Supreme Court Update: Practical Impact of Supreme Court Decisions

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SUPREME COURT UPDATE:

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SIGNIFICANT BANKRUPTCY CASES DECIDED IN THE 2014-15 TERM AND THEIR IMPACT ON PRACTICE AND PROCEDURE

Baker Botts v. Asarco, 135 S. Ct. 2158 (2015).

Facts: The trustee's § 327(a) professionals obtained a judgment on a fraudulent transfer claim worth between $7 and $10 billion. After the debtor emerged from bankruptcy, it opposed the firms' fee applications. The firms ultimately won a $120 million fee award, a $4.1 million enhancement fee for exceptional performance, and more than $5 million fees on fees. The debtor appealed.)

Holding: Bankruptcy Courts are not permitted to award attorneys' fees to professionals for defending fee applications in court. Time spent preparing fee applications is compensable.)

Rational: Under the American Rule, litigants are responsible for their own attorney fees, whether they win or lose, absent statutory or contractual fee shifting

Practical Implications:

1. Discuss provisions in engagement letters and approval of those terms by the court?

In re Boomerang Tube, LLC, Case No. 15-11247 (Bankr. D. Del. January 29, 2016)(sustaining US Trustee's objections to successful fee defense indemnifications in retention applications).

2. What about a performance bonus in lieu of the fees?

Harris v. Viegelahn, 135 S. Ct. 1829 (2015).

Issue: What happens to post-petition wages held by a Chapter 13 trustee at the time the case is converted to a Chapter 7.

Holding: Post-petition wages must be returned to the Debtor

Rationale: The S. Ct. focused on the nature of the funds. Post-petition wages do not become property of the estate in a Chapter 7.

Practical Implications:

1. What if the money held by the Chapter 13 Trustee is not wages?

2. What if the case is converted before the Chapter 13 plan is confirmed?

In re Ulmer, 2015 WL 3955258 (Bankr. W.D. La. June 25, 2015)

In re Spraggins, 2015 WL 5227836 (Bankr. D.N.J Sept. 4, 2015)

3. What if the case is dismissed after the Chapter 13 plan is confirmed?

In re Edwards, 538 B.R. 536 (Bankr. S.D. Ill. 2015)

4. What if the case is dismissed before the Chapter 13 plan is confirmed?

In re Hightower, 2015 WL 5766676 (Bankr. S.D. Ga. Sept. 30, 2015).

Bank of America v. Caulkett, 135 S. Ct. 1995 (2015).

Holding: Chapter 7 Debtor could not strip off a wholly underwater junior lien pursuant to section 506(d).

Practical Implications:

1. What happens to the liens that have been stripped? Potential motions for reconsideration?

In re Chartier, Case No. 6:14-bk-06563 (M.D. Fla. 2015)

(denying a Rule 60 motion seeking to vacate a *McNeal* strip off order because of *Caulkett*. Rule 60(b)(6) relief "is an extraordinary remedy," and creditor failed to file an appeal.)

2. What can debtors do going forward?

Chapter 20?

In re Whiting, Case No. 3:14-bk-2004 (M.D. Fla., Oct. 8, 2015).

(The Court discharged the Chapter 7 debtors' debt to SunTrust. In the debtors' subsequent Chapter 13, the Court stripped SunTrust's fully unsecured second mortgage on debtors' homestead. As a result, "SunTrust's unsecured claim is not allowable in this case pursuant to § 502(G)" and the debtors' Chapter 13 plan was permitted to provide that "the Trustee shall make no payments" to SunTrust on account of SunTrust's unsecured claim.)

In re Boukatch, 533 B.R. 292 (B.A.P. 9th Cir. 2015).

(Recognizing a split in authority, the BAP held Chapter 20 debtor may avoid wholly unsecured junior lien against principal residence under §§ 506(a) and 1322(b)(2), even though debtor is not eligible for Chapter 13 discharge: "'growing consensus of courts'... hold that nothing in the Code prevents chapter 20 debtors from stripping a wholly unsecured junior lien against the debtor's principal residence, notwithstanding their lack of eligibility for a chapter 13 discharge")

In re Scantling, 754 F.3d 1323 (11th Cir. 2014).

(strip off of wholly unsecured junior mortgage permitted in a Chapter 20 case)(decided prior to *Caulkett*)

Wellness Int'l Network, Ltd. v. Sharif, 135 S. Ct. 1932 (2015).

Holding: A bankruptcy court can finally adjudicate Stern claims with the parties knowing and voluntary consent. Consent can be implied based on actions and words.

1. Can parties consent extend to jury trials?

2. Experience with *de novo* review of *Stern* claims?

3. Practice and procedures for handling pretrial matters where there is not consent. How are dispositive motions handled?

THE CURRENT 2015-16 TERM

Husky International Electronics, Inc. v. Ritz, 787 F.3d 312 (5th Cir. 2015), *cert. granted* 2015 U.S. Lexis 7036 (U.S. Nov. 6, 2015).

Issue: Whether the "actual fraud" bar to discharge under Section 523(a)(2)(A) of the Bankruptcy Code applies only when the debtor has made a false representation, or whether the bar also applies when the debtor has deliberately obtained money through a fraudulent-transfer scheme that was actually intended to cheat a creditor.

Practical Implications: Predictions

1. An Amicus brief filed by law professors from St. John's Law School argues that a discharge for fraudulent transfer liability is governed exclusively by 727(a), namely fraudulent transfer debt more than one year old is discharged. Thoughts on this argument?

2. *Law v. Siegel*, 134 S. Ct. 1188 (2014) provided that the Code must be applied according to its plain text, not "based on whatever considerations [the courts] deem appropriate." 134 S .Ct. at 1196. Despite the debtor's egregious misconduct, the Supreme Court held that the bankruptcy courts lacked statutory authority to surcharge the debtor's exempt property for the legal costs incurred as a consequence. Does this suggest that the 5th Circuit will be affirmed?

3. Types of non-dischargeability cases that may be impacted by *Husky*.

NOTABLE CASES FROM PRIOR TERMS AND THEIR RESIDUAL IMPACT ON BANKRUPTCY PRACTICE

Law v. Siegel, 134 S. Ct. 1188 (2014).

Holding: A bankruptcy court cannot use equitable powers to surcharge a valid state exemption for payment of a Chapter 7 Trustee's attorneys' fees incurred in avoiding a fraudulent lien created by the Chapter 7 Debtor.

Practical Implications:

1. Has the case curtailed the activities of chapter 7 trustees or the equitable powers of the bankruptcy court significantly?

2. Does the decision impair the bankruptcy court's ability to enter "inherent" authority sanctions?

In re Charbono, 790 F.3d 80 (1st Cir. 2015)(recognizing that such sanctions are permissible after *Law v. Siegel,* as acknowledged by the S.Ct.).

Dhiya v. Kramer (In re Khan), 593 Fed. Appx. 83 (2d Cir. 2015)(sanctions permitted under 28 U.S.C. § 1927).

3. Does the decision preclude disgorgement of interim fees?

In re Headlee Mgmt. Corp., 519 B.R. 452 (Bankr. S.D.N.Y. 2014)(citing Law v. Siegal as a reason why the court lacks authority to disgorge interim fees paid to professionals); *see also In re Home Loan Serv. Corp.*, 533 B.R. 302 (Bankr. N.D. Calif. 2015).

