IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	Chapter 11
	:	
OSH 1 Liquidating Corporation (f/k/a In re: Orchard Supply Hardware Stores Corporation), et al.,	:	Case No. 13-11565 (CSS) (Jointly Administered)
	:	
Debtors.	:	
	:	
Alamo Group, LLC, a California limited liability company, and Kirin Alamo, LLC, a California limited liability Company,	:	
	:	
Plaintiffs,	:	
	:	
v.	:	Adv. Proc. No. 14-50103 (CSS)
	:	
A&G Realty Partners, LLC, a New York limited liability company, Michael Jerbich, an individual; and DOES 1-25,	:	
	:	
Defendants.	:	

MEMORANDUM ORDER

Upon consideration and review of plaintiffs' (the "Plaintiffs") *Motion to Disqualify Ballard Spahr LLP as Defendants' Counsel* (Adv. D.I. 16) (the "Motion"), the memorandum of law in support of the Motion (Adv. D.I. 17 and 18), the Declaration of Eric Hardeman, Esq. in support of the Motion (Adv. D.I. 19), the Declaration of Don Gaube, as managing member of Alamo Group, LLC ("Alamo Group"), in support of the Motion (Adv. D.I. 20), the above-captioned defendants' (the "Defendants") opposition to the Motion (Adv. D.I.

26), and the Plaintiff's reply brief (Adv. D.I. 27); and the Court having heard oral argument on the Motion on December 2, 2014 (the "Hearing"); and the Court having taken the Motion under advisement at the Hearing;

The Court hereby DENIES the Motion for the reasons set forth herein:

A. Factual Background

1. Alamo Group's business involves the acquisition of commercial real estate and other related assets, including commercial leases. In October 2013, Alamo Group purchased a portfolio of leases from the above-captioned debtors ("Debtors").

2. Thereafter, Plaintiffs filed a fraudulent misrepresentation claim ("Fraud Action") against the Defendants claiming that the Defendants fraudulently induced the Plaintiffs to increase their bid to procure the Debtors' lease designation rights. More specifically, Plaintiffs allege that they placed a bid to purchase a lease portfolio from the Debtors' estates. Plaintiffs and Defendants, the Debtors' real estate professionals, engaged in negotiations after Plaintiffs placed their initial bid. Plaintiffs continue that they entered into a Designation of Rights Agreement (the "Agreement") to purchase the lease portfolio for $315,000. After the entry of the Agreement, but prior to the sale hearing, Plaintiffs allege that Defendants informed them that they had received a competing bid of $1.1 million for one of the leases within the portfolio. After reviewing the competing offer, which included a Letter of Intent, Plaintiffs raised their offer to $1.2 million to acquire the entire lease portfolio. The Court subsequently approved the sale

to Plaintiffs for $1.2 million. Thereafter, Plaintiffs claim that the competing bid was a sham transaction, orchestrated by Defendants to induce Plaintiffs to raise their offer.[1]

3. Ballard Spahr, LLP ("Ballard Spahr") represents the Defendants in the Fraud Action. However, Ballard Spahr has also represented the Plaintiffs in several matters which precede the filing of the Motion. More specifically:

a. In early 2011, Alamo Group began a series of negotiations with United Farm Workers Alberta Co-Operative Limited ("UFA") to purchase commercial real estate assets owned by UFA within the United States, including acquisition of "Wholesale Sports USA, Inc." stores ("Wholesale Sports"). This sale was eventually completed in early 2013. During this sale process, Ballard Spahr represented UFA; whereas, Alamo Group, the purchaser, was represented by separate counsel.

b. After the UFA deal closed, Alamo Group was involved in three separate actions with various landlords in Washington (each a "Washington Action" and collectively, the "Washington Actions"). In the first, Ballard Spahr assisted Plaintiffs in finding local counsel and facilitated discussions between local counsel and the Plaintiffs herein. Ballard Spahr had no substantive role in the first Washington Action. In the second Washington Action, Ballard Spahr was actively engaged, defending Plaintiffs, among others, against an alleged breach of a lease for non-payment, breach of the collateral assignment of the lease, UFA's guarantee of the lease, UFA's alleged misrepresentations, an alter-ego claim, and that Alamo Group intentionally interfered

