IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	Chapter 11
BOOMERANG TUBE, LLC, a Delaware limited liability company, *et al.*,	:	Case No. 15-11247 (MFW) Jointly Administered
Debtors.	:	Re: D.I. 314, 315 & 393

UNITED STATES TRUSTEE'S SUPPLEMENTAL BRIEF OBJECTING TO APPLICATIONS FOR ORDERS AUTHORIZING THE RETENTION OF BROWN RUDNICK LLP AND MORRIS NICHOLS ARSHT & TUNNELL LLP AS CO-COUNSEL FOR THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS

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 files this supplemental brief in accordance with the Court's order at the conclusion of the hearing on August 11, 2015, and in response to the supplemental brief filed on August 17, 2015 by the Committee.

I. BACKGROUND AND INTRODUCTION

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

2. On June 19, 2015, the U.S. Trustee appointed an official committee of unsecured creditors (the "Committee").

[1] Unless otherwise indicated, all chapter, section, federal bankruptcy 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 Bankruptcy Rules of the United States Bankruptcy Court for the District of Delaware.

3. On July 20, 2015, the Committee filed retention applications (the "Applications") for Brown Rudnick LLP ("Brown Rudnick") and Morris Nichols Arsht & Tunnell LLP ("Morris Nichols"). *See* D.I. 271 & 273.

4. On August 3, 2015, the U.S. Trustee filed objections to fee-defense provisions (the "Fee Defense Provisions") in the Applications. *See* D.I. 314 & 315.

5. On August 11, 2015, at a hearing held on the Applications, the Court took the Fee Defense Provisions and the U.S. Trustee's objections thereto under advisement and requested supplemental briefing.

6. On August 17, 2015, the Court entered orders submitted under certification of counsel authorizing the Committee's retention of Morris Nichols and Brown Rudnick, reserving a ruling on the Fee Defense Provisions. *See* D.I. 390 & 391.

7. On August 17, 2015, the Committee filed its supplemental brief in support of the Fee Defense Provisions. *See* D.I. 393.

II. ARGUMENT

A. THE COURT IN *ASARCO* CONSIDERED AND REJECTED THE MARKET APPROACH ADVANCED BY THE PROFESSIONALS HERE.

8. The professionals' argument that fees for defending fee objections may be approved under section 328(a) based on a market approach is foreclosed by *ASARCO*. *Baker Botts L.L.P. v. ASARCO L.L.C.*, 576 U. S. ____, 135 S. Ct. 2158, 2168 (2015). The Court considered that argument in determining whether to allow fee shifting—and rejected it. *Id.*

9. In *ASARCO*, the government argued that public policy supported a statutory interpretation that allowed bankruptcy professionals in some instances to shift fees to

the estate. *Id*. In rejecting the government's view, the Court squarely held that a market approach may not be employed to justify fee shifting by bankruptcy professionals:

> [W]e find this policy argument [by the United States to be] 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.

Id. (emphasis in the original).

10. This Court is bound to follow the Supreme Court's holding on this point and may not rely on a market-determined, policy approach as a basis for allowing a bankruptcy professional to obtain fees on fees. Supreme Court precedent binds the lower courts, including this Court.[2] *United States v. Tann*, 577 F.3d 533, 541 (3d Cir. 2009) (explaining "[w]hile we strive to maintain a consistent body of jurisprudence, we also recognize the overriding principle

[2] Under Third Circuit precedent, this Court would have been required to defer to the Supreme Court's analysis on this point even if it were mere dicta. In interpreting section 506(a) of the Code, the Third Circuit rejected the path forged by some "[a]ppellate courts that dismiss these expressions [in dicta] and strike off on their own [because it will] increase the disparity among tribunals (for other judges are likely to follow the Supreme Court's marching orders) and frustrate the evenhanded administration of justice by giving litigants an outcome other than the one the Supreme Court would be likely to reach were the case heard there." *McDonald v. Master Financial, Inc*., 205 F.3d 606, 612-13 (3d Cir. 2000) (quoting *United States v. Bloom*, 149 F.3d 649, 653 (7th Cir.1998)). *Accord Cuevas v. United States*, 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.")

But the Court's pronouncement in *ASARCO* is not dicta because dicta is only "a statement in a judicial opinion that could have been deleted without seriously impairing the analytical foundations of the holding—that, being peripheral, [and] may not have received the full and careful consideration of the court that uttered it." *McDonald*, 149 F.3d at 653 (quoting *Sarnoff v. American Home Prods. Corp.*, 798 F.2d 1075, 1084 (7th Cir.1986)). Like the statement at issue in *McDonald*, which the Third Circuit determined was not dicta, so, too, the statement in *ASARCO* is not dicta either, as it was the opposite of "peripheral." Justice Thomas relied upon it to reject the government's merits argument, a merits argument the dissent adopted. *ASARCO*, 135 S. Ct. at 2168 (ruling), and at 2169 (dissent agreeing "with the Government that compensation for fee-defense work" should be authorized even though such work is not a service). Either way, the Court's analysis on the market issue must be followed the parties, by the Third Circuit under its precedent, and by lower federal courts, too.

that '[a]s an inferior court in the federal hierarchy, we are, of course, compelled to apply the law announced by the Supreme Court as we find it on the date of our decision.'" (quoting in part *United States v. City of Phila.*, 644 F.2d 187, 192 n.3 (3d Cir. 1980)). Although the professionals may have unearthed dozens of cases in multiple judicial districts pre-dating *ASARCO* to show that it is "historically common, and expected" for bankruptcy professionals, including attorneys, to recover fees for successfully litigating objections to compensation, those cases are irrelevant and no longer good law after *ASARCO*. *See* Committee Supp. Brief, ¶ 4.