4. Does *Law v. Siegel* restrict *Marrama v. Citizens Bank*, 549 U.S. 365 (2007) with respect to a debtors right to convert a Chapter 7 to a Chapter 11?

In re Foster, 530 B.R. 650 (N.D Tex. 2015)(affirming the denial of a conversion motion, notwithstanding *Law v. Siegel*).

5. Does *Law v. Siegel* preclude the equitable remedy of substantive consolidation?

In re Kodsi, 2015 Bankr. Lexis 143 (Bank. S.D. Fla. January 13, 2015)(limiting *Law v. Siegel* to the use of equitable powers to override specific provisions of the Bankruptcy Code)

RadLAX Gateway Hotel, LLC v. Amalgamated Bank, 132 S. Ct. 2065 (2012).

Holding: A cram down plan cannot be confirmed if the secured creditor is not permitted to credit bid at a proposed sale of collateral free and clear. This case also stands for the proposition that general provisions in the Bankruptcy Code cannot be used to avoid a specific statutory provision.

Practical Implications:

1. How does RadLAX relate to the ability to recover fees for substantial contribution in a Chapter 7 case?

Mediofactoring v. McDermott (In re Connolly N. Am., LLC), 802 F.3d 810 (6th Cir. 2015)(analyzing the general/specific proposition in the context of administrative claim for substantial contribution in a Chapter 7 case).

2. How does RadLAX relate to the issue of whether post-confirmation inheritance was property of the estate in a Chapter 13 case?

In re Gilbert, 526 B.R. 414 (Bankr. N.D. Ga. 2015)(applying the RadLAX general/specific analysis to the interplay between §§ 541 and 1306(a)(1)).

In re: BOOMERANG TUBE, INC., et al., Chapter 11, Debtors.

Case No. 15-11247 Jointly Administered.

United States Bankruptcy Court, D. Delaware.

January 29, 2016.

OPINION[1]

MARY F. WALRATH, Bankruptcy Judge.

Before the Court are the Objections of the United States Trustee (the "UST") to the Applications of Brown Rudnick LLP, and Morris, Nichols, Arsht & Tunnel LLP ("Committee Counsel") as counsel to the Official Committee of Unsecured Creditors (the "Committee") of **Boomerang Tube**, LLC (the "Debtor") because they include a provision indemnifying them for expenses incurred in any successful defense of their **fees**. For the reasons stated below, the Court will sustain the UST's objection.

I. BACKGROUND

On June 9, 2015, the Debtor and its affiliates filed chapter 11 petitions. The UST appointed the Committee, which thereafter retained counsel. Committee Counsel each seek approval under section 328(a) of a provision in their retention applications entitling them to compensation from the Debtors' estates (subject to approval by the Court pursuant to sections 330 and 331) for any **fees**, costs or expenses, arising from the successful defense of their **fees**.

The UST objected to the inclusion of the fee defense provisions in the retention applications.[2] The UST contends that the provision is precluded by the recent Supreme Court holding in ASARCO. See Baker Botts L.L.P. v. ASARCO LLC, 135 S. Ct. 2158, 2169 (2015). The UST also argues that the fee defense provisions should not be approved because such **fees** are outside the scope of employment and are unreasonable.

The Court heard argument and ordered supplemental briefings on the issue at the hearing held on August 11, 2015. The matter is now ripe for decision.

II. JURISDICTION

The Court has jurisdiction over this contested matter. 28 U.S.C. §§ 1334 & 157(b)(1).

III. DISCUSSION

The UST advances three arguments in its objection: (1) the Supreme Court decision in ASARCO directly bars the fee defense provisions; (2) section 328(a) creates no exception to the American Rule's general prohibition against fee shifting; and (3) the fee defense provisions cannot be approved under section 328(a) because they are unreasonable and seek to compensate professionals for work not within the scope of their employment.

A. The ASARCO Decision

The UST argues that the fee defense provisions are barred by the Supreme Court's decision in ASARCO. In ASARCO,

the Supreme Court affirmed the Fifth Circuit's denial of **fees** to debtor's counsel for defending its **fees** from objections raised by the debtor. The Supreme Court stated that the "basic point of reference when considering the award of attorney's **fees** is the bedrock principle known as the American Rule: Each litigant pays his own attorney's **fees**, win or lose, unless a statute or contract provides otherwise." ASARCO, 135 S. Ct. at 2164 (quoting Hardt v. Reliance Std. Life Ins. Co., 560 U.S. 242, 252-53 (2010)). The Court held that any statutory departures from the American Rule must be "specific and explicit" and must "authorize the award of `a reasonable attorney's fee,' `**fees**,' or `litigation costs,' and usually refer to a `prevailing party' in the context of an `adversarial action.'" Id. at 2164.

Applying this two-part test, the Supreme Court ruled that Congress did not depart from the American Rule in section 330(a) of the Bankruptcy Code. Id. Rather, that section only allows a court to award "reasonable compensation for actual, necessary services rendered." Id. at 2165. The Supreme Court found that that phrase "neither specifically nor explicitly authorizes courts to shift the costs of adversarial litigation from one side to the other — in this case, from the **attorneys** seeking **fees** to the administrator of the estate — as most statutes that displace the American Rule do." Id. As a result, the Court held that the **fees** incurred in defending the firm's fee application were not compensable from the estate. Id. at 2169.

The UST argues that ASARCO is binding precedent which mandates that the Court deny the fee defense provisions in Committee Counsel's retention applications.

The Committee responds that ASARCO does not prohibit the fee defense provisions because in that case the Supreme Court found only that section 330(a) of the Bankruptcy Code did not contain an express statutory exception to the American Rule. Id. at 2164. In this case, the Committee is seeking approval of the fee defense provisions under section 328(a) not section 330. Therefore, the Committee argues that ASARCO is not applicable binding precedent.

The UST disagrees, contending that the Committee's professionals — though retained under section 328 — can only be compensated under section 330. Therefore, the UST argues that ASARCO is directly on point: section 330 is not a statutory exception to the American Rule that **attorneys' fees** for defending a fee application cannot be paid by the estate.

The Committee acknowledges that its professionals get paid under section 330 but note that section 328 is an express exception to section 330[3] and that section 328 allows compensation to professionals (if approved in advance by the court) that would otherwise not be available under section 330 (such as fixed **fees**, contingent **fees**, etc.). The Committee, therefore, contends that the Court has the authority under section 328 to approve the fee defense provisions.

The Court concludes that although section 328 is an exception to section 330, it, like section 330, is not a "specific and explicit" statute which "authorize[s] the award of `a reasonable attorney's fee,' `**fees**,' or `litigation costs,'" that "refer[s] to a `prevailing party' in the context of an `adversarial action.'" ASARCO, 135 S. Ct. at 2164. Section 328 merely provides that, with court approval, a professional may be employed "on any reasonable terms and conditions of employment, including on a retainer, on an hourly basis, on a fixed or percentage fee basis, or on a contingent fee basis." 11 U.S.C. § 328(a). The text does not refer to the award of defense **fees** to a prevailing party. Therefore, the Court concludes that section 328 does not provide a statutory exception to the American Rule and cannot provide authority for approval of the fee defense provisions.

