Answer Key[1]

Wait, Wait, Don't Tell Me…[2]
Ethical Considerations for Bankruptcy Practice

Game Show Host: Honorable James B. Haines, Jr.

Judicial Contestants	**Attorney Contestants**
Honorable A. Benjamin Goldgar	**Professor Nancy B. Rapoport**
Honorable Neil P. Olack	**Christine E. Devine, Esq.**
Honorable Erithe A. Smith	**Timothy F. Nixon, Esq.**

Question 1 – Answer 1

Due Diligence
Counsel Duty to Investigate Debtor's Assets Pre-Petition

Bankruptcy attorneys have an ethical obligation to conduct a reasonable investigation of their client's assets and liabilities pre-petition. Debtor's counsel cannot simply rely on what she is told by her client when preparing bankruptcy pleadings, including Schedules. See In re Garrard, 2013 WL 4009324 *1, *4 (Bankr. N.D. Ala. 2013). To ensure a thorough investigation, further inquiry into the debtor's financial affairs may be necessary. See id.

The Bankruptcy Court in Garrard adopted the reasonable inquiry standard as espoused by the Courts in In re Thomas, 337 B.R. 879 (Bankr. S.D. Tex. 2006), aff'd, 223 Fed. Appx. 310 (5th Cir. 2007) and In re Henry Lubaczewski, No. 98-19398 (Bankr. D.N.J. 2005) as requiring the attorney: "(1) to explain the requirement of full, complete, accurate, and honest disclosure of all information required of a debtor; (2) to ask probing and pertinent questions designed to elicit full, complete, accurate, and honest disclosure of all information required of a debtor; (3) to check the debtor's responses in the petition and Schedules to assure they are internally and externally consistent; (4) to demand of the debtor full, complete, accurate, and honest disclosure of all information required before the attorney signs and files the petition; and (5) to seek relief from the court in the event that the attorney learns that he or she may have been misled by a debtor . . . ." Thomas, 337 B.R. at 892 (quoting Lubaczewksi). In summary, before filing the bankruptcy petition, "an attorney is required to determine that [its] content is well grounded in fact, and his signature on the petition serves as a certification that he has no knowledge *after an*

[1] Panel materials were prepared with the assistance of Kate P. Foley, Esq., an associate at Mirick O'Connell LLP in Westborough, Massachusetts.

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inquiry reasonable under the circumstances that the information contained in the schedules is other than true and accurate." Garrard, 2013 WL 4009324 at *7 (emphasis in original).

Relevant cases discussing pre-petition due diligence and related ethical concerns include the following:

1. In re Garrard, 2013 WL 4009324 (Bankr. N.D. Ala. 2013) – The Court determined that debtor's attorney failed to properly inquire into the implausibility of the debtor's expenses set forth in the debtor's Schedule J. Further, the Court held that the debtor filed his Schedule J for the purpose of misleading the court and the debtor's creditors related to issues of the feasibility of the debtor's Chapter 13 plan and the prospects for reorganization.

2. In re Kayne, 453 B.R. 372 (9th Cir. B.A.P. 2011) – The Court held that a debtor's attorney's failure to list a promissory note payable to debtor as a bankruptcy asset constituted a sanctionable violation of Federal Rule of Bankruptcy Procedure 9011 and of 11 U.S.C. § 707.

3. In re Witherow, 391 B.R. 217 (Bankr. D. Mass. 2008) – The Court sanctioned a debtor's attorney as a result of various omissions and errors in the debtor's Schedules. As grounds for the issuance of sanctions, the Court determined that the attorney violated his Rule 9011 and statutory "certification" obligations. Applying the reasonable inquiry standard, the Court considered these questions:

> (1) did the attorney impress upon the debtor the critical importance of accuracy in the preparation of documents to be presented to the Court; (2) did the attorney seek from the debtor, and then review, whatever documents were within the debtor's possession, custody or control in order to verify the information provided by the debtor; (3) did the attorney employ such external verification tools as were available and not time or cost prohibitive (e.g., on-line real estate title compilations, on-line lien search, tax 'scripts'); (4) was any of the information provided by the debtor and then set forth in the debtor's court filings internally inconsistent—that is, was there anything which should have obviously alerted the attorney that the information provided by the debtor could not be accurate; and (5) did the attorney act promptly to correct any information presented to the Court which turned out, notwithstanding the attorney's best efforts, to be inaccurate. These questions can be further simplified and reduced to one question, their common denominator: Did the attorney do his or her level best to get it right?