11. Nor may a court disregard a Supreme Court pronouncement because the litigants disagree with its premise. *Cf. Bankruptcy Services, Inc. v. Ernst & Young (In re CBI Holding Co.)*, 529 F.3d 432, 469 (2d Cir. 2008) (explaining "a Court does not have the discretion to ignore Supreme Court precedent simply because the reasoning on which it is premised may seem no longer viable."). *Accord Rogers v. Corbett*, 468 F.3d 188, 198, n.10 (3d Cir. 2006) (explaining that the "Plaintiffs have questioned the wisdom of the Supreme Court's decision in *Jenness*. We note in passing that it is not the role of this Court to overturn Supreme Court precedent.").

B. THE FEE DEFENSE PROVISIONS ARE NOT A "CONTRACT."

12. Just as the professionals cannot evade *ASARCO* under a market-based theory, they cannot evade it under a contract theory either.[3] The professionals' request to be compensated for their legal defense costs does not constitute a "contract"—and even if it did, that contract could not be enforced in a manner that violates the Code.

[3] The Committee states that the Fee Defense Provisions are analogous to contract terms found in engagement letters and indemnification agreements with various professionals. Committee Supp. Brief, ¶ 10.

13. Professionals' employment and compensation rights in bankruptcy are not bestowed by "contract." Instead, the retention and payment of professionals is governed by statute. Under the Code, an employment application under section 327 or 1103 is filed with the court, which may also approve reasonable terms and conditions of a professional's employment under section 328(a). *See* 11 U.S.C. § 328(a) (providing that "a committee . . . with the court's approval, may employ or authorize the employment of a professional person"). Regardless of how it is titled, the application is not a contract because it is not an agreement. It is a request that a judge, acting within the constraints of section 328(a), authorize the term or condition of employment. And what a judge can approve is a matter of federal statutory law, not the law of contracts. *In re Federal 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 that were not proposed by the committee but that the court found necessary to satisfy the requirement of reasonableness under section 328(a)).

14. The proposed order approving the application is also not a contract. First, any rights or obligations created by the order are the result of the court's approval, not the agreement of the party to be obligated. RESTATEMENT (SECOND) OF CONTRACTS 9 (1981) (providing that "[t]here must be at least two parties to a contract, a promisor and a promisee."). Second, as stated above, the scope of permissible terms is governed by federal statute, not the agreement of the parties. *In re Federal Mogul-Global, Inc.*, 348 F.3d at 397-98. So while an order approving employment terms may create a statutory right, it does not create a contractual one.

15. Finally, the proposal here looks nothing like a contract. The professionals do not propose an agreement between parties who mutually agree that in the event of litigation,

the losing party will pay the prevailing party's legal fees. The professionals have not agreed to a reciprocal obligation to pay the estate's (or anyone else's) legal fees should the professionals unsuccessfully litigate objections to their fee applications. Rather, the professionals seek to impose a one-way shift of fees to the estate—not a losing party—and to do so regardless of whether it is the estate or some other party who objects to the fees.[4]

16. A party other than the estate could object since bankruptcy is not a bilateral contract or proceeding. Rather, it is a comprehensive, court-supervised process implicating diverse constituencies with a multiplicity of interests. It is a "collective proceeding through which" creditors' claims are "vindicated for creditors' mutual benefit." *In re A.G. Financial Service Center, Inc.*, 395 F.3d 410, 415 (7th Cir. 2005). As a result, the Code provides "numerous and detailed provisions concerning the employment of professional persons, their compensation and payment." *In re Financial News Network, Inc.*, 134 B.R. 732, 735 (Bankr. S.D.N.Y. 1991). But professionals cannot by contract require third parties to pay their legal fees. Although one can become a third party beneficiary of a contract without giving consent, the law does not recognize unilateral imposition of contractual obligations on third-party benefactors. *See Motorsport Eng'g, Inc. v. Maserati SPA*, 316 F.3d 26, 29 (1st Cir. 2002) (holding that a third party cannot be bound to a contract it did not sign or otherwise assent to); *Abraham Zion Corp. v. Lebow*, 761 F.2d 93, 103 (2d Cir. 1985) (same). That the Committee seeks to justify the Fee Defense Provisions as a contract, in part, because the "committee and the firms are sophisticated

[4] The professionals' own authorities support the U.S. Trustee's position. To support their claim that the Fee Defense Provisions were common outside of bankruptcy, the professionals cited *Opinion 2009-2 of the Delaware State Bar Association Committee on Professional Ethics* as evidence that such provisions complied with applicable ethics rules (the "*Ethics Opinion*"). The *Ethics Opinion* (attached to the Committee's supplemental brief as Exhibit 4) makes clear that any written fee-shifting agreement should contain a "clear statement that the right to recover costs and outside counsel fees is reciprocal or mutual in nature, in that the client, in the event a fee dispute arises, also has the ability to seek the same costs and reasonable attorneys' fees in defending the action by Attorney . . . ." *Ethics Opinion*, pp. 1 of 7.

business entities with equal bargaining power who engaged in arms' length negotiations" wholly misses the point. Committee Supp. Brief, ¶ 10.