The Court finds it significant that Congress did provide in several sections of the Bankruptcy Code the express language necessary to create an exception to the American Rule. See, e.g., 11 U.S.C. § 110(i)(1)(C) (providing that court shall order a petition preparer to pay reasonable **attorneys' fees** and costs to the debtor if the petition preparer violates that section); 11 U.S.C. § 303(i)(1)(B) (providing that court may order unsuccessful involuntary petition filers to pay reasonable **attorneys's fees** to the alleged debtor); 11 U.S.C. § 362(k)(1) (providing that court may order creditor who violates the automatic stay to pay debtor actual damages, including costs and **attorneys' fees**); 11 U.S.C. § 526(c)(2) (providing that a debt relief agency which violates the statute shall be liable for reasonable **attorneys' fees** and costs); 11 U.S.C. § 707(b)(4)(A) (providing that the court may order that the trustee's **attorneys' fees** and costs for successful prosecution of a motion to dismiss be paid by an attorney who files a petition in violation of Rule 11); 11 U.S.C. § 707(b)(5)(A) (authorizing the award of costs and **attorneys' fees** to a debtor who successfully defeats a motion to dismiss filed

by a party in interest other than the trustee or UST).

Neither section 330 nor section 328 contain similar express language awarding **attorneys' fees** for successful prosecution of a defense to a fee objection. Therefore, the Court concludes that section 328, like section 330, does not provide an exception to the American Rule and cannot support the fee defense provisions at issue under the Supreme Court's ruling in ASARCO.

B. Contract Exception to the American Rule

The Committee argues that the Supreme Court in ASARCO did not rule that section 330 (or any other provision of the Bankruptcy Code) prohibited the allowance of defense **fees**. Rather, the Supreme Court merely held that section 330 did not contain a specific or explicit exception to the American Rule authorizing their payment. ASARCO, 135 S. Ct. at 2169 ("Section 330(a)(1) itself does not authorize the award of **fees** for defending a fee application, and that is the end of the matter."). The Committee further argues that the Supreme Court in ASARCO acknowledged that, in addition to a statutory exception to the American Rule, there could be an exception by contract. ASARCO, 135 S. Ct. at 2164 ("Each litigant pays his own attorney's **fees**, win or lose, unless a statute or contract provides otherwise.") (emphasis added) (citing Hardt v. Reliance Std. Life Ins. Co., 560 U.S. 242, 252-53 (2010)).

The UST responds that the parties' consent cannot override the statute. It argues that if the ASARCO prohibition on allowance of defense **fees** could be overridden by consent, other Code provisions relating to compensation could as well — including prohibitions on compensation for unnecessary or duplicative services or fee-splitting. 11 U.S.C. §§ 330(a)4) & 504.

The Court agrees with the Committee that the Supreme Court in ASARCO did not hold that section 330 prohibits the allowance of defense **fees** and merely held that it did not expressly authorize them. The application of that holding to section 328 is the same: that section does not prohibit defense **fees**, it simply does not expressly authorize them. Therefore, the Court agrees with the Committee's argument that the contract exception to the American Rule is not precluded by the ruling in ASARCO. The Court nonetheless agrees with the UST's assertion that the parties cannot, by contract, violate another provision of the Code. Therefore, although the Committee is correct that the ASARCO Court did acknowledge a contractual exception to the American Rule, any such contract has to be consistent with the other provisions of the Bankruptcy Code.

1. Are the retention agreements contracts?

The Committee contends that the retention agreements with Committee Counsel are contracts. See, e.g., In re ASARCO, LLC, 702 F.3d 250, 268 (5th Cir. 2012) ("In disputes governed by § 328(a), the contractual arrangement is supreme, and we shall enforce the contract as written.") (emphasis added); In re Nat'l Gypsum Co., 123 F.3d 861, 863 (5th Cir. 1997) ("Courts must protect [§ 328(a)] agreements and expectations, once found to be acceptable.") (emphasis added); U.S. Trustee v. Newmark Retail Fin. Advisors LLC (In re Joan & David Helpern, Inc.), No. 00 CIV. 3601 (JSM), 2000 WL 1800690, at *1 (S.D.N.Y. Dec. 6, 2000) (affirming bankruptcy court approval of indemnification provision in financial advisor's professional services contract under section 328(a) because they are not per se unreasonable); In re Merced Falls Ranch, LLC, Bankr. No. 2012 WL 8255520, at *4 (Bankr. E.D. Cal. Oct. 16, 2012) ("Once § 328(a) is invoked, the bankruptcy court has limited discretion to vary the contractual terms of that employment.") (emphasis added). But see In re United Artists Theatre Co., 315 F.3d 217, 234 (3d Cir. 2003) (approving indemnification agreement of financial advisor with modifications eliminating indemnification for gross negligence or breach of contract).

The UST argues that the contract exception is not available because professionals' employment and compensation rights in bankruptcy are not bestowed by "contract." Instead, they are created by statute. Under the Bankruptcy Code, any employment agreement must be filed with and approved by the Court. 11 U.S.C. §§ 327, 328 & 1103. Regardless of how it is named, the UST contends that a professional's retention application is a request of a judge, acting within the constraints of the Bankruptcy Code, to approve their terms of employment. The order so approving the employment is a

Court Order not a contract between two parties. Cf. Restatement (Second) of Contracts 9 (1981) (defining a contract as an agreement between two parties, a promisor and a promisee). Further, the UST notes that the scope of the permissible terms of employment is governed by the Bankruptcy Code, not the parties' agreement. See, e.g., In re Fed. Mogul-Global, Inc., 348 F.3d 390, 397-98 (3d Cir. 2003) (holding that bankruptcy court could approve professional's employment on terms and conditions different from those proposed by the committee that the court found were necessary to satisfy the requirement of reasonableness under section 328(a)).

The Court agrees with the Committee that the retention agreement is a contract. However, it is not a bi-lateral one; rather, it is subject to objection by other parties and is ultimately subject to approval (and modification) by the Court. See, e.g., Fed. Mogul-Global, 348 F.3d at 397-98; United Artists, 315 F.3d at 234.

2. Is the contract an exception to the American Rule?

It is not enough, however, that the retention agreements be contracts, however. They must be contractual exceptions to the American Rule. The UST argues that they are not exceptions to the American Rule because they are not agreements by two parties that in the event of litigation between them, the loser will pay the winner's legal costs. In this case, the UST notes that the agreement is a one-way street: Committee Counsel seeks a ruling that the estate is liable for their legal **fees** but make no similar commitment to the estate. The UST argues that the Committee cannot by contract require a third party (the estate) to pay their legal **fees** in the event of litigation by someone else. See, e.g., Motorsport Eng'g, Inc. v. Maserati SPA, 316 F.3d 26, 29 (1st Cir. 2002) (holding that a third party — even if it is a beneficiary of a contract — cannot be bound by a contract it did not sign or otherwise assent to); Abraham Zion Corp. v. Lebow, 761 F.2d 93, 103 (2d Cir. 1985) (same).

The Court agrees with the UST that the retention agreements in this case are not contractual exceptions to the American Rule. Here, there is not a contract between two parties providing that each will be responsible for the other's legal **fees** if it loses a dispute between them. Rather, here there is a contract between two parties (the Committee and Committee Counsel) that in the event Committee Counsel win a challenge to their **fees**, a third party (the estate) will pay their defense costs even if the estate is not the party who objected. As the UST notes, this is not the typical contract modifying the American Rule.