Witherow, 391 B.R. at 228.

Relevant Bankruptcy Code provisions and Rules discussing pre-petition due diligence and related ethical concerns include the following:

Answer Key

1. 11 U.S.C. § 526(a)(2) – "A debt relief agency [including an attorney] shall not – make any statement, or counsel or advise any assisted person or prospective assisted person to make a statement in a document filed in a case or proceeding under this title, that is untrue or misleading, or that upon the exercise of reasonable care, should have been known by such agency to be untrue or misleading."

2. 11 U.S.C. § 707(b)(4)(C) – "The signature of an attorney on a petition, pleading, or written motion shall constitute a certification that the attorney has – (i) performed a reasonable investigation into the circumstances that gave rise to the petition, pleading, or written motion; and determined that the petition, pleading, or written motion – (I) is well grounded in fact . . . ."

3. 11 U.S.C. § 707(b)(4)(D) – "The signature of an attorney on the petition shall constitute a certification that the attorney has no knowledge after an inquiry that the information in the schedules filed with such petition is incorrect . . . ."

4. Fed. R. Bankr. P. 9011(b) – "*Representations to the Court.* By presenting to the court (whether by signing, filing, submitting, or later advocating) a petition, pleading, written motion, or other paper, an attorney . . . is certifying that to the best of the [attorney's] knowledge, information, and belief, formed after an inquiry reasonable under the circumstances, – (1) it is not being presented for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation [and] . . . (3) the allegations and other factual contentions have evidentiary support . . . ."

5. 11 U.S.C. § 707(b)(4)(B) – "If the court finds that the attorney for the debtor violated Rule 9011 of the Federal Rules of Bankruptcy Procedure, the court, on its own initiative or on the motion of a party in interest, in accordance with such procedures, may order – (i) the assessment of an appropriate civil penalty against the attorney for the debtor; and (ii) the payment of such civil penalty to the trustee, the United States trustee (or the bankruptcy administrator, if any)."

6. ABA Model Rule 3.3(a) – "A lawyer shall not knowingly: (1) make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by the lawyer . . . ."

For additional relevant authority, see G. Thomas Curran Jr., *How Much Diligence is Due?: Defining an Attorney's Duty to Perform a Pre-Petition Inquiry*, ABI Journal, November 2013, at 24.

Question 2 – Answer 2

Limited Scope Representation
Counsel Duty of Competence and Informed Consent

Unbundling is the term commonly used to describe the practice of limiting the scope of legal services to be provided to a client by dividing comprehensive legal representation into a series of discrete tasks, only some of which the client contracts with the lawyer to perform. See In re Seare, 493 B.R. 158, 183 (Bankr. D. Nev. 2013), aff'd, 2014 WL 4186483 (9th Cir. B.A.P 2014). Among other things, the Bankruptcy Court noted that unbundling can benefit clients by providing access to legal services that would otherwise be too expensive, particularly in family and bankruptcy law, but the practice can also raise ethical concerns if the attorney fails to ensure that the client will receive all of the services reasonably necessary to achieve the client's goals. Bankruptcy lawyers must effectively disclose the risks of an unbundling arrangement and also obtain informed consent form the client. Further, in certain circumstances, obtaining informed consent may be impossible.

Relevant cases discussing the limits of unbundling and the relevant ethical concerns include the following:

1. In re Seare, 493 B.R. 158 (Bankr. D. Nev. 2013), aff'd, 2014 WL 4186483 (9th Cir. B.A.P. 2014) – In connection with a Chapter 7 individual bankruptcy case and a fee agreement which "unbundled" certain services, the Bankruptcy Court sanctioned a bankruptcy lawyer for violating the Nevada Rules of Professional Conduct. The Court found that the attorney had failed to assess the clients' goals in connection with filing bankruptcy and, as a result, failed to provide the legal services needed to achieve that goal. The Court found that the attorney should have known that the clients would require representation in adversary proceedings to eliminate a wage garnishment stemming from a fraud judgment.

