2023 Caribbean Insolvency Symposium

Judges' Roundtable: Ethics Issues

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ABI 2023 Caribbean Insolvency Symposium
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Judges' Roundtable
Ethical Issues in Professional Retention Scenarios in Bankruptcy Cases

Moderator: Trish Redmond

Panelists: Judge Mark (Bankr. S.D. Fla.); Judge Isicoff (Bankr. S.D. Fla.); Judge Lamoutte (Bankr. D.P.R.); Judge Wanslee (Bankr. D. Ariz.); Judge Mora (Bankr. S.D. Fla.); Judge Carey (Hogan Lovells)

The panel will focus on ethics and particularly the risks involved in serving as local counsel, special counsel, and conflicts counsel. The panel will discuss the role of the court in monitoring and reviewing the scope and responsibilities of counsel in each of these roles. The panel will also discuss the relevant caselaw impacting an attorneys; ethical obligations, both to clients and to the Court.

I. The Ethical Rules

a. Attorneys must comply with the ethical obligations imposed by the jurisdiction in which they practice law.

b. For example, attorneys barred in Florida must comply with the Florida Rules of Professional Responsibility regarding retention requirements in addition to any requirements imposed by the Bankruptcy Code and Rules. (*See e.g.* Rule 4-1.7-4-1.10); (*See also* Model Rules of Professional Conduct 1.7-1.10 on conflicts of interest and duties to former and current clients).

c. "Directly adverse" – the Rules of Professional Responsibility dictate that a lawyer must not represent a client if the representation of one client will be "directly adverse" to another client. Direct adversity may not be so clear in a bankruptcy case, especially a large bankruptcy case, where there are multiple parties and attorneys involved in different capacities.

d. Conflicts at large law firms – Model Rule 1.10 generally imputes a conflict of one attorney to the entire law firm. However, there may be ways to avoid the conflict with proper screening.

II. The Bankruptcy Code & Rules

a. 11 U.S.C. § 327: Establishes specific requirements for the employment of certain professionals in bankruptcy cases.

   i. Under Section 327(a), to be employed by the trustee or debtor-in-possession, a professional may not hold an interest adverse to the bankruptcy estate and (2) must be "disinterested."

      1. "Disinterested" is defined in 11 U.S.C. 101(14) as:

         a. "The term 'disinterested person' means a person that—

            i. Is not a creditor, an equity security holder, or an insider;

            ii. Is not an was not, within 2 years before the date of the filing of the petition, a director, officer, or employee of the debtor; and

            iii. Does not have an interest materially adverse to the interest of the estate or of any class or 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."

   ii. Under Section 327(c), a professional is not disqualified from employment by a trustee or a debtor-in-possession solely because the professional represented an unsecured creditor in a case, unless a party objects to the employment. Consider who may have standing to object or a reason to object here.

iii. Under 327(e), a professional may be employed on a specific matter or for a "special purpose" in a bankruptcy case, if that professional previously represented the debtor, it would be in the best interest of the estate to hire the professional, and the professional does not hold an adverse interest as to the special purpose for which the professional is being employed. Special counsel is usually employed under this section.

iv. Who is a "professional" requiring court approval for their retention? Different jurisdictions may define "professional" differently depending on facts of the case. *See e.g. In re Metropolitan Hosp.*, 119 B.R. 910 (Bankr. E.D. Pa. 1990) (a professional is "someone with special knowledge and skill usually achieved through study and educational attainments whether licensed or not" who assists "the trustee [or the debtor-in-possession] with the fulfillment of his or her official duties."); *In re Nine West Holdings, Inc.*, 588 B.R. 678 (Bankr. S.D.N.Y. 2018) ("[A] professional person is one who plays an intimate or central role in the administration of the debtor's bankruptcy proceeding … In this Circuit, professional persons are defined to include firms or individuals who have been hired for the purpose of reorganizing the corporation or otherwise assisting it through Chapter 11 bankruptcy process") (internal citations and quotation marks omitted).

b. 11 U.S.C. § 328: Provides that professionals may be employed on any reasonable terms and conditions of employment, including on a contingent fee basis. Before filing, consider whether your jurisdiction or judge has a specific rule or practices on contingency or alternative fee arrangements.

c. 11 U.S.C. § 1103: Describes requirements for professionals to be retained by appointed committees. Committee professionals owe duty to committee body, not an individual creditor.

d. Fed. R. Bankr. P. 2014 & 2016

i. Rule 2014: Describes employment applications. Specifically requires professionals to state *all connections* with "the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States Trustee, or any person employed in the office of the United States trustee."