Nor can this contract bind the estate, which is not a party to it. Motorsport Eng'g, 316 F.3d at 29; Abraham Zion Corp., 761 F.2d at 103. The fact that it was negotiated between sophisticated parties (the Committee and Committee Counsel) is beside the point; it seeks to bind a non-party to that agreement.

Finally, it is clear that retention agreements in bankruptcy are not simply contractual matters. It is the obligation of the Bankruptcy Court to approve the terms of employment of professionals, in accordance with the provisions of the Bankruptcy Code, regardless of the terms articulated in the employment contract. Therefore, if the Court finds that a contract that the Debtor or the Committee negotiated is impermissible, the Court may not approve it or may modify it. See, e.g., Fed. Mogul-Global, 348 F.3d at 397-98 (holding that bankruptcy court could approve professional's employment on terms and conditions different from those proposed by the committee that the court found were necessary to satisfy the requirement of reasonableness under section 328(a)); United Artists, 315 F.3d at 234 (affirming approval of indemnification agreement in financial advisors' retention application but with two modifications required by the Court).

Therefore, the Court concludes that the retention agreements are not contractual exceptions to the American Rule. Even if they were, however, the Court must still determine if they are permissible under the Bankruptcy Code.

C. Scope of Section 328(a)

The UST argues that even if ASARCO did not directly preclude approval of the fee defense provisions, they cannot be approved under section 328 because they do not fit the scope of that section. It argues that the provisions are not

"reasonable terms and conditions of employment" of a committee professional employed under section 1103. 11 U.S.C. § 328(a). The UST contends that all such terms of employment must actually relate to the services to be rendered by the professionals, i.e., the representation of the Committee and its interests. It argues that defending their own **fees** is not a service performed by Committee Counsel for the Committee but instead are services they are performing only for themselves. ASARCO, 135 S. Ct. at 2165 ("The term `services' ordinarily refers to `labor performed for another.' . . . Time spent litigating a fee application against the administrator of a bankruptcy estate cannot be fairly described as `labor performed for' — let alone `disinterested service to' — that administrator.").

The Court agrees with the UST. The fee defense provisions are not reasonable terms for the employment of Committee Counsel because they do not involve any services for the Committee. Rather, they are for services performed by Committee Counsel only for their own interests.

The Committee argues nonetheless that "[c]ourts generally hold that exculpation and indemnification clauses are permissible in retention agreements if the clauses are reasonable in accordance with 11 U.S.C. § 328(a)." In re Firstline Corp., No. 06-70145, 2007 WL 269086, at *2 (Bankr. M.D. Ga. Jan. 25, 2007) (citing United Artists, 315 F.3d at 230). See also, In re DEC Int'l, Inc., 282 B.R. 423, 424 (W.D. Wis. 2002) (rejecting UST's argument that indemnification provisions are per se invalid as against public policy); In re Potter, 377 B.R. 305, 308 (Bankr. D.N.M. 2007) (approving provision allowing **fees** for defending **fees** from objection by third party because similar provision had been approved in another attorney's retention application); In re Joan & David Halpern, Inc., 248 B.R. 43, 47 (Bankr. S.D.N.Y. 2000) (allowing provision as reasonable in that case because state trust and corporate law allows indemnification of fiduciaries).

There are, of course, cases which disagree with this general proposition. See, e.g., In re Drexel Burnham Lambert Group, Inc., 133 B.R. 13, 27 (Bankr. S.D.N.Y. 1991) (stating that indemnification provisions for investment bankers are inappropriate); In re Mortgage & Realty Trust, 123 B.R. 626, 630-31 (Bankr. C.D. Cal. 1991) (disallowing any indemnity provision as inconsistent with professionalism); In re Allegheny Int'l, Inc., 100 B.R. 244, 247 (Bankr. W.D. Pa. 1989) (disallowing indemnification for ordinary negligence in financial advisor's retention because "holding a fiduciary harmless for ordinary negligence is shockingly inconsistent with the strict standard of conduct for fiduciaries.").

The Third Circuit, however, has held that indemnification provisions sought by professionals may be approved as reasonable under section 328(a), but with limits. United Artists, 315 F.3d at 230 ("Our approach is `market driven,' not `market-determined,' especially in the realm of bankruptcy, where courts play a special supervisory role. With the understanding and limitations set out below, we believe [the financial advisor's] indemnification agreement to be reasonable and therefore permissible under § 328.").

That case though predated the ASARCO decision and did not address whether section 328(a) is an explicit statutory exception, or whether a retention agreement approved under that section is a contractual exception, to the American Rule. In addition, it dealt with indemnification of financial advisors, which were typically provided similar protections outside bankruptcy. Id. at 229.

In this case, the Court asked the parties to provide evidence that similar indemnification provisions are normally provided to counsel in non-bankruptcy contexts. (Tr. 8/11/2015 at 21:1-24, 48:15-24.) In its Supplemental Brief, the Committee again cited to numerous bankruptcy cases where indemnification provisions and **fees** for successfully defending **fees** have been approved. (D.I. 393 at 3-5.) The Committee also noted that the UST guidelines permit award of such **fees** if it is judicially allowed in the district.

The citation to the UST guidelines is not compelling. The UST guidelines generally state that the UST will object to requests for **fees** defending fee applications.[4]

The cases cited by the Committee are not persuasive because they all predate ASARCO and most involve cases granting **fees** in bankruptcy cases for defending fee applications with little analysis of why such services benefitted the estate or counsel's client.[5] (D.I. 393 at 3-5.)

The Committee argues nonetheless that fee defense provisions are common in the non-bankruptcy market and are,

therefore, reasonable terms of compensation under section 328. Though that is not dispositive, the Third Circuit found that "some reference to the market is not out of place when considering whether terms of retention are `reasonable' in the bankruptcy context." United Artists, 315 F.3d at 229 (citing In re Busy Beaver Bldg. Ctrs., Inc., 19 F.3d 833, 852 (3d Cir. 1994)). In support of its market argument, the Committee cites decisions in eleven states, including Delaware, where courts or state bar disciplinary authorities have held that similar indemnification provisions are permissible and do not run afoul of the Model Rules of Professional Conduct. (D.I. 393 at 8-9.)

The UST responds that this market-driven approach was expressly rejected by the Supreme Court in ASARCO and is no longer valid:

> [W]e find this policy argument [to follow the market approach, made by the UST] unconvincing. In our legal system, no **attorneys**, regardless of whether they practice in bankruptcy, are entitled to receive **fees** for fee-defense litigation absent express statutory authorization. Requiring bankruptcy **attorneys** to pay for the defense of their **fees** thus will not result in any disparity between bankruptcy and nonbankruptcy lawyers.

ASARCO, 135 S. Ct. at 2168. Therefore, the UST contends that this Court is bound to follow the Supreme Court's holding on this point (even if it is dicta) and may not rely on a market-determined approach as a basis for allowing Committee Counsel to get fee defense costs and **fees**. See, e.g., Cuevas v. U.S., 778 F.3d 267, 272-73 (1st Cir. 2015) ("federal appellate courts are bound by the Supreme Court's considered dicta almost as firmly as by the Court's outright holdings, particularly when, as here, a dictum is of recent vintage and not enfeebled by any subsequent statement.") (quoting McCoy v. Mass. Inst. of Tech., 950 F.2d 13, 19 (1st Cir. 1991). Accord In re McDonald, 205 F.3d 606, 612-13 (3d Cir. 2000) ("But even if the discussion of § 506(a) could be accurately characterized as dictum — and we think it cannot be — we should not idly ignore considered statements the Supreme Court makes in dicta. The Supreme Court uses dicta to help control and influence the many issues it cannot decide because of its limited docket.").