2. In re Cuomo, 2013 WL 3155425 (Bankr. D. Nev. 2013) – The Bankruptcy Court held that a bankruptcy attorney failed to meet his duty of competence by failing to sufficiently investigate the needs of his client. The Court rejected counsel's argument that he was excused from a duty to investigate because of provisions in the retainer agreement which placed the responsibility on the client for accurate preparation of a bankruptcy petition. The Court held that a lawyer may not use a contract to limit the scope of legal services such that he essentially becomes responsible only for transcribing information provided by the client onto the Schedule F. The case, however, is distinguishable from Seare in that the Court found counsel had not truly unbundled his legal services for this client because he had offered to provide a wide scope of services, including representation in adversary proceedings, which were rejected by the client as too expensive.

3. In re Ortiz, 496 B.R. 144 (Bankr. S.D.N.Y. 2013) – The Bankruptcy Court found that the lawyer had improperly unbundled his services by refusing to provide the service of more than one appearance at a § 341(a) meeting. See Ortiz, 496 B.R. at 149. The Court ruled that this was a violation of New York Rule of Professional Responsibility 1.2(c) because the importance of representation at these meetings was tied to the duty of competence of the lawyer. See id. By limiting the scope of essential services, he violated his duty of competence to the client and improperly unbundled his legal services. See id. at 149-50. The lawyer further failed to obtain the informed consent of the client as to the consequences of limiting the scope of his services. See id. at 150.

4. Relevant Model Rules:

   a. ABA Model Rule 1.1 – "A lawyer shall provide competent representation to a client . . . the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation." Competent representation depends on the client's objectives. Notwithstanding a client's informed consent to an attorney's limited representation, certain exclusions may not be reasonable.

   b. ABA Model Rule 1.2(c) – "A lawyer may limit the scope of the representation if the limitation is reasonable under the circumstances and the client gives informed consent."

For additional relevant authority, see Carrie A. Zuniga, *The Ethics of Unbundling Legal Services in Consumer Cases*, ABI Journal, October 2013, at 14.

Question 3 – Answer 2

CRO Retention
Statutory Bases for Retention of Non-Estate Professionals

Chapter 11 debtors may seek to retain a chief restructuring officer ("CRO") pursuant to 11 U.S.C. § 327, which governs retention of estate professionals. Section 327 requires that the professional be disinterested. Recently, however, Chapter 11 debtors are seeking to retain CROs pursuant to 11 U.S.C. §§ 105(a) and 363(b)(1). Relying on these Code sections, debtors have alleged that retention and payment of CROs constitute use of the debtors' assets other than in the ordinary course of business as contemplated by 11 U.S.C. § 363(b)(1). Most prominently in the District of Delaware and the Southern District of New York, courts that consider CRO retention pursuant to 11 U.S.C. §§ 105(a) and 363(b)(1) will require the retention to comply with the "Jay Alix Protocols." See Timothy W. Brink and James R. Irving, *Emerging Trends and Lingering Criticisms: A CRO Retention Update*, ABI Journal, September 2013, at 18. Elements of these protocols include:

1. The professional may only serve in one capacity (i.e., as a CRO, crisis manager, financial advisor, claims agent or investor);

2. The professional may not be a member of the debtor's board or have served on the board within the two years prior to the petition date;

3. The professional must disclose its relationships with all interested parties; and

4. The professional's compensation will be reviewed under a reasonableness standard at the end of the case; however, the professional is not required to file a formal fee application, and any success fees payable to the professional must be approved at the conclusion of the case.

Id.

