is limited to abuse of discretion" and

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<sup>1</sup> Nunc pro tunc, a Latin term meaning "now for then," describes an act allowed to be done after the time when it should be done with a retroactive effect back to the original date in which the act should have been done. Black's Law Dictionary 964 (5th ed. 1979).

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the district court will "follow the bankruptcy court's findings of fact unless clearly erroneous." Michel v. Federated Dep't Stores, Inc. (In re Federated Dep't Stores, Inc.) 44 F.3d 1310, 1315 (6th Cir. 1995) (citations omitted).

## II. BACKGROUND

XL Sports, an Ohio limited liability company, has its principal place of business in Memphis, Tennessee. In late 1997, Parrish was hired by XL Sports to represent it in a RICO/fraud action it filed in Ohio and in connection with a possible bankruptcy filing.<sup>2</sup> The RICO/FRAUD suit was later voluntarily dismissed by XL Sports.<sup>3</sup> Parrish was paid \$40,000 by an equity holder by November 20, 1997 for his legal work in the RICO/fraud action.<sup>4</sup> The next day, November 21, 1997, XL Sports filed a Chapter 11 bankruptcy petition in United States Bankruptcy Court in the Western District of Tennessee. No application for employment of legal counsel to assist XL Sports in its bankruptcy proceeding was filed at that time. However, Parrish was still acting as XL Sports' counsel.

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<sup>2</sup> The record is unclear on the exact date Parrish was retained by XL Sports to represent it in the RICO/fraud action. However, it is apparent from the record that Parrish had actively represented XL Sports in this matter weeks before the bankruptcy petition was filed.

<sup>3</sup> The RICO/fraud suit was later refiled in the United States District Court in Memphis after bankruptcy proceedings had been initiated.

<sup>4</sup> The bankruptcy court determined that the \$40,000 payment to Parrish for his legal fees was an indirect payment made by Phyllis Selker, an equity holder in XL Sports, on behalf of XL Sports. Selker has withdrawn any claims that she may have against XL Sports in this matter.

On January 26, 1998, sixty-six days after the bankruptcy petition was filed, XL Sports' representative Mark Selker filed an application seeking nunc pro tunc approval of XL Sports' employment of Parrish as its attorney of record. The application sought approval of all legal fees incurred by Parrish from the November 21 initial bankruptcy filing to the date the application was filed.<sup>5</sup>

The application was opposed by the United States Trustee, as well as Larry Burton and Jerry Lawler, both potential creditors of XL Sports. Burton, Lawler and the United States Trustee opposed the application on the grounds that the application was not timely made and that Parrish was not the "disinterested" counsel required under 11 U.S.C. § 327 and Federal Rule of Bankruptcy Procedure 2014.<sup>6</sup> The bankruptcy court held that Parrish qualified as a "disinterested" counsel and approved the application. The approval was conditioned upon a \$10,000 reduction in Parrish's fees due to the untimely application.

### III. STANDING

It is first necessary to address the issue of Lawler's standing to appeal the bankruptcy court's order. XL Sports claims that Lawler is a "non-creditor, a non-equityholder and hostile adversary" to XL Sports and thus has no standing to appeal the bankruptcy court's order.

"To appeal from an order of [the] bankruptcy court, appellants

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<sup>5</sup> Parrish's legal fees and expenses during this period amounted to \$34,450.17.

<sup>6</sup> Burton and the U.S. Trustee have not appealed the bankruptcy court's decision.

must have been directly and adversely affected pecuniarily by the order." Fidelity Bank v. M.M. Group, Inc., 77 F.3d 880, 882 (6th Cir. 1996) (citations omitted). "This principal, also known as the 'person aggrieved' doctrine, limits standing to persons with a financial stake in the bankruptcy court's order." Id. (quoting In re Revco D.S., Inc., 898 F.2d 498, 499 (6th Cir. 1990). "Only when the order directly diminishes a person's property, increases his burdens, or impairs his rights will he have standing to appeal." Id. (citations omitted).