The Committee counters that the ASARCO decision dealt with section 330 and that the market approach is a valid test of reasonableness under section 328. United Artists, 315 F.3d at 230.

The UST responds that in determining reasonableness under section 328, the Third Circuit has stated that courts should consider the same factors as those under section 330. See, e.g., Fed. Mogul-Global, 348 F.3d at 407-08 ("It is well established that `[i]dentical words used in different parts of the same act are intended to have the same meaning.' . . . Though we need not decide whether Congress intended to limit Bankruptcy Courts to considering only the Section 330(a)(1) factors when determining the reasonableness of a requested fee structure under Section 328(a), we believe that the Section 330(a)(1) factors may be taken into account in asking whether a fee request is reasonable.") (citations omitted). Therefore, the UST contends that the Supreme Court's ruling in ASARCO precludes the Court's consideration of the market in determining the reasonableness of the indemnification agreements.

The Court agrees with the UST. The cases that considered market factors relevant to the question of whether defense **fees** can be recovered all pre-dated the ASARCO decision which expressly rejected the consideration of such factors in determining that issue. Therefore, the Court concludes that ASARCO prevents the Court from concluding that section 328 permits defense **fees** even if they were routinely allowed by the market in bankruptcy or non-bankruptcy contexts prior to that ruling.

D. Expenses under Section 328(a)

The Committee also argues that, even though section 328(a) does not contain an express exception to the American Rule, it nonetheless permits the approval of the fee defense provision as reasonable expenses of serving as counsel for the Committee. It cites cases allowing as expenses, **attorneys' fees** incurred by estate professionals for both retention and defense of **fees** under section 328(a) as reasonable. See, e.g., In re Borders Grp., Inc., 456 B. R. 195, 213 (Bankr. S.D.N.Y. 2011) ("Retained professionals that retain outside counsel only to represent the professional in connection with retention or preparation of fee applications may be reimbursed for reasonable expenses of such counsel when the

engagement agreement and retention order provide for such expense reimbursement."); Geneva Steel Co., 258 B.R. 799, 803 (Bankr. D. Utah 2001) (holding that the reimbursement of reasonable **fees** and expenses incurred by advisor's law firm is allowable because the advisor's retention agreement required the debtor to indemnify the advisor for all reasonable expenses including **fees**, expenses, and disbursements of counsel). The Committee argues that this case is distinguishable from ASARCO because in that case there was not an agreement in advance under section 328(a) to pay the expenses associated with defense of counsel's **fees**.

The Court finds this argument unavailing. Again, the cases all pre-date ASARCO. Further, there is no difference in the analysis between approving the defense costs as **fees** (because the retained professional defends its own **fees**) or as expenses (because the retained professional hires outside counsel to represent it). Both are subject to the American Rule and to the Supreme Court's ruling in ASARCO. (The Supreme Court in ASARCO dealt with section 330(a)(1) which governs both **fees** and expenses.) Nor is there any suggestion in ASARCO that the Court's ruling would have been different if there had been an agreement in advance under section 328(a).

Further, as noted above, section 328(a) permits only approval of **fees** or expenses for performing services for the Committee. In this case, the expenses sought would be for services performed for the professionals, not for the Committee. Therefore, the Court concludes that the fee defense provision is not a reasonable term of employment for serving as Committee Counsel.

IV. CONCLUSION

For all the foregoing reasons, the Court will deny the request for approval of the fee defense provision in the retention applications of Committee Counsel.[6]

An appropriate Order is attached.

[1] This Opinion constitutes the findings of fact and conclusions of law of the Court pursuant to Rule 7052 of the Federal Rules of Bankruptcy Procedure, which is made applicable to contested matters by Rule 9014 of the Federal Rules of Bankruptcy Procedure.

[2] The retention applications have been approved without the fee defense provision, pending ruling by the Court on the UST's objection to that provision.

[3] Section 330 provides that "subject to sections . . . 328. . ., the court may award to [professionals] . . . reasonable compensation for actual, necessary services rendered by the [professional]." 11 U.S.C. § 330(a).

[4] Section B(2)(g) of Appendix B — Guidelines for Reviewing Applications for Compensation and Reimbursement of Expenses Filed under 11 U.S.C. § 330 for **Attorneys** in Larger Chapter 11 Cases provides:

Contesting or litigating fee objections. Whether the fee application seeks compensation for time spent explaining or defending monthly invoices or fee applications that would normally not be compensable outside of bankruptcy. Most are not compensable because professionals typically do not charge clients for time spent explaining or defending a bill. The USTP's position is that awarding compensation for matters related to a fee application after its initial preparation is generally inappropriate, unless those activities fall within a judicial exception applicable within the district (such as litigating an objection to the application where the applicant substantially prevails). Thus, the United States Trustee may object to time spent explaining the **fees**, negotiating objections, and litigating contested fee matters that are properly characterized as work that is for the benefit of the professional and not the estate.

(emphasis added).

[5] The Committee also cites two bare orders. The Court does not consider bare orders persuasive authority, because it is usually not clear from the order whether the court considered the issue or what its reasoning was if it did.

[6] The Court would reach the same conclusion if the fee defense provisions were in a retention agreement filed by any professional under section 328(a) — including one retained by the debtor. Such provisions are not statutory or contractual exceptions to the American Rule and are not reasonable terms of employment of professionals.

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	Chapter 11 Case No. 15-11247 (MFW) Jointly Administered
BOOMERANG TUBE, LLC, a Delaware limited liability company, *et al.*,	:	Re: D.I. 271 & 272
Debtors.	:	**Hearing Date: August 11, 2015 at 2:00 p.m. (prevailing Eastern Time)**
		Objection Deadline: August 3, 2015 at 4:00 p.m. (prevailing Eastern Time)

OBJECTION OF THE UNITED STATES TRUSTEE TO APPLICATION FOR ORDER AUTHORIZING THE RETENTION OF BROWN RUDNICK LLP AS CO-COUNSEL FOR THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF BOOMERANG TUBE, LLC, *NUNC PRO TUNC* TO JUNE 19, 2015

Andrew R. Vara, the Acting United States Trustee for Region 3 (the "U.S. Trustee"), pursuant to 11 U.S.C. §§ 327-331 and Federal Rule of Bankruptcy Procedure 2014,[1] hereby objects to the *Application for Order Authorizing the Retention of Brown Rudnick LLP as Co-Counsel for the Official Committee of Unsecured Creditors of Boomerang Tube, LLC,* Nunc Pro Tunc *to June 19, 2015*, (the "Retention Application") filed by the Official Committee of Unsecured Creditors of Boomerang Tube, LLC (the "Committee"), and in support of his objection respectfully states as follows:

I. SUMMARY OF ARGUMENT

1. Brown Rudnick LLP (the "Firm") seeks to be paid "from the Debtors' estates, subject to approval by the Court pursuant to 11 U.S.C. §§ 330 and 331, for any fees,

[1] Unless otherwise indicated, all chapter, section, rule, and local bankruptcy rule references are to the Bankruptcy Code (the "Code"), 11 U.S.C. §§ 101-1532, the Federal Rules of Bankruptcy Procedure (the "Rules"), Rules 1001-9037, and to the Local Rules of Bankruptcy Practice and Procedure of the United States Bankruptcy Court for the District of Delaware.

costs or expenses, arising out of the successful defense of any fee application by Brown Rudnick in these bankruptcy cases in response to any objection to its fees or expenses" (the "Fee Defense Provisions"). Retention Application, ¶ 16.