Notably, a CRO retained pursuant to 11 U.S.C. §§ 105(a) and 363(b)(1) is not required to file formal fee applications. Further, there is no "disinterestedness" requirement. Courts considering the "Jay Alix Protocols", however, typically will require that the CRO disclose its relationships with all interested parties. Notwithstanding the trend toward CRO retention based on 11 U.S.C. §§ 105(a) and 363(b)(1), some courts have criticized this approach as a means to avoid the "disinterestedness" and compensation requirements of traditional estate professional retention pursuant to 11 U.S.C. §§ 327(a). See, e.g., In re Blue Stone Real Estate, Constr. & Dev. Corp., 392 B.R. 897 (Bankr. M.D. Fla. 2008); In re Mirant Corp., 354 B.R. 113 (Bankr. N.D. Tex. 2006). Regardless of the statutory basis relied upon for CRO retention, Chapter 11 debtors should address in their applications various concerns related to "disinterestedness" and payment of fees and expenses.

Relevant cases discussing some ethical concerns raised by courts and U.S. Trustees regarding CRO retention pursuant to 11 U.S.C. §§ 105(a) and 363(b)(1) include the following:

1. In re Mirant Corp., 354 B.R. 113 (Bankr. N.D. Tex. 2006) – The Bankruptcy Court approved a fee application for a company which provided crisis services to the debtors. The Court noted that the company was retained pursuant to 11 U.S.C. § 363 because part of its role was to provide the debtors with a CRO. Because the company complied with the procedures for payment of professionals, the Court granted the fee application. In a footnote, the Court noted: "The UST and other parties acquiesced in this method of retention (which was intended to avoid application to AP of the disinterestedness test of 11 U.S.C. § 101(14) due to AP's personnel serving as officers of Debtors.) The court is not satisfied that use of Code § 363 is appropriate for such a purpose, but need not here reach that issue." Mirant, 354 B.R. at 172, n. 29.

2. In re Blue Stone Real Estate, Constr. & Dev. Corp., 392 B.R. 897 (Bankr. M.D. Fla. 2008) – The Bankruptcy Court determined that the proposed CRO was clearly a "professional" within the meaning of 11 U.S.C. § 327(a) and, as such, his retention should be subject to § 327(a) and his compensation subject to review and authorization. As a result, the Court authorized the proposed CRO's retention, but pursuant to 11 U.S.C. §§ 327(a) and 105(a), rather than 11 U.S.C. § 363 as requested by the debtors. In a footnote, the Court noted:

> The two main purposes of section 327 are to permit the Court to control administrative expenses in the form of professionals' compensation and ensure that the professional is conflict free and impartial. Absent such judicial oversight and the opportunity for continuing party-in-interest scrutiny of both a professional's retention and compensation, these important goals of the Bankruptcy Code cannot be met. The so-called 'Jay Alix' protocol that depends upon section 363 for retention of an executive officer does not provide the Court the same ability to meet the twin goals of section 327 when the candidate for employment is also a professional.

Blue Stone, 392 B.R. at 907, n. 14.

3. In re Nesbitt Portland Prop. LLC, No. 12-12883 (Bankr. C.D. Cal. 2012), Dkt. Nos. 265 and 296 – The U.S. Trustee objected to the debtor's application to retain a CRO pursuant to 11 U.S.C. §§ 363(b)(1) on the grounds that the CRO would have unfettered discretion because the CRO did not have to report to any board of directors and the debtor could not terminate the CRO. As in Blue Stone, the Court granted the retention application, but under 11 U.S.C. § 327(a), rather than pursuant to 11 U.S.C. §§ 105(a) and 363(b)(1) as requested by the debtor.

Question 4 – Answer 3

Retention of Estate Professionals
Disinterestedness Requirements

"The Bankruptcy Code does not provide for the disqualification of an entire law firm based on the non-disinterestedness of one of its attorneys." In re Sea Island Co., No. 10-21034, 2010 WL 4386855, at *2 (Bankr. S.D. Ga. Oct. 20, 2010) (citation omitted). The concept of imputation of conflicts of interest is, however, contained in the Model Rules of Professional Conduct Rule 1.10. The Model Rules of Professional Conduct Rule 1.7, defining conflicts of interest, is an analogous concept but it is not the same definition as that of "disinterested person" in 11 U.S.C. § 101(14).

Consider also the application of Federal Rule of Bankruptcy Procedure 2014 which requires the applicant to state "to the best of the applicant's knowledge, all of the person's connections with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee." Fed. R. Bankr. P. 2014.