1. Disclosure is key, and continuing obligations are imposed to disclose potential connections that are discovered later in case.

2. Verified statement must be attached to application showing any connection.

3. Who is a "party in interest" in a bankruptcy case? How broad does the disclosure process need to go? For example, consider whether a creditor of a creditor is a party in interest in a bankruptcy case. Is this connection "so remote as to be de minimis"? *See In re Leslie Fay Companies, Inc.*, 175 B.R. 525 (Bankr. S.D.N.Y. 1994) (Rule 2014 requires disclosure of all connections "that are not so remote as to be *de minimis*"); *See In re Fundamental Long Term Care, Inc.*, 613 B.R. 484 (Bankr. M.D. Fla. 2014) (for discussion of remote connections not requiring disclosure).

4. When in doubt, "err, if at all, on the side of over-disclosure." *In re Enron Corp.*, 2002 Bankr. LEXIS 1720 at *17 (Bankr. S.D.N.Y. May 23, 2002).

ii. Rule 2016: Describes fee applications and additional disclosures required.

III. United States Trustee Guidelines (Appendix B Guidelines for Reviewing Applications for Compensation and Reimbursement of Expenses Filed Under United States Code by Attorneys in Larger Chapter 11 Cases)

a. UST Guidelines discuss the retention and compensation of co-counsel in larger bankruptcy cases.

b. UST Guidelines describe situations where debtors' counsel may seek to employ a "conflicts counsel" when general counsel is subject to a limited conflict that prevents general counsel from performing part of its duties.

    i. The Guidelines also describe the situations in which an objection to the proposed retention of conflicts counsel may be appropriate as follows: "(i) the responsibilities of conflicts counsel are not confined to discrete legal matters; (ii) the conflicts counsel will be used to handle matters that are inseparable from the major reorganization activities of the case (e.g. negotiation of major plan provisions); (iii) the conflicts counsel will act under the direct supervision of, and at the direction of, the lead counsel; (iv) the conflicts counsel's role will include filing or advocating pleadings that have been drafted by lead counsel; (v) the conflicts counsel has been retained to litigate matters in which the lead counsel has represented the debtor in settlement negotiations; (vi) the debtor will not (or cannot) create an ethical wall to screen the lead counsel from the work of the conflicts counsel."

        1. Like the UST guidelines, bankruptcy courts have also determined certain situations where conflicts counsel is objectionable or inappropriate, such as where proposed general bankruptcy counsel has a conflict of interest with a creditor who is central to the debtor's reorganization or where the adverse interests of two individual debtors are so extensive that each debtor should have its own independent bankruptcy counsel. *In re WM Distribution, Inc.*, 571 B.R. 866 (Bankr. D.N.M. 2017); *In re Project Orange Associates, LLC*, 431 B.R. 363, 375 (Bankr. S.D.N.Y. 2010).

c. UST Guidelines also describe situations where debtors' counsel may seek to employ "efficiency counsel" to perform "commoditized" work, such as claim objections or

avoidance actions, when the efficiency counsel may perform that work at a lower cost to the bankruptcy estate (or perhaps only does that type of work in the context of avoidance actions).

IV. Local Rules

a. Consider whether your jurisdiction has specific local rules on retention of general counsel, conflicts counsel, special counsel, or local counsel.

b. Why do certain jurisdictions impose requirements that others do not? Number of filings? Number of attorneys admitted?

c. Examples of specific local rules:

   i. Florida:

      1. S.D. Fla.: For debtors or trustee, specific forms required and must include copy of engagement letter or retention agreement (Local Rule 2014-1(A)); out of state lawyers must associate with local counsel with an office in the District (Local Rule 2090-1(C)(2)).

      2. M.D. Fla.: Requires local counsel, also has specific rule that you cannot appear too often on a pro hac vice basis so as to constitute "regular practice" in the M.D. Fla. (Local Rule 2090-1(C)(1))

   ii. New York: S.D.N.Y./E.D.N.Y do not have a requirement to associate with local counsel.

   iii. Delaware:

      1. Requires local counsel; local counsel must file all papers an attend all hearings (unless otherwise ordered) (Local Rule 9010-1). However, there are some exceptions.

      2. For example, attorneys who are admitted in Delaware but do not have an office in Delaware, may still appear (Local Rule 9010-

1(e)(ii). Local Rule 2014-1(a) requires professionals disclose material information relating to employment "promptly" after learning about it.

iv. Puerto Rico:

1. Must associate with local counsel unless the matter is uncontested with the exception of representation as counsel to a debtor or trustee (Local Rule 2090-1(c); Local Rule 9010-1(b)).