2. The Fee Defense Provisions violate the Code, ignore the express directives of the United States Supreme Court, and are otherwise unreasonable. The Supreme Court recently held that section 330(a) does not authorize a court to approve a law firm's fee for litigating its fee application. *Baker Botts LLP v. ASARCO LLC*, ___ U.S. ___, 135 S. Ct. 2158 (2015). For five separate and independent reasons,[2] the Firm cannot circumvent *ASARCO* by having the same fees approved as a term or condition of its employment under section 328(a). Unless the Fee Defense Provisions are removed or stricken, the Court should deny the Retention Application.

II. JURISDICTION

3. Pursuant to 28 U.S.C. § 1334, applicable order(s) of the United States District Court for the District of Delaware issued pursuant to 28 U.S.C. § 157(a), and 28 U.S.C. § 157(b)(2)(A), this Court has jurisdiction to hear and resolve this objection.

4. Pursuant to 28 U.S.C. § 586, the U.S. Trustee is charged with monitoring the federal bankruptcy system. *See United States Trustee v. Columbia Gas Sys., Inc. (In re Columbia Gas Sys., Inc.)*, 33 F.3d 294, 295-96 (3d Cir. 1994) (noting that 11 U.S.C. § 307 gives

[2] Although the Fee Defense Provisions expressly reference sections 330 and 331 only, Paragraph 14 of the Retention Application suggests that the Firm seeks pre-approval of the Fee Defense Provisions pursuant to section 328(a). *See* Retention Application, ¶ 14. The proposed form of order accompanying the Retention Application also relies on section 328(a): "Brown Rudnick shall be indemnified and be entitled to payment . . . pursuant to section 328(a) of the Bankruptcy Code."

the U.S. Trustee "public interest standing"); *Morgenstern v. Revco D.S., Inc. (In re Revco D.S., Inc.)*, 898 F.2d 498, 500 (6th Cir. 1990) (describing the U.S. Trustee as a "watchdog").

5. The U.S. Trustee has standing to be heard on the Retention Application pursuant to 11 U.S.C. § 307.

III. BACKGROUND

6. On June 9, 2015, the above-captioned debtors (the "Debtors") filed chapter 11 petitions in this Court.

7. On June 19, 2015, the U.S. Trustee appointed the Committee.

8. On July 20, 2015, the Committee filed the Retention Application.

9. The proposed form of order accompanying the Brown Rudnick Application provides in part:

> Brown Rudnick shall be indemnified and be entitled to payment from the Debtors' estates, for any fees or costs arising out of the successful defense of any fee application by Brown Rudnick in response to any objection to its fees or expenses in these cases pursuant to section 328(a) of the Bankruptcy Code[.]

(emphasis added).

IV. ARGUMENT

A. Section 328(a) Creates No Exception to the "American Rule's" General Prohibition Against Shifting Fees.

10. In *ASARCO*, the Court stated that the "basic point of reference when considering the award of attorney's fees is the bedrock principle known as the American Rule: Each litigant pays his own attorney's fees, win or lose, unless a statute or contract provides otherwise." *ASARCO*, 135 S. Ct. 2158, 2164 (2015) (quoting *Hardt v. Reliance Standard Life*

Ins. Co., 560 U.S. 242, 252–253 (2010)). Although statutory provisions overruling the American Rule "take various forms," any statutory departures from the American Rule must be contained in "specific and explicit provisions." *ASARCO*, 135 S. Ct. at 2164. The Court further ruled that a fee-shifting statute typically must both (1) "authorize the award of 'a reasonable attorney's fee,' 'fees,' or 'litigation costs,' and [(2)] usually refer to a 'prevailing party' in the context of an adversarial 'action.'" *Id.*

11. Applying this two-part test, the Court ruled that Congress did not depart from the American Rule in section 330(a). *Id.* Rather, the statute allows a court to award only "reasonable compensation for actual, necessary services rendered." *Id.* at 2165. The Court reasoned that section 330(a) authorizes a court to award fees for work done to assist the estate in the bankruptcy case, but it does not specifically or explicitly award fees to a "'prevailing party' in the context of an adversarial 'action.'" *Id.* at 2164. Relying on the bedrock principle of the American Rule, the Court held that 11 U.S.C. "§ 330(a)(1) [does not] permit[] a bankruptcy court to award attorneys' fees for work performed in defending a fee application." *Id.* at 2164.

12. For the same reasons articulated by the Court in *ASARCO*, the Fee Defense Provisions cannot be approved here. Section 328(a), like section 330(a), does not overcome the American Rule's presumption that each party will pay its own fees for fee defense litigation. Section 328(a) provides that, with the court's approval, a professional may be employed "on any reasonable terms and conditions of employment, including on a retainer, on an hourly basis, on a fixed or percentage fee basis, or on a contingent fee basis." This text does not "specifically" or "explicitly" allow a "prevailing party" to recover its fees from the other party in an "adversarial action," *see id.* at 2164-65, and, therefore, it too fails to satisfy the second prong

of the *ASARCO* test. Because section 328(a) does not expressly vary the American Rule against fee shifting, the Fee Defense Provisions cannot be approved.

13. In *ASARCO*, the Court also found it significant that certain Code provisions, unlike sections 328(a) and 330(a), *do* explicitly shift a prevailing party's fees to the other side. *ASARCO*, 135 S. Ct. at 2164 (citing as an example 28 U.S.C. § 2412(d)(1)(A)). Those include:

- **11 U.S.C. § 110(i)(1)(C)** (providing that "the court shall order the bankruptcy petition preparer to pay to the debtor . . . reasonable attorneys' fees and costs");
- **11 U.S.C. § 303(i)(1)(B)** (providing that unsuccessful involuntary petitioners may be ordered to pay "a reasonable attorney's fee" to the alleged debtor);
- **11 U.S.C. § 362(k)(1)** (providing that "an individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees . . ." from the violating creditor);
- **11 U.S.C. § 526(c)(2)** (providing that a debt relief agency shall be liable to an assisted person "for reasonable attorneys' fees and costs" if it is found liable under the statute);
- **11 U.S.C. § 707(b)(4)(A)** (providing that a trustee who successfully prosecutes a motion to dismiss may recover from the debtor's attorney who filed the petition "all reasonable costs in prosecuting [the] motion . . . including reasonable attorneys' fees" when specific criteria are met); and
- **11 U.S.C. § 707(b)(5)(A)** (providing that a court "may award" to certain debtors, who defeat a motion to dismiss, "all reasonable costs (including reasonable attorneys' fees").

These Code fee-shifting provisions confirm that Congress did not draft either section 328(a) or section 330(a) in a way that shifts a prevailing party's fees to the loser.[3] Section 328(a), just like section 330(a), stands in stark contrast to the Code provisions that expressly require a losing party to pay the prevailing party's litigation costs, including their attorneys' fees. Congress

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[3] None of these provisions shift the fee burden from the prevailing party *to the estate*.

knows how to shift litigation fees in bankruptcy when it wants them shifted, and it did not shift them under section 328(a). The Fee Defense Provisions, therefore, cannot be approved.