Is it then a matter of simple disclosure or is there an implication from the broad disclosure requirement? Consider the practical impact in large bankruptcies with large law firms. Also, at least as one court raised the wider issue of the importance of public perception and confidence in the process.

Unsurprisingly, unanimity does not exist. Courts struggle with how to deal with these issues of actual versus potential harm. As in many decision-making contexts, there are those that favor "bright line" rules and those that dive into a more detailed case-by-case factual analysis. Under either approach, the specific facts are important so there may not be as much divergence as a quick reading of case summaries may lead one to believe.

1. Majority View—It is a *per se* rule that the disinterestedness of a member of a firm is imputed to the entire firm. In re Essential Therapeutics, Inc., 295 B.R. 203, 211 (Bankr. D. Del. 2003).

2. Minority View—There is no *per se* rule in the Fifth Circuit and retention may be permitted. In re Cygnus Oil & Gas Corp., 48 Bankr. Ct. Dec. 87, 2007 WL 1580111 (Bankr. S.D. Tex. 2007).

It may be possible to retain NY Law pursuant to 11 U.S.C. § 327(e) because there is no material adverse interest and no disinterestedness requirement. In re Coda Holdings, Inc., No. 13-11153 (Bankr. D. Del. June 17, 2013).

For additional relevant authority, see Jerald I. Ancel and Jeffrey J. Graham, *Renewed Interest in Disinterestedness Under §§ 101(14) and 327(a)*, ABI Journal, September 2013, at 14.

Question 5 – Answer 2

Joint Representation of Debtors
Ethical Considerations Regarding Conflicts

This is an area in which, again, the specific facts are important. A client's wishes as well as the practicality and costs are considered. In larger cases, that practical resolution many times is a "conflicts counsel" to deal with the issue.

1. Majority View—There is no *per se* rule. In re BH&P, Inc., 949 F.2d 1300, 1316 (3d Cir. 1991). Courts must undertake a case-by-case analysis of factors, among them, the nature of the disclosure, the nature of the inter-creditor claims, and the nature of the conflict (potential or actual). If the claims cannot be resolved, then counsel must remove himself from the dispute. In re Adelphia Commens Corp., 336 B.R. 610, 673 (Bankr. S.D.N.Y. 2006), aff'd, 342 B.R. 122 (S.D.N.Y. 2006).

2. Minority View—There is a rebuttable presumption that the representation is improper. In re Lee, 94 B.R. 172 (Bankr. C.D. Cal. 1988). It is improper to appoint the same counsel when creditors have dealt with debtors as an economic unit, there is creditor overlap, or there is entanglement.

B&P's waiver is ineffective and insufficient to waive actual conflicts. In re JMK Constr. Group, Ltd., 441 B.R. 222, 226 (Bankr. S.D.N.Y. 2010).

Is it an actual conflict or a potential conflict? Consider 11 U.S.C. § 327(c), which provides: "[i]n a case under chapter 7, 12, or 11 of this title, a person is not disqualified for employment under this section solely because of such person's employment by or representation of a creditor, unless there is objection by another creditor or the United States trustee, in which case the court shall disapprove such employment if there is an actual conflict of interest . . . ." 11 U.S.C. § 327(c) (emphasis added).

Consider also by analogy the Model Rule 1.7(b):

Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:

1. the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;

2. the representation is not prohibited by law;

3. the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and

4. each affected client gives informed consent, confirmed in writing.

For additional relevant authority, see Lois R. Lupica and Nancy B. Rapoport, *Final Report of the ABI National Ethics Task Force*, American Bankruptcy Institute (April 21, 2013) at pp. 37-47 (discussing the use of conflicts counsel in business reorganization cases).