2. Local Rules also require specific disclosures (Local Rule 2014-1) and also provide guidance regarding disinterestedness and the term "connections." For example, "connections" include the representation of a creditor on a regular basis or in connection with a substantial matter.

v. Arizona: Requires local counsel with an office in the District and local counsel may be required to appear at hearings. (Local Rule 2090-1(b)).

V. Continuing Disclosures & Employment Applications

a. Continuing disclosures are necessary if information is discovered after initial application. "If facts arise that cause [Law Firm] to become interested, compensation will be in jeopardy, meaning constant vigilance of that risk falls to [Law Firm]." *In re Bear Communications, LLC*, 2021 WL 4256161 at *4 (Bankr. D. Kan. Sep. 17, 2021).

b. Timing – check local jurisdiction for when employment application is due and whether retroactive employment is necessary or contemplated under local rules.

i. *See e.g.* Local Rule 2014-1(b) from the S.D. Tex.: "If an application for approval of the employment of a professional is made within 30 days of the commencement of that professional's provision of services, it is deemed contemporaneous."

ii. If application is made more than 30 days after professional commences services, the application must explain why it was not filed sooner, why employment is required *nunc pro tunc*, and how approval of the application may prejudice interested parties.

VI. Recent Professional Retention Cases in Bankruptcy Context:

a. *In re Imerys Talc America, Inc.*, 38 F.4th 361 (3d Cir. 2022): Specific issue of appointment of future claims representative and standard for employing those representatives under 11 U.S.C. 524(g).

b. *In re Boy Scouts of America*, 35 F.4th 149 (3d Cir. 2022): Discussion of whether firm had actual conflict of interest due to pre-petition representation of insurance company. Discusses intersection of rules of professional responsibility and Bankruptcy Code.

V. Vignettes/Fact Patterns for Discussion:

a. Big Law Firm represents Tech Company in a Chapter 11 bankruptcy case. Big Law Firm also represents Tech Investor in unrelated SEC investigation. Tech Investor is a creditor in Tech Company's chapter 11 case. Big Law Firm seeks the employment of Small Law Firm to represent Tech Investor in the bankruptcy case as "conflicts counsel." Any issues with this relationship?

b. Pharmaceutical Company files a Chapter 11 bankruptcy case to address nationwide litigation against it and its parent Bigger Company. Bigger Company lends Pharmaceutical Company money to finance bankruptcy case. Pharmaceutical Company hires Big Law Firm to represent it in the bankruptcy case. Big Law Firm also represents Pharmaceutical Company and Bigger Company in the nationwide litigation outside of the bankruptcy case. Bigger Company hires Bigger Law Firm to represent it in the Pharmaceutical Company's bankruptcy case. Any issues with this relationship? Can Big Law Firm serve as general counsel? Does the retention of conflicts counsel for Pharmaceutical Company in dealing with Bigger Company resolve the conflict?

c. Restaurant Chain is incorporated in Connecticut, and all its restaurants are in New England. Restaurant Chain files bankruptcy case in Connecticut. Restaurant Chain hires Boston Law Firm to represent it in the bankruptcy case. Restaurant Chain hires Boutique Connecticut Firm as local counsel to Boston Law Firm, as Connecticut requires local counsel to have an office in Connecticut. Boutique Connecticut Firm is friendly with Boston Law Firm and has served as local counsel to Boston Law Firm several times before. Boston Law Firm partner sends Boutique Connecticut Firm associate filing on a Friday night and requests to file pleading immediately. What should associate do before filing?

d. Medium Law Firm represented Small Hospital in litigation against Big Hospital before bankruptcy case. Big Hospital files for bankruptcy, and it seeks to employ Small Law Firm as debtor's counsel. Big Hospital files an application to retain Medium Law Firm as special counsel to address certain regulatory issues for Big Hospital in which Medium Law Firm has expertise. Medium Law Firm works closely with Smaller Law Firm on all aspects of the bankruptcy case, including providing comments on all Smaller Law Firm's draft motions before filing them with the Court. Any issues with this retention and conduct during the case?

e. Medium Law Firm represented Plumbing Company in construction litigation pre-petition against General Contractor. General Contractor files for bankruptcy and hires partner at Medium Law Firm to be its bankruptcy lawyer. Plumbing Company asks associate at Medium Law Firm to file proof of claim in General Contractor bankruptcy case. How should associate respond to this request?

f. Giant Company files bankruptcy. Giant Law Firm has multiple clients with potential claims against Giant Company. Giant Law Firm associate files proof of claim in Giant Company bankruptcy case. The Court appoints a Chapter 11 Trustee for Giant Company's bankruptcy case. Chapter 11 Trustee seeks to employ Giant Law Firm as counsel, after Giant Law Firm associate filed proof of claim. Any objections to this application? Can Grant Law Firm serve as counsel to the Trustee?