B. The Fee Defense Provisions Cannot be Approved Under Section 328(a) Because They Seek To Pay Professionals for Work Not Within the Scope of their Employment.

14. Even if the American Rule against fee shifting did not preclude approval of the Fee Defense Provisions, those provisions cannot be authorized because they fall outside the scope of section 328(a), the statutory provision on which the Retention Application ostensibly relies. Section 328(a) only authorizes courts to approve "reasonable terms and conditions of *employment . . . under section 327 or 1103 of this title.*" 11 U.S.C. § 328(a) (emphasis added). Nothing in the text of section 328(a) provides courts with authority to pay a professional from the estate for work outside the scope of the professional's employment under either section 327 or 1103.[4] For this reason, any "terms and conditions" approved under section 328(a) must relate only to activities that a professional could be retained to perform under sections 327 or 1103. *Id.* After *ASARCO*, those activities cannot include the professional's defense of its own fee application.

15. For committee professionals, the relevant retention provision of the Code is section 1103(a), which authorizes "*employment* by such committee of one or more attorneys, accountants, or other agents, to represent or perform services for such committee."[5] 11 U.S.C. § 1103(a) (emphasis added). "Employ" means "to engage the *services* of." The American

[4] "Congress has not granted us 'roving authority . . . to allow counsel fees . . . whenever [we] might deem them warranted.' [internal citation omitted]. Our job is to follow the text . . . ." *ASARCO*, 135 S. Ct. at 2169 (quoting *Aleyeska Pipeline Serv. Co. v. Wildnerness Soc'y*, 421 U.S. 240, 260 (1975)).

[5] Similarly, section 327 is entitled "employment of professional persons" and likewise authorizes the trustee to "employ" professionals "to represent or assist the trustee" or debtor-in-possession "in carrying out the trustee's duties." 11 U.S.C. § 327(a).

Heritage Dictionary 450 (def. 3.a.) (2d ed. 1982) (emphasis added). Black's Law Dictionary defines "employ" as "[t]o engage in one's *service*." Black's Law Dictionary 471 (5th ed. 1979) (emphasis added). Black's Law Dictionary similarly defines "employer" as "[o]ne who employs the *services* of others." *Id.* (emphasis added).

16. In *ASARCO*, the Supreme Court held that the litigation efforts of a professional employed by the estate in defense of its own fees are not services under section 330 and, therefore, not compensable. *See ASARCO*, 135 S. Ct. at 2165 (internal citations omitted). That same analysis precludes paying for fee defense litigation under a section 328(a) term or condition. Employment by a client necessarily entails the professional providing services to the client. *See* RESTATEMENT (SECOND) OF AGENCY 228(1) (1957) (for an action to be within the scope of "employment" it must be "actuated, at least in part, by a purpose *to serve* the master") (emphasis added). A professional defending an objection to its fee application is not serving the client's interest but instead acts for its own benefit and own interests. *ASARCO* compels the conclusion that a professional does not provide a client "service" when defending an objection to its fee application, and by extension, that doing so is not a term of the professional's "employment" under section 1103. Because fees for fee defense are therefore outside the scope of the professional's employment by its client, the Fee Defense Provisions are also outside the scope of what may be authorized under section 328(a).[6]

17. This conclusion is consistent with the structure of section 328(a). In general, section 328(a) addresses the question of *how* the professional is to be paid, but not the type of services *for which* the professional may be paid. Section 328(a)'s examples all involve forms of payment, and a term authorizing fees for fee defense is not a form of payment. Section

[6] Should there be any doubt, section 1103 also provides that a committee professional performs "services" for the committee. That same term also appears in section 330(a), the subject of the *ASARCO* decision.

328(a) includes four examples of "reasonable terms and conditions of employment . . . [:1] a retainer, [2] on an hourly basis, [3] on a fixed or percentage fee basis, or [4] on a contingent fee basis." 11 U.S.C. § 328(a). Each addresses how a professional will be compensated for the work that it does. None addresses the *type* of work for which a professional may be compensated. Rather, the type or scope of work is governed by either section 1103 (represent or perform services for committees) or section 327 (represent or assist trustees or debtors-in-possession).

18. Statutory terms, arguably ambiguous when considered alone, should be given related meaning when grouped together. Under the doctrine of *noscitur a sociis*, the meaning of an ambiguous statutory term may be derived from the meaning of accompanying terms. *In re Cont'l Airlines, Inc.*, 932 F.2d 282, 288 (3d Cir. 1991). It follows that the "terms and conditions" that can be approved under section 328(a) should be limited to those addressing the forms of compensation and similar matters, like hourly vs. contingent fees, not the scope of substantive work for which the professional may be compensated, like fee defense litigation. As a result, section 328(a) does not authorize the Court to approve the Fee Defense Provisions.

C. The Fee Defense Provisions Cannot be Approved under Section 328(a) Because They Are Not Reasonable.

19. Not only must section 328(a) terms relate to the scope of employment, they must also be reasonable. Section 328(a) permits courts to approve "any reasonable terms and conditions of employment." 11 U.S.C. § 328(a). A term allowing fees for fee defense is not "reasonable" for two reasons.

20. First, courts should and do consider section 330(a) factors when determining whether a proposed term and condition of employment is reasonable under section 328(a). *In re Federal Mogul-Global, Inc.*, 348 F.3d 390, 407-08 (3d Cir. 2003) (Alito, J.). In

Federal Mogul, Judge, now Justice, Alito writing for the Third Circuit ruled that section 330(a)(1) factors could be considered when determining the reasonableness of a fee structure sought to be approved under section 328(a):

> Section 328(a), as noted above, authorizes the retention of a professional "on any *reasonable* terms and conditions of employment." 11 U.S.C. § 328(a) (emphasis added). Section 330(a)(1) authorizes a Bankruptcy Court to award a professional "reasonable compensation for actual, necessary services rendered," and then lists several criteria to be used in determining the reasonableness of the fees sought. 11 U.S.C. § 330(a)(1). It is well established that "[i]dentical words used in different parts of the same act are intended to have the same meaning." *Barnhart v. Walton*, 535 U.S. 212, 221, 122 S.Ct. 1265, 152 L.Ed.2d 330 (2002) (*quoting Dept. of Revenue of Ore. v. ACF Indus., Inc.*, 510 U.S. 332, 342, 114 S.Ct. 843, 127 L.Ed.2d 165 (1994)). **Though we need not decide whether Congress intended to limit Bankruptcy Courts to considering only the Section 330(a)(1) factors when determining the reasonableness of a requested fee structure under Section 328(a), we believe that the Section 330(a)(1) factors may be taken into account in asking whether a fee request is reasonable.** The District Court therefore did not err in considering the Section 330(a)(1) factors when evaluating the reasonableness . . . of the terms and conditions of employment proposed by the Equity Committee.

Id. at 390, 407-08 (emphasis added). As explained by then Judge Alito, the plain statutory text of section 328(a) allows courts to consider the section 330(a)(1) factors when presented with section 328(a) terms. Although the Third Circuit did not rule that courts must consider the section 330(a)(1) factors when presented with section 328(a) terms, it conclusively stated that it was proper to do so. Based on the plain statutory text and *Federal Mogul*, a term or condition in a retention application providing for compensation that *ASARCO* held cannot legally be awarded under section 330(a)(1) should not be approved under section 328(a) as reasonable.