Lawler was listed on Schedule G of the Bankruptcy Petition as a party to an executory contract with XL Sports. This contract has been rejected by XL Sports under order of the bankruptcy court. However, the Bankruptcy Code states that:

A claim arising from the rejection . . . under a plan under chapter 9, 11, 12 or 13 of this title, of an executory contract or unexpired lease of the debtor that has not been assumed shall be determined, and shall be allowed . . . the same as if such claim had arisen before the date of the filing of the petition.

11 U.S.C. § 502(g). The rejection of Lawler's contract provides him with a pre-petition claim on XL Sports. This claim meets the "person aggrieved" doctrine, providing Lawler standing to appeal the bankruptcy court's order.

#### IV. ANALYSIS

The bankruptcy court's order approved XL Sports' application to employ Parrish nunc pro tunc but reduced the amount of the fees due by \$10,000. The bankruptcy court found that Parrish was not a pre-petition creditor of XL Sports for legal fees incurred during the RICO/fraud action because of \$40,000 in pre-petition payments

to Parrish that satisfied all pre-bankruptcy legal fees incurred by XL Sports.

The court also rejected arguments by the parties opposing the application that Parrish was not the "disinterested" party required to act as counsel in a bankruptcy case. Applying the three part test found in In re Marvel Entertainment Group, Inc., 140 F.3d 463 (3d Cir. 1998), the bankruptcy court found Parrish had a mere appearance of a conflict of interest which did "not warrant the disallowance of [XL Sports'] application."

Finally, applying a series of criteria previously set forth in In re Martin, 102 B.R. 653, 656 (Bankr. W.D. Tenn. 1989), the bankruptcy court approved the nunc pro tunc application.<sup>7</sup> The

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<sup>7</sup> The criteria consists of the following items: (1) The application must be one which would have been approved originally by the court, measured by the requirements of 11 U.S.C. § 327 and Bankruptcy Rule 2014 at or before the time the services were actually commenced; (2) Evidence must appear in the record of the case which demonstrates that the court and other interested parties had actual knowledge of the legal services being rendered by the applicant; (3) An application seeking an order nunc pro tunc must be filed as soon as the matter is brought to the attention of the applicant; (4) The party for whom the work was performed approves the entry of the nunc pro tunc order; (5) The applicant has provided notice of the application for the nunc pro tunc order to creditors and parties in interest and has provided an opportunity for filing objections; (6) No creditor or party in interest offers reasonable objection to the entry of the nunc pro tunc order; (7) If the applicant is also seeking compensation at this point, the applicant must have provided notice of the application for fees to any parties in interest, thus providing an opportunity for objections as provided in 11 U.S.C. § 330; (8) A sustainable objection must not be filed to the applicant's request for attorney fees; (9) No actual or potential prejudice will inure to the estate or other parties in interest; (10) The applicant's failure to seek pre-employment approval is satisfactorily explained; (11) The applicant exhibits no pattern of inattention or negligence in seeking judicial approval for employment of professionals, measured in some degree by the applicant's experience in this field of law.

court, however, citing a failure to timely file the application, reduced the fees due Parrish by \$10,000. Lawler appealed this order, claiming that Parrish was a pre-petition creditor, not "disinterested" and thus unable to serve as counsel and that the bankruptcy court erred in approving the application to employ Parrish nunc pro tunc.

A. Was Parrish a pre-petition creditor of XL Sports and thus unable to serve as its counsel?

The Bankruptcy Code defines a creditor as an "entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor." 11 U.S.C. § 101(10). In order to have a claim an entity must have a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured or unsecured." 11 U.S.C. § 101(5).

The determination of whether Parrish has a pre-petition claim on XL Sports and is thus a pre-petition creditor involves the determination of a series of facts. The bankruptcy court found that the fees due Parrish for his pre-bankruptcy legal work on the RICO/fraud action were fully satisfied by Selker's payment on November 20, 1997. Since this finding of fact is not clearly erroneous, this court must follow it. In re Federated, 44 F.3d at 1315.

As Parrish's pre-petition claims were satisfied by Selker's payment, Parrish no longer has any claim or "right to payment" against XL Sports for these fees. Without a "claim against the

debtor that arose at the time of or before the order for relief," it is impossible for Parrish to be a pre-petition creditor. Thus, the bankruptcy court was correct in its determination that Parrish should not be disqualified from acting as counsel for XL Sports due to the fact that he was a creditor.<sup>8</sup>

B. Does Parrish hold an interest adverse to the estate?

The Bankruptcy Code defines a "disinterested person" as 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 . . . or for any other reason." 11 U.S.C. §101(14)(E).

