2022 Delaware Views from the Bench

Luncheon Keynote

Hon. Craig T. Goldblatt, Moderator
U.S. Bankruptcy Court (D. Del.) | Wilmington

Daniel B. Kamensky
Creditor Rights Coalition | Roslyn, N.Y.

Morgan L. Patterson, Facilitator
Womble Bond Dickinson | Wilmington

2022

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November 17, 2022

Luncheon Fireside Chat: Creditor Committee Fiduciary Duties

A. Panelists

a. Honorable Judge Craig Goldblatt:

i. Judge Goldblatt is a U.S. Bankruptcy Judge for the District of Delaware in Wilmington, where he has served since his appointment in April 2021. Prior to his appointment, he was a bankruptcy litigator in the Washington, D.C. office of WilmerHale, where his practice primarily involved the representation of financial institutions and other commercial creditors in complex bankruptcy litigation and appeals. Earlier in his career, Judge Goldblatt clerked for Hon. Richard D. Cudahy of the U.S. Court of Appeals for the Seventh Circuit and Hon. David H. Souter of the U.S. Supreme Court. He is a Conferee in the National Bankruptcy Conference (for which he serves as Secretary) and is a vice president of the American College of Bankruptcy. He also has been active on the Business Bankruptcy Committee of the American Bar Association's Business Law Section. Judge Goldblatt has served on the Education Committee of the National Conference of Bankruptcy Judges and as an adjunct professor at Georgetown University Law Center and George Washington University Law School, where he teaches classes focused on bankruptcy law

b. Mr. Daniel Kamensky:

i. Mr. Kamensky is a Member of the Advisory Board of the Creditor Rights Coalition, a nonprofit association established to serve as the collective and leading voice representing all stakeholders with an interest in protecting creditor rights. Mr. Kamensky is the former managing partner of Marble Ridge Capital which was recognized as leading manager by Absolute Return Magazine for all new funds in 2016 and nominated as a leading manager for all distressed funds in 2017. Prior to founding his firm, Mr. Kamensky was a Partner at Paulson & Co. Inc., and held various senior positions at Barclays Capital and Lehman Brothers in their Distressed & Special Situations Groups. Mr. Kamensky started his career as an attorney at Simpson Thacher & Bartlett. He formerly served as Chairman of the Bankruptcy & Creditor Rights Group of the Managed Funds Association and as Co-Chair of the Trade Practices Committee of the Loan Sales & Trading Association. He also served as an advisory board member of the American Bankruptcy Institute Commission to Study Reform of Chapter 11 and has written and lectured extensively on bankruptcy and restructuring topics.

B. Topic Introduction

It is well settled that official committee members owe a fiduciary duty to act in the best interest of the class it represents. Such duty is violated when a committee member acts in its own

best interest as opposed to the group as a whole. Similarly, committee counsel owes a fiduciary duty to the group.

The panel will discuss the issues that can arise during stressful, fast-paced negotiations that so often take place in chapter 11 cases. Specifically, Mr. Kamensky acted as a member of the Official Committee of Unsecured Creditors on behalf of bondholder, Marble Ridge Capital, during the chapter 11 proceeding of Neiman Marcus. Mr. Kamensky and Judge Goldblatt will have an in-depth discussion regarding the mistakes and missteps of committee members and counsel during Neiman Marcus and the lessons to be learned for future committees.

The written materials contained here provide a legal and factual foundation for the discussion.

C. Factual Background Neiman Marcus

a. Neiman Marcus distress began as early as 2015 due to the shift in consumer spending from brick and mortar to online shopping
b. Marble Ridge invested in Neiman Marcus summer 2018 by purchasing its unsecured bonds which were sold at a deep discount
c. Marble Ridge believed that Neiman Marcus's sponsors should monetize its valuable online shopping affiliate, MyTheresa, to deleverage the company to avoid a default
d. Neiman Marcus sponsor, Ares Management, instead distributed the MyTheresa business as a dividend to the sponsors without payment of any consideration
e. Marble Ridge and other bondholders commenced litigation in various state courts over the transaction
f. Neiman Marcus filed bankruptcy in May 2020, shortly after the start of the Covid-19 pandemic in the United States
g. Marble Ridge joined the creditors committee as the largest unsecured creditor with $75 million of bonds at the time of the filing

D. Creditor Committee Member Duties

a. Committee Appointed Pursuant to Section 1102:

    i. (a)(1) Except as provided in paragraph (3), as soon as practicable after the order for relief under chapter 11 of this title, the United States trustee shall

appoint a committee of creditors holding unsecured claims and may appoint additional committees of creditors or of equity security holders as the United States trustee deems appropriate.

a. 11 U.S.C. § 1102

b. Committee Members Appointed by U.S. Trustee. The process includes submission of an application and interview by the U.S. Trustee.