Question 6 – Answer 3

Disgorgement of Counsel Fees
Scope of Bankruptcy Court Authority

This hypothetical addresses the scope of a bankruptcy court's authority to regulate attorney compensation and, specifically, to enter disgorgement orders. Recently, the Fifth Circuit Court of Appeals addressed this issue in In re Whitley, 737 F.3d 980 (5th Cir. 2013). A Bankruptcy Court has the authority to regulate attorney compensation by ordering debtor's counsel to return excessive compensation to the estate. 11 U.S.C. § 329(b). The Court also has the authority to discipline attorneys for violating disclosure requirements. In Whitley, debtor's counsel had failed to disclose certain transactions to the Court whereby the debtor had transferred certain properties to his counsel and whereby counsel subsequently re-acquired such properties at a foreclosure auction. See Whitley, 737 F.3d at 983. In the context of an adversary proceeding by a chapter 7 trustee of the debtor's case against counsel, the Bankruptcy Court below issued a show cause order pursuant to 11 U.S.C. § 329(b) instructing counsel to provide evidence of the reasonable value of his services to the debtor. See id. at 984. The Bankruptcy Court entered an order denying counsel all of his requested fees and ordering counsel to return all of the consideration that he had received to the estate, which included the two foreclosure properties. See id. The District Court affirmed the ruling below. See id. Counsel subsequently appealed to the Fifth Circuit Court of Appeals, seeking a reversal of the portion of the order which required him to return the two properties outright. See id. at 985.

"A bankruptcy court's decision to disgorge fees or impose a sanction is reviewed for abuse of discretion." In re Am. Int'l Refinery, 676 F.3d 455, 461 (5th Cir. 2012). The Court ultimately determined that the Bankruptcy Court improperly relied on 11 U.S.C. § 329(b) in ordering the return of the two properties. See id. at 987. The Court of Appeals held that while the Bankruptcy Court ordered counsel to return all "consideration" he received from the debtor, it imposed an additional sanction beyond return of compensation. Id. at 988. The Court of Appeals emphasized that while a bankruptcy court has broad discretion to regulate attorney compensation and order disgorgement, when doing so, a court must use the lease restrictive sanction necessary to deter the inappropriate behavior. Id. at 987 (quoting In re First City Banorporation of Tex., Inc., 282 F.3d 864, 867 (5th Cir. 2002)). Further, the sanction imposed must be commensurate with the egregiousness of the conduct such that the court compares the sanction amount to the conduct of the sanctioned party. Id. (quoting In re Downs, 103 F.3d 472, 478 (6th Cir. 1996)); see also In re GSC Group, Inc., 502 B.R. 673 (Bankr. S.D.N.Y. 2013) (discussing appropriate sanctions for violation of disclosure obligations).

A relevant Bankruptcy Code provision and Rule of Federal Bankruptcy Procedure to consider are:

1. 11 U.S.C. § 329(b) – "If such compensation [of a debtor's attorney] exceeds the reasonable value of any such services, the court may cancel any such agreement, or order the return of any such payment, to the extent excessive, to –

    (1) the estate, if the property transferred –

        (A) would have been property of the estate; or

        (B) was to be paid by or on behalf of the debtor under a plan under chapter 11, 12, or 13 of this title; or

    (2) the entity that made such payment."

2. Corollary in Rule 9011(c)(2) – "*Nature of Sanctions; Limitations.* A sanction imposed for violation of this rule shall be limited to what is sufficient to deter repetition of such conduct or comparable conduct by others similarly situated . . . [T]he sanction may . . . include . . . an order directing payment to the movant of some or all of the reasonable attorneys' fees and other expenses incurred as a direct result of the violation."

Question 7 – Answer 3

Withdrawal of Representation
Ethical Obligations of Counsel

The hypothetical is "purposefully vague" as to whether the valuation is merely questionable or could be considered outright fraudulent. As in real life, that is sometimes in the eye of the beholder. Similarly, it could be that the appeal actually has merit but that is unknown at the time the lawyer receives the direction.

Rule 1.16 of American Bar Association Model Rules of Professional Conduct, entitled "Declining or Terminating Representation," states:

(a) Except as stated in paragraph (c), a lawyer shall not represent a client or, where representation has commenced, shall withdraw from the representation of a client if:

(1) the representation will result in violation of the rules of professional conduct or other law; . . .

(b) Except as stated in paragraph (c), a lawyer may withdraw from representing a client if:

(1) withdrawal can be accomplished without material adverse effect on the interests of the client; . . .

(2) the client insists upon taking action that the lawyer considers repugnant or with which the lawyer has a fundamental disagreement; or . . .

(3) other