17. But even if the proposed employment agreement could somehow be construed to be a contract, it would have to be rejected. The American Rule's prohibition against fee shifting can be altered by statute, and it can be altered by contract. But the American Rule cannot be altered by a contract that violates a statute. Courts have an independent obligation to ensure that what they approve is lawful under the Code. *See United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260, 277 (2010) (holding that bankruptcy courts have the authority to ensure that proposed actions conform to the requirements of the Code). And courts have no power to take actions that violate the Code. *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206 (1988) (stating that whatever "equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code"); *Law v Siegel*, __ U.S. __, 134 S. Ct. 1188, 1194 (2014) (holding that "in exercising [its] statutory and inherent powers, a bankruptcy court may not contravene specific statutory provisions."). As explained in the U.S. Trustee's original objections [D.I. 314-316,] the proposed employment provisions violate sections 328 and 330 of the Code. Thus, the Applications asking the Court to approve these provisions must be rejected.

C. LEGAL FEES FOR DEFENDING FEE LITIGATION OBJECTIONS MAY NOT BE REIMBURSED AS EXPENSES FOR EITHER LEGAL OR FINANCIAL PROFESSIONALS.

18. The U.S. Trustee objected to the Fee Defense Provisions sought by all of the professionals for the Committee, including Alvarez & Marsal, who seeks to be retained as a financial advisor. Given the still-pending application for Alvarez & Marsal and the attorneys'

heavy reliance on indemnification provisions for financial advisors, the U.S. Trustee briefly addresses the *ASARCO* issue in the context of expense reimbursement and indemnification.

19. Non-lawyer professionals, such as financial advisors, are entitled to no better and no worse treatment than lawyers with respect to legal fees for defending objections to fee applications in a bankruptcy proceeding. The Third Circuit's decision in *United Artists Theatre Co. v. Walton*, 315 F.3d 217 (3d Cir. 2003), does not compel a different result. In that case, the Third Circuit held that the bankruptcy court was authorized (but not required) to approve a reasonable, "market-driven" indemnification provision in a financial advisor's retention application, which purported to give the non-attorney professionals serving as corporate officers the same rights of indemnification enjoyed by the debtor's officers in the event they were sued for negligence. *Id*. at 230. But *United Artists* does not address the very different scenario of a bankruptcy professional litigating to recover its own fees, and its analogy to the contractual protections offered to in-house employees would be irrelevant absent proof that corporate employees are typically reimbursed their legal fees in compensation disputes with their employers.[5] Even if, however, *United Artists* were to be given such a broad interpretation, its holding would necessarily be limited by the subsequent Supreme Court decisions in *ASARCO,* as well as *Espinosa* and *Law*.

20. Not only is such parity between legal and non-legal professionals fair; the law requires it. First, section 330(a)(1)(B) allows the award of "necessary" expenses. But those expenses must relate and be incident to the client services for which the professional can be compensated under section 3301(a)(1)(A). Because legal fees for defending fee application

[5] Even so, the Third Circuit explained that simply because terms of engagement "are now common in the marketplace does not automatically make them 'reasonable' under § 328. Our approach is 'market driven,' not 'market-determined,' especially in the realm of bankruptcy, where courts play a special supervisory role." *United Artists Theatre Co. v. Walton*, 315 F.3d 217, 230 (3d Cir. 2003).

objections cannot be paid as compensation, those same legal fees cannot be reimbursed as expenses. Otherwise, in *ASARCO*, Baker Botts need only have retained outside counsel to defend its fee applications and expensed the legal fees rather than seek compensation for them. Surely "outsourcing" the firm's fee defense work is not a result that the Supreme Court would have countenanced given its analysis in *ASARCO*.

21. Second, any terms for reimbursement of the non-legal professionals' expenses approved under section 328(a) must relate to "employment." Under sections 327 and 1103, professionals are employed to represent their client's interests, not their own. The professionals are not employed to litigate their fees, and thus they cannot be reimbursed their legal fees for doing so.

22. Third, any terms for reimbursement of the non-legal professionals' expenses approved under section 328(a) must also be reasonable. It is not reasonable to pay expenses not incurred in representing one's client.

III. CONCLUSION

23. For the reasons stated above and originally stated in the U.S. Trustee's objections, the Court should deny the Applications unless the Fee Defense Provisions are removed or stricken.

DATED: August 24, 2015

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