[1] Defendants have filed a Motion to Dismiss the Complaint for Fraudulent Misrepresentation, which has been fully briefed and is currently under advisement with the Court.

with the lease and collateral assignment agreements. The third Washington Action, although filed by another lessor, asserted claims identical to those asserted in the second Washington Action. The second and third Washington Actions were consolidated and are still pending. Ultimately, Ballard Spahr withdrew as counsel from the consolidated Washington Actions in early January 2014.[2]

c. Furthermore, as the new owner of Wholesale Sports, Alamo Group assumed the defense of a lawsuit relating to an alleged prior obligation of Wholesale Sports pending in North Dakota state court ("Fargo Action"). Ballard Spahr was counsel of record to Wholesale Sports in the Fargo Action prior to and after Plaintiffs assumed the defense. Alamo Group was not a named defendant in the Fargo Action; thus, Ballard Spahr continued to represent Wholesale Sports at the direction of Mr. Gaube. The claims in the Fargo Action were limited to breach of contract on account of Wholesale Sports allegedly vacating the leased premises in default of the lease and ceasing to make monthly lease payments. The Fargo Action settled on the eve of trial**.**

B. Ballard Spahr's Prior Representations Are Not Substantially Related to the Fraud Action.

4. "A party's choice of counsel is entitled to substantial deference and the court should not quickly deprive parties of their freedom to choose the advocate who will

[2] Ballard Spahr's work for Plaintiffs ended several months prior to the commencement of the Fraud Action. *See* Adv. Proc. No. 14-50103.

represent their claims, particularly due to the risk that motions to disqualify may be motivated by an attempt to achieve a tactical advantage in the litigation."[3]

5. However, courts have

> inherent power to supervise the professional conduct of attorneys appearing before it. This power includes the authority to disqualify an attorney. At the outset, however, the court wants to emphasize that motions to disqualify are generally disfavored. The party seeking disqualification must clearly show that continued representation would be impermissible. As such, vague and unsupported allegations are not sufficient to meet this standard.[4]

6. Rule 1.9(a) of the Model Rules of Professional Conduct, which has been adopted by the District of Delaware as the Delaware Lawyers' Rules for Professional Conduct, provides:

> A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client

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[3] *In re David Cutler Indus., Ltd.*, 432 B.R. 529, 540 (Bankr. E.D. Pa. 2010) (citations and internal quotations marks omitted).

[4] *Integrated Health Servs. of Cliff Manor, Inc. v. THCI, Co. LLC*, 327 B.R. 200, 204 (D. Del. 2005) (citations and internal quotation marks omitted). *Lamson & Sessions Co. v. Mundinger*, No. 4:08CV1226, 2009 WL 1183217, at *3 (N.D. Ohio May 1, 2009) (citations and internal quotation marks omitted) (This right is not absolute and the Court must consider whether "the social need for ethical practice outweighs the party's right to counsel of his own choice."); *In re David Cutler Indus., Ltd.*, 432 B.R. at 540 (citations omitted).

> unless the former client gives informed consent, confirmed in writing.[5]

In the matter *sub judice*, the appropriate standard for ruling on Plaintiff's motion is the "substantial relationship" test. More specifically, the issue presented here is whether the Washington Actions and the Fargo Action are substantially related to Ballard Spahr's representation of Defendants in this action.

7. In determining whether a "substantial relationship" exists, "the court need not, nor should it, inquire into whether an attorney actually acquired confidential information during the prior representation related to the current representation. Rather, the court's primary concern is whether confidential information that might have been gained in the first representation may be used to the detriment of the former client in the subsequent action."[6]

8. In determining whether Ballard Spahr violated Rule 1.9(a), the Court must answer the following three questions:

> (1) What is the nature and scope of the prior representation at issue; (2) what is the nature of the present lawsuit against the former client; and (3) in the course of the prior representation, might the client have disclosed to his attorney confidences which could be relevant to the present

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[5] DE R. RPC Rule 1.9(a) (2014); Model Rule of Professional Conduct 1.9(a) (hereinafter "Rule 1.9"). Rule 1.9 serves three purposes:

> First, it is a prophylactic rule to prevent even the potential that a former client's confidences and secrets may be used against him. Without such a rule, clients may be reluctant to confide completely in their attorneys. Second, the rule is important for the maintenance of public confidence in the integrity of the bar. Finally, and importantly, a client has a right to expect the loyalty of his attorney in the matter for which he is retained.