Does hiring special counsel solve the conflict? Can Giant Law Firm ask the Creditors' Committee to undertake any issues with the proof of claim?

g. Small Law Office seeks to file a chapter 11 bankruptcy case due to several employees leaving the firm and/or retiring. Small Law Office believes it has various claims against former partners of the firm. Small Law Office wants to pursue that litigation in the bankruptcy case. Small Law Office hires Debtor Lawyer to represent Small Law Office in bankruptcy case. Debtor Lawyer files application to employ Small Law Office's Managing Partner as special counsel solely to pursue litigation against former partners. Any objections to that application?

h. Unsecured Creditors Committee Member Big Business had a relationship with Big Law Firm pre-petition. Big Business becomes chairman of Committee. Big Law Firm filed notice of appearance in Debtor's bankruptcy case on behalf of Member. Unsecured Creditors Committee then seeks to hire Big Law Firm as Committee counsel. Any objections?

Faculty

Hon. Kevin J. Carey is a partner in Hogan Lovells US LLP's Business Restructuring and Insolvency practice in Philadelphia and is a retired bankruptcy judge. He also is ABI's President and represents both companies and creditors in domestic and cross-border bankruptcy proceedings. Judge Carey was first appointed to the U.S. Bankruptcy Court for the Eastern District of Pennsylvania in 2001, then in 2005 began service on the U.S. Bankruptcy Court for the District of Delaware (serving as chief judge from 2008-11). During that time, he authored more than 200 reported decisions, issued important rulings on key issues such as valuation, fiduciary duties and other complex chapter 11 and confirmation issues, and presided over such high-profile cases as *Exide Technologies*, *Tribune Co.* and *New Century Financial*. Judge Carey was the first judge to serve as global chair of the Turnaround Management Association and is an honorary member of the Turnaround, Restructuring and Distressed Investing Hall of Fame, as well as a Distinguished Fellow of the Association of Insolvency & Restructuring Advisors. In addition, he is a Fellow of the American College of Bankruptcy and a member of the International Insolvency Institute, as well as a contributing author to *Collier on Bankruptcy*. He also is a part-time adjunct professor in the LL.M. in Bankruptcy program at St. John's University School of Law in New York City. Judge Carey began his legal career in 1979 clerking for Bankruptcy Judge Thomas M. Twardowski, then served as clerk of court of the U.S. Bankruptcy Court for the Eastern District of Pennsylvania. He received his B.A. in 1976 from Pennsylvania State University and his J.D. in 1979 from Villanova University School of Law.

Hon. Laurel M. Isicoff is Chief Judge for the U.S. Bankruptcy Court for the Southern District of Florida in Miami, initially appointed on Feb. 13, 2006, and named chief judge on Oct. 1, 2016. She serves on the Judicial Conference Committee on the Administration of the Bankruptcy System. Judge Isicoff serves on the Judicial Conference Committee on the Administration of the Bankruptcy System and on its subcommittee on Diversity, Equity and Inclusion. As a member of the American College of Bankruptcy, she serves a member of its *Pro Bono* Committee and is immediate past chair of its Judicial Outreach Committee, and from 2021-22 she co-chaired the College's Commission on Diversity, Equity and Inclusion. In recognition of that service, as well as her long-standing commitment to diversity, equity and inclusion, she received the inaugural DEI Excellence Award from the College. Judge Isicoff also currently serves as judicial chair of the *Pro Bono* Committee of the Business Law Section of the Florida Bar, and as judicial chair of the BLS Financial Literacy Task Force, and she is a member of the Florida Bar Standing Committee on *Pro Bono*. Prior to becoming a judge, Judge Isicoff specialized in commercial bankruptcy, foreclosure and workout matters both as a transactional attorney and litigator for 14 years with the law firm of Kozyak Tropin & Throckmorton, after practicing for eight years with Squire, Sanders & Dempsey, now known as Squire Patton Boggs. Following law school, she clerked for Hon. Daniel S. Pearson at the Florida Third District Court of Appeal before entering private practice. Judge Isicoff is a past president of the National Conference of Bankruptcy Judges and of the Bankruptcy Bar Association (BBA) of the Southern District of Florida, and, until she took the bench, chaired the *Pro Bono* Task Force for the BBA. She speaks extensively on bankruptcy around the country, and is committed to increasing *pro bono* service, diversity, equity and inclusion, and financial literacy for all. Judge Isicoff received her J.D. from the University of Miami School of Law in 1982.