c. Committee Members May Include the Following:

i. Trade Creditors
ii. Local Interest Creditors
iii. Claims Traders
iv. Legacy liabilities (i.e. unions, PBGC)
v. Tort Claimants
vi. Employee/WARN Claimants

d. Committee granted powers by Bankruptcy Code to:

i. Investigate debtors
ii. Negotiate plan
iii. "other" duties that would be in the interest of those the committee represents

a. 11 U.S.C. § 1103

e. Third Circuit Recognizes Committee Member Fiduciary Duties in Section 1103(c):

i. "The Bankruptcy Code authorizes the appointment of a committee of creditors, see 11 U.S.C. § 1102, and grants to such committees the power to investigate debtors, to negotiate a bankruptcy reorganization plan, and to "perform such other services as are in the interest of those represented,"

ii. "We have construed § 1103(c) as implying a fiduciary duty on the part of members of a creditor's committee, such as the present Unsecured Creditors Committee, toward their constituent members."

a. *Westmoreland Hum. Opportunities, Inc. v. Walsh*, 246 F.3d 233, 256 (3d Cir. 2001)

f. Committees are made up of parties with competing interests – it is widely accepted that committee members are entitled to act in their own financial interests.

i. "Although Committee members owe fiduciary duties, they are hybrids who serve more than one master. Every member of the Committee is, by definition, a creditor. Thus, he is in competition with every other creditor for a piece of a shrinking pie. He may assert his rights as a creditor to the detriment of the creditor body as a whole without running afoul of his fiduciary obligations."

a. *Rickel & Associates, Inc. v. Smit (In re Rickel & Associates, Inc.)*, 272 B.R. 74, 100 (Bankr. S.D.N.Y. 2002) (emphasis added).

g. Committee member violates its fiduciary duty if it pursues its own interests over that of the whole.

i. Third Circuit:

1. "A committee member violates its fiduciary duty by pursuing a course of action that furthers its self-interest to the potential detriment of fellow committee members."

a. *Westmoreland Hum. Opportunities, Inc. v. Walsh*, 246 F.3d 233, 256 (3d Cir. 2001)

ii. Second Circuit:

1. "The Second Circuit has further written that a creditors' committee, as fiduciary, 'must guide its actions so as to safeguard as much as possible the rights of minority as well as majority creditors.'"

a. *In re Spiegel*, 292 B.R. 748, 750 (Bankr. S.D.N.Y. 2003) (*citing In re Bohack Corp. et al.*, 607 F.2d 258, 262 n. 4 (2d Cir. 1979))

h. Courts Hold Committees to Strict Fiduciary Standard

i. *In re Spiegel*, 292 B.R. 748, 751 (Bankr. S.D.N.Y. 2003) (stating "this Court intends to hold the Committee to full and strict compliance with its fiduciary obligations" in denying Committee request to allow individuals at committee member companies not involved in the case to trade in the debtor's securities).

ii. "To be effective in that representation, it is necessary for the committee to speak with one voice."

a. *Westmoreland Hum. Opportunities, Inc. v. Walsh*, 327 B.R. 561, 573 (W.D. Pa. 2005)

i. Committee Members Liable Only Where Acting Outside their Authority

i. Bankruptcy Code "is silent as to the liability of that entity for breaches of its duty or other misconduct. . . ."

a. *In re Walnut Equip. Leasing Co., Inc.*, No. 97-19699DWS, 2000 WL 1456951, at *2 (Bankr. E.D. Pa. Sept. 22, 2000)

ii. "[C]ommittee members enjoy qualified immunity "from legal action for matters relating to the performance of the committee's duties."

iii. "They are liable only for actions taken outside their authority or for willful misconduct."

a. *In re Walnut Leasing Co., Inc.*, No. 97-19699, 2000 WL 283843, at *2 (E.D. Pa. Mar. 15, 2000) (internal citations omitted).

E. Creditor Committee Counsel Duties

a. Committee counsel has similar fiduciary duties to the class the committee represents.

i. "Counsel may not represent any other entity having an adverse interest to these parties in connection with the case under Section 1103(b) of the Bankruptcy Code."

a. *In re Mesta Mach. Co.*, 67 B.R. 151, 157 (Bankr. W.D. Pa. 1986).

ii. "A creditors committee has a fiduciary duty to the individual members that committee represents. Counsel for the committee has a fiduciary duty to the committee and its constituency. These fiduciary duties cannot be misdirected by the relationship of the committee's counsel with other entities that have other considerations than the committee or its constituency."

a. *Matter of Celotex Corp.*, 123 B.R. 917, 920 (Bankr. M.D. Fla. 1991) (internal citations omitted).

b. Attorneys should avoid conflicts.

i. An attorney representing a creditors' committee should not place himself in a position where he is serving dual or conflicting duties.

a. *In re Mesta Mach. Co.*, 67 B.R. 151, 158 (Bankr. W.D. Pa. 1986).

c. Attorneys seeking fees from the Bankruptcy Court also owe a fiduciary duty to the Court.

i. We repeat that an attorney seeking a fee in a bankruptcy matter does have a fiduciary obligation to the court.

a. *Matter of Arlan's Dep't Stores, Inc.*, 615 F.2d 925, 941 (2d Cir. 1979).