In re Corn Derivatives Antitrust Litig., 748 F.2d 157, 162 (3d Cir. 1984). *See also Miller v. Sun Capital Partners, Inc. (In re IH 1, Inc.)*, 441 B.R. 742, 745 (Bankr. D. Del. 2011) (citations omitted).

[6] *Integrated Health Servs.*, 327 B.R. at 206 (citations and internal quotation marks omitted).

> action and, in particular, could any such confidences be detrimental to the former client in the current litigation?[7]

Plaintiffs, as movants, have the burden of establishing this "substantial relationship."[8]

9. Furthermore, the Third Circuit has adopted a balancing test when determining whether to disqualify counsel:

> Commitment of this matter to the district court's discretion means that the court should disqualify an attorney only when it determines, on the facts of the particular case, that disqualification is an appropriate means of enforcing the applicable disciplinary rule. It should consider the ends that the disciplinary rule is designed to serve and any countervailing policies, such as permitting a litigant to retain the counsel of his choice and enabling attorneys to practice without excessive restrictions.[9]

With this balancing test in mind, the Court will consider the three questions to determine whether Plaintiffs have met their burden in showing a "substantial relationship."

10. "In answering the first question, the court should focus upon the reasons for the retention of counsel and the tasks which the attorney was employed to perform."[10] In the Washington Actions and the Fargo Action, the issues revolved around breach of contract actions. As set forth above, in two of the Washington Actions, Ballard Spahr

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[7] *Integrated Health Servs.*, 327 B.R. at 206-07 (citations and internal quotation marks omitted).

[8] *INA Underwriters Ins. Co. v. Nalibotsky*, 594 F. Supp. 1199, 1207 (E.D. Pa. 1984).

[9] *United States v. Miller*, 624 F.2d 1198, 1201 (3d Cir. 1980) (citations omitted). Furthermore, if necessary, the Court may fashion on appropriate remedy if the Court believes that the Fraud Action is compromised by Ballard Spahr's prior representations. *Clark Capital Mgmt. Grp., Inc. v. Annuity Investors Life Ins. Co.*, 149 F. Supp. 2d 193, 198 (E.D. Pa. 2001) (footnote excluded) (holding that "when there is a risk that the underlying litigation may be tainted by participation of counsel, the court has the power to fashion an appropriate remedy."). *See also Intellectual Ventures I LLC v. Checkpoint Software Technologies Ltd.*, No. CIV. 10-1067-LPS, 2011 WL 2692968, at *5 (D. Del. June 22, 2011) (citations and internal quotation marks omitted) (holding that "disqualification is proper when the similarity in the two representations is enough to raise a common-sense inference that what the lawyer learned from his former client will prove useful in his representation of another client whose interests are adverse to those of the former client.").

[10] *Com. Ins. Co. v. Graphix Hot Line, Inc.*, 808 F. Supp. 1200, 1204 (E.D. Pa. 1992).

actively litigated on behalf of Alamo Group, including motion practice and propounding and responding to discovery requests.

11. "With respect to the second question, the court should evaluate the issues raised in the present litigation and the underlying facts."[11] None of the leases and contracts in the Washington Actions or the Fargo Actions are subject to the litigation in the Fraud Action, wherein the Plaintiffs have alleged fraud arising out of a purchase of a lease portfolio. Although the Washington Actions and the Fargo Action concerns leases, to some extent, the actions arise out of different facts and legal theories and different purchases of commercial real estate (the UFA transaction for the Washington Actions and the Fargo Action, and the Debtors' sale of leases in the Fraud Action).