Hon. Robert A. Mark is a U.S. Bankruptcy Judge for the Southern District of Florida in Miami, appointed in 1990, and he served as Chief Judge from 1999-2006. Prior to his appointment to the bench, Judge Mark was head of the bankruptcy department of the Miami firm of Stearns, Weaver, Miller, Weissler, Alhadeff & Sitterson, PA. He is a frequent speaker at international programs sponsored by INSOL, III, IWIRC and ABI, and he has served for several years as the co-judicial chair of the ABI's Caribbean Insolvency Symposium. Judge Mark is a Fellow of the American College of Bankruptcy and an author for *Collier on Bankruptcy*. His community activities include participation in a program that offers internships to minority law students, and participation in financial education programs for high school students through the Bankruptcy Bar Association's CARE program, which teaches students about the dangers of credit card abuse. Judge Mark is a graduate of Boalt Hall School of Law, University of California at Berkeley.

Hon. Mindy A. Mora is U.S. Bankruptcy Judge for the Southern District of Florida in West Palm Beach, appointed on April 6, 2018. She practiced in the areas of bankruptcy, commercial finance, and securitized real estate finance and litigation from 1982-2018 prior to her appointment to the bench by the Eleventh Circuit Court of Appeals. Judge Mora is a Fellow of both the American College of Bankruptcy and the American College of Commercial Finance Attorneys. She previously chaired the Business Law Section of The Florida Bar, which represents the interests of more than 5,000 business lawyers within the State of Florida. Throughout much of her legal practice, she has been active in the development of Florida's commercial laws, most recently as a member of The Florida Bar Business Law Section task force that prepared draft Florida legislation adopting a modified version of the Uniform Commercial Real Estate Receivership Act. Judge Mora is a member of NCBJ (National Conference of Bankruptcy Judges) and has served on its Technology, New Member and Education Committees. She also participates as a member of the Business Law Sections of both the American Bar Association and The Florida Bar, the Association of Commercial Finance Attorneys, the Bankruptcy Bar Association of South Florida, and the International Women's Insolvency & Restructuring Confederation. Judge Mora regularly lectures on commercial law and bankruptcy topics to lawyers and other judges throughout the U.S. From 2018-20, Judge Mora served as the judicial chair of the Local Rules Committee, which promulgated the proposed amendments to the Local Rules for consideration by the bench of the Bankruptcy Court for the Southern District of Florida. She received her B.B.A. from George Washington University in 1979 and her J.D. from New York University School of Law in 1982.

Hon. Madeleine C. Wanslee is a U.S. Bankruptcy Judge for the District of Arizona in Phoenix, sworn in on March 17, 2014. Previously, she was an associate and then partner at Gust Rosenfeld, PLC, where she was active in the firm's management committee and co-chaired the firm's Bankruptcy Practice Group. Her practice focused on bankruptcy and creditors' rights, and she represented small businesses, financial institutions, corporations and state agencies. While in private practice, Judge Wanslee was a certified bankruptcy specialist. She also argued a number of appeals, including *United Student Aid Funds Inc. v. Espinosa* before the U.S. Supreme Court. Judge Wanslee sits on the Ninth Circuit Conference Executive Committee, is program chair for the 2023 Ninth Circuit Judicial Conference, and is a former chair of the Ninth Circuit Bankruptcy Judges Education Committee. She helped to charter and is past president of the Arizona Bankruptcy American Inn of Court. Before becoming a judge, she served on the ABC's Standards Committee and on the Arizona State Bar's Bankruptcy Advisory Committee, which certifies bankruptcy specialists, and chaired the Arizona State Bar's Bankruptcy Section and the Lawyer Representatives to the Ninth Circuit Court of Ap-

peals. Judge Wanslee received her B.F.A. and B.A. from the University of Arizona and her J.D. from Gonzaga University School of Law, where she served as a writer and executive editor of the *Gonzaga Law Review*. Following law school, she clerked for Chief Bankruptcy Judge Robert C. Jones of the District of Nevada.