F. Lessons Learned from Neiman Marcus

a. Identify and Acknowledge Conflicts and Recuse Yourself
b. Seek and Take Adequate Time in Decision Making
c. Be Aware of Communications and Seek Counsel
d. Acknowledge an Issue Immediately and Seek Counsel

Faculty

Hon. Craig T. Goldblatt is a U.S. Bankruptcy Judge for the District of Delaware in Wilmington, where he has served since his appointment in April 2021. rior to his appointment, he was a bankruptcy litigator in the Washington, D.C. office of WilmerHale, where his practice primarily involved the representation of financial institutions and other commercial creditors in complex bankruptcy litigation and appeals. Earlier in his career, Judge Goldblatt clerked for Hon. Richard D. Cudahy of the U.S. Court of Appeals for the Seventh Circuit and Hon. David H. Souter of the U.S. Supreme Court. He is a Conferee in the National Bankruptcy Conference (for which he serves as Secretary) and is a vice president of the American College of Bankruptcy. He also has been active on the Business Bankruptcy Committee of the American Bar Association's Business Law Section. Judge Goldblatt has served on the Education Committee of the National Conference of Bankruptcy Judges and as an adjunct professor at Georgetown University Law Center and George Washington University Law School, where he teaches classes focused on bankruptcy law. He received his Bachelor's degree *magna cum laude* from Georgetown University in 1990 and his J.D. with honors from the University of Chicago Law School in 1993, where he served as comment editor of the *University of Chicago Law Review*.

Daniel B. Kamensky is a member of the advisory board of the Creditor Rights Coalition in Roslyn, N.Y., and is the former managing partner of an SEC-registered investment advisory firm that was recognized as a leading manager by *Absolute Return Magazine* for two consecutive years. Prior to founding his firm, he was a partner at Paulson & Co. Inc, and held various senior positions at Barclays Capital and Lehman Brothers in their Distressed & Special Situations Groups. Mr. Kamensky started his career as an attorney at Simpson Thacher & Bartlett. He formerly served as chairman of the Bankruptcy & Creditor Rights Group of the Managed Funds Association and as co-chair of the Trade Practices Committee of the Loan Sales & Trading Association. He also served as an advisory board member of ABI's Commission to Study the Reform of Chapter 11 and has written and lectured extensively on bankruptcy and restructuring topics. Mr. Kamensky clerked for Hon. Susan H. Black of the Eleventh Circuit Court of Appeals from 1998-99. He received his B.A. *magna cum laude* in 1995 from Georgetown University and his J.D. *cum laude* in 1998 from Georgetown University Law Center.

Morgan L. Patterson is a partner with Womble Bond Dickinson in Wilmington, Del., where her practice focuses on corporate bankruptcy and creditors' rights in complex chapter 11 proceedings. She has broad experience representing debtors, creditors' committees, lenders, bondholders, secured and unsecured creditors, liquidation trustees, landlords, asset-purchasers, and other interested entities in various bankruptcy reorganization and liquidation proceedings. Ms. Patterson's bankruptcy work includes all matters of litigation and transactions, including involuntary petitions, avoidance actions, relief-from-stay proceedings, trustee motions, sale and purchase of assets, executory contracts and lease issues, post-petition financing, disclosure statements, plan confirmation, and representing liquidating trustees and plan administrators in the winding down of estates. She also has expertise with cross-border insolvency proceedings, specifically with respect to the consummation of large cross-border asset sales. Ms. Patterson is Membership chair for the International Women's Insolvency & Restructuring Confederation's Delaware Chapter and is a member of the Federal Bar

Association, ABI, the Delaware Bankruptcy Inn of Court and the Delaware State Bar Association. She has been listed in *Chambers USA* as a Ranked Lawyer for Bankruptcy/Restructuring in Delaware since 2022 and was listed as a "Delaware Rising Star" in Bankruptcy by *Super Lawyers* from 2018-19. Ms. Patterson received her B.A. *magna cum laude* in 2005 from Temple University and her J.D. *magna cum laude* in 2009 from Widener University School of Law, where she was Bluebook editor of the *Delaware Journal of Corporate Law*.