Appellant suggests that Parrish holds an adverse interest to the estate and creditors because he is a pre-petition creditor and received payment from debtor for pre-petition legal services on the eve of the bankruptcy petition which payments were either preferential or fraudulent conveyances. However, as discussed above, the bankruptcy court found that Parrish is not a pre-petition creditor. In addition, the bankruptcy court found that Selker paid Parrish's fees in benefit of XL Sports, not as a representative of XL Sports. The bankruptcy court found that "[b]ased upon the Court's analysis of the facts and circumstances

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<sup>8</sup> Although the question of whether the \$40,000 constituted full payment was unnecessarily made complex by statements of Parrish in the bankruptcy court and in debtor's filing in the bankruptcy court, Parrish has unmistakably waived any claim he might have had with respect to pre-petition services. See Brief of Appellee, XL Sports, Ltd. at 3-4, filed in this court on September 18, 1998, and signed by Parrish.

surrounding the payment of Mr. Parrish's fees, the Court determines that the circumstances presented in this case, create . . . merely the appearance of a conflict or adverse interest." As these findings of fact are not clearly erroneous, this court is bound to follow them. Using the facts as determined by the bankruptcy court, it is clear that there was is no legal basis for a determination that Parrish had an adverse interest to the estate and the bankruptcy court's holding in this matter was correct.

Appellant suggests that the bankruptcy court erred in applying the three-part test for determining a "disinterested person" found in In re Marvel Entertainment Group, Inc., 140 F.3d 463 (3d Cir. 1998). Appellant suggests that the Sixth Circuit ruling in In re Federated, prohibited the employment of professionals with even an appearance of a conflict of interest. This court disagrees with that assessment of the Sixth Circuit ruling. In re Federated involved professionals who admitted that they were "not a disinterested person within the language of § 327(a)." In re Federated, 44 F.3d at 1319. These professionals sought approval by the bankruptcy court "absent a showing by the Trustee of an actual conflict of interest." Id. The Sixth Circuit ruled that since the professionals were not disinterested persons, the statute prevented a bankruptcy court from using its discretion to approve their employment. Id.

In this case, the question to be decided is whether Parrish is a disinterested person. It is clear from the Sixth Circuit ruling in In re Federated that a finding that Parrish was not a

"disinterested person" would require his rejection as counsel for XL Sports. However, the bankruptcy court has determined that Parrish is a disinterested person and this court agrees with its findings. Thus, In re Federated does not control in this matter.

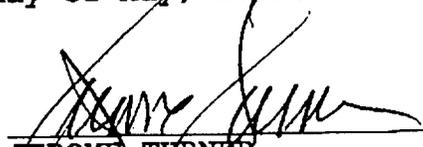
C. Did the bankruptcy court err in approving XL Sports' application to employ Parrish nunc pro tunc?

A district "court's review of the bankruptcy court's retention and compensation orders is limited to abuse of discretion." In re Federated, 44 F.3d 1310 at 1315 (citing Calhoun v. Stratton, 61 F.2d 302, 303 (6th Cir. 1932)). In addition, a "bankruptcy court does have equitable power to authorize retroactive employment of counsel through the use of nunc pro tunc orders." Ibbetson v. United States Trustee, 100 B.R. 548, 550 (D. Kan. 1989) (citations omitted). A careful review of the order and memorandum of the nunc pro tunc appointment of Parrish as XL Sports' counsel shows no abuse of discretion by the bankruptcy court in this authorization. As no abuse of discretion has been found, this court finds that the bankruptcy court did not err in its appointment of Parrish nunc pro tunc.

#### VI. CONCLUSION

For the foregoing reasons, the order of the bankruptcy court approving debtor's application to employ attorney Parrish nunc pro tunc is hereby affirmed.

IT IS SO ORDERED this 14<sup>th</sup> day of May, 1989.

  
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JEROME TURNER  
UNITED STATES DISTRICT JUDGE