21. Second, section 1103(a)—the employment authorization provision at issue here—specifies that committee professionals are employed "to represent or perform services for such committee." 11 U.S.C. 1103(a).[7] The Supreme Court has definitively ruled that fee

[7] *Cf.* 11 U.S.C. § 327(a) (professionals are employed under that section "to represent or assist [the client] . . . in carrying out the . . . duties under this title").

defense litigation is not a client service. *ASARCO*, 135 S. Ct. at 2166 ("The term 'services' in this provision cannot be read to encompass adversarial fee-defense litigation"). Because the Fee Defense Provisions are not related to the work for which the professionals may be compensated—to represent or perform services for such committee—they are not reasonable and, therefore, cannot be approved under section 328(a). *See Hensley v. Eckerhart*, 461 U.S. 424, 435 (1983) (holding that a fee is not "reasonable" if it is "unrelated to [the] work" for which the attorney is being compensated.).

D. ASARCO Directly Bars The Fee Defense Provisions Because All Compensation Must Be Approved For Final Payment Under Section 330.

22. Professionals are employed under sections 327 or 1103, their terms of employment may be approved under section 328(a), and they are paid under section 330, subject to sections 326, 328, and 329. Sections 330 and 331 are the exclusive Code provisions authorizing payments to professionals. *In re Ferguson*, 445 B.R. 744, 751 (Bankr. N.D. Tex. 2011). "While section 330(a)(1) makes an award of compensation 'subject to sections 326, 328, and 329,' **sections 330 and 331 are the only provisions of the Code which authorize the payment of professionals**" employed under sections 327 or 1103. *Id.* (emphasis added). Indeed, the Committee itself correctly acknowledges that any compensation awarded for defense fees will be "subject to approval by the Court pursuant to 11 U.S.C. §§ 330 and 331." Retention Application, ¶ 16.

23. Any other interpretation of the interplay between sections 328(a) and 330(a) risks forfeiting a professional's claim for an administrative expense. Only a section 330 award gives professionals an administrative claim against estate assets under 11 U.S.C. §

503(b)(2).[8] *Ferguson,* 445 B.R. at 751 ("[S]ection 503(b)(2) is the only statutory basis for according that status to compensation awarded to persons employed under section 327 (and section 1103)."). *Cf. F/S Airlease II, Inc. v. Simon*, 844 F.2d 99, 108–09 (3d Cir. 1988), *cert. denied*, 488 U.S. 852 (1988) (professional who was not entitled to a section 330 award of compensation and, therefore, ineligible for an administrative expense under section 503(b)(2) may not receive an administrative expense under section 503(b)(1)(A)'s catchall);[9] *In re Garden Ridge Corp.*, 326 B.R. 278, 281 (Bankr. D. Del. 2005) ("[T]he Third Circuit [in *F/S Airlease*] unequivocally held that section 503(b)(1)(A) cannot be used to reimburse professionals for services rendered to the estate.").[10]

24. Because section 330(a)(1) is the exclusive provision authorizing the "award" of compensation to a retained professional, even those with pre-approved terms under section 328(a), *ASARCO* conclusively resolves the matter. Under *ASARCO*, bankruptcy courts may not award section 330(a)(1) fees for fee defense litigation. 135 S. Ct. at 2164. Section 328(a) does not independently authorize the award of these fees and, thus, the Fee Defense Provisions cannot be approved as "reasonable."

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[8] Section 503(b)(2) provides that: "After notice and a hearing, there shall be allowed administrative expenses . . . including compensation and reimbursement awarded under section 330(a) of this title." Section 507(a)(2) gives that professional's administrative claim second priority, trumping almost all other types of unsecured claims. 11 U.S.C. § 507(a)(2).

[9] *See also In re Milwaukee Engraving Co.*, 219 F.3d 635, 637 (7th Cir. 2000), *cert. denied*, 531 U.S. 1112 (2001); *In re Keren Ltd. P'ship*, 189 F.3d 86, 88 (2d Cir. 1999).

[10] Similarly, section 504's broad fee-sharing prohibition for retained professionals is made operative by reference to those "receiving compensation or reimbursement under section 503(b)(2)." 11 U.S.C. § 504. Section 503(b)(2) applies only to compensation awarded under section 330. If section 330 is not the exclusive authority for awarding compensation to retained professionals, then section 504's fee-sharing prohibition would be rendered meaningless.

E. The Parties Cannot "Consent" to Unauthorized Compensation.

25. The Fee Defense Provisions, even if the Committee and other parties agree to them, cannot override the statutory requirements discussed above. The Code, through sections 326-331 and 503, regulates both professional compensation and administrative expenses paid from the estate in a comprehensive way that parties are not free to rewrite. *See* 11 U.S.C. §§ 326-331, 503; *see also In re Lehman Bros. Holdings, Inc.*, 508 B.R. 283, 294 (S.D.N.Y. 2014) ("The Bankruptcy Code is meant to be a "comprehensive federal scheme . . . to govern" the bankruptcy process. Although flexibility is necessary[,] the federal scheme cannot remain comprehensive if interested parties and bankruptcy courts in each case are free to tweak the law to fit their preferences . . .") (citations omitted).

26. The Code's numerous limitations on professional compensation—including the limitation on defense fees recognized by *ASARCO*—would be undermined if they could be bypassed through consent. A professional could evade its burden to make the detailed showings required under sections 330 and 503 if payment depended on nothing more than client consent. *See Lehman*, 508 B.R. at 293 (noting the comprehensive nature of section 503(b) was inconsistent with allowing "backdoor" payments through plan provision). And if defense fees prohibited by *ASARCO* could be circumvented by consent, other Code provisions relating to compensation could similarly be evaded—including prohibitions on compensation for unnecessary or duplicative services, *see* 11 U.S.C. § 330(a)(4); on fee-splitting, *see* 11 U.S.C. § 504; and on compensation for unretained or non-disinterested professionals, *see* 11 U.S.C. §§ 328(c), 330(a)(1). Even if all creditors were to affirmatively consent to the Fee Defense

Provisions, there would be no basis for this Court to create a consent exception to ASARCO that contravenes the Code.[11]

III. CONCLUSION

For the reasons stated above, the Court should deny the Retention Application unless the Fee Defense Provisions are removed or stricken.[12]

DATED: August 3, 2015

Respectfully submitted,

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[11] The absence of objection to one term in a retention application should not be mistaken for affirmative consent. Rather, parties-in-interest may see no economic benefit to objecting when all creditors will share the burden pro rata. *See Lehman*, 508 B.R. at 293, n.8. "Appellees overstate the amount of consent involved in the approval of section 6.7 [of the plan]. True, majorities of each class of claimant voted for the Plan, but claimants had only an up-or-down vote on the Plan as a whole and could not vote provision-by-provision. (See Reply at 2, 10.) Even if a majority of claimants opposed section 6.7, the Plan would still have won a majority if claimants were willing to swallow the relatively small price of $26 million spread across all claimants in exchange for moving the process forward."

[12] The Court "may approve some of the terms and conditions proposed in an employment application while rejecting others." *Federal Mogul*, 348 F.3d at 398-99 (citing *Zolfo, Cooper & Co. v. Sunbeam-Oster Co.*, 50 F.3d 253 (3d Cir. 1995)).