12. Finally, in answering the third question, the court should be guided by the interpretation of the word "might have acquired" substantially related information if:

> (a) the lawyer and the client ought to have talked about particular facts during the course of the representation, or (b) the information is of such a character that it would not have been unusual for it to have been discussed between lawyer and client during their relationship.[12]

Here, Plaintiffs assert that Mark Gaylord, the attorney at Ballard Spahr who worked on the Washington Actions and the Fargo Action, had extensive personal contact with Alamo Group's principal owner, Don Gaube. Plaintiffs claim that Mr. Gaylord was provided with, and was privy to, extensive confidential information regarding Alamo

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[11] *Com. Ins. Co. v. Graphix Hot Line, Inc.*, 808 F. Supp. 1200, 1204 (E.D. Pa. 1992).

[12] *Realco Servs., Inc. v. Holt*, 479 F. Supp. 867, 872 (E.D. Pa. 1979); *see also Com. Ins. Co. v. Graphix Hot Line, Inc.*, 808 F. Supp. 1200, 1204 (E.D. Pa. 1992).

Group in relation to the deal with UFA, as well as Alamo Group's history of acquiring commercial real property, including Alamo Group's criteria for acquiring commercial leases. Plaintiffs allege that the Fraud Action against Defendants, like the Washington Actions and Fargo Action, arise directly out of Alamo Group's negotiations on a deal to acquire a portfolio of commercial leases.

13. The Court disagrees. In the case *sub judice*, Ballard Spahr was not involved when Plaintiffs purchased the lease portfolio underlying the Fraud Action; Ballard Spahr was originally retained by A&G to file retention application and then later to defend A&G in the Fraud Action.[13]

14. Furthermore, as set forth above, Ballard Spahr represented UFA in the negotiations that led to the UFA transaction, not Alamo Group – it was only after the UFA transaction was consummated that various landlords brought the Washington Actions and Alamo Group assumed the defense in the Fargo Action.

15. As to whether Ballard Spahr could have learned the litigation strategy of Plaintiffs during their representation of Alamo Group, the Court finds that these assertions are too vague. As stated in the official comments to Rule 1.9, in defining "substantially related" and the type of confidential information covered, states:

> [i]n the case of an organizational client, general knowledge of the client's policies and practices ordinarily will not preclude

[13] Ballard Spahr represented A&G Realty Partners, LLC ("A&G"), one of the Defendants, in August 30, 2013, in connection with A&G's retention. A&G's retention by the Debtors was prior to the sale to Alamo Group; thus there was no potential conflict at that time. The Court entered the sale Order regarding the leases purchased from the Debtors in October 2013. *See* Case No. 13-11565, D.I. 670. Subsequently, Plaintiffs filed the Fraud Action in March 2014. Thereafter, A&G contacted Ballard Spahr to represent the Defendants in the Fraud Action.

> a subsequent representation, on the other hand, knowledge of specific facts gained in a prior representation that are relevant to the matter in question ordinarily will preclude such representation.[14]

At most, Ballard Spahr may have information relating to Alamo Group's general policies and strategies – but nothing specific or confidential in nature as to preclude Ballard Spahr's representation of Defendants in the Fraud Action. Although the Washington Actions, Fargo Action, and Fraud Action all relate to various commercial leases, the litigations are sufficiently different in nature and scope to find that there is not substantial risk that confidential information was obtained that would be "materially adverse" to Plaintiffs' position in the Fraud Action.[15]

C. Conclusion

16. Balancing the above, including consideration of the substance of the Washington Actions, the Fargo Action, and the Fraud Action, and Defendant's right to retain counsel of their own choice, the Court hereby DENIES the Motion.

Christopher S. Sontchi
United States Bankruptcy Judge

Date: February 2, 2015

[14] Rule 1.9: Duties to Former Clients, Legis. Hist. (ABA) Rule 1.9, cmt. 3.

[15] *Id. See In re eToys, Inc.*, 331 B.R. 176, 197 (Bankr. D. Del. 2005) (citations omitted) ("While the relationships may raise an appearance of a conflict, they are not actual conflicts and disqualification is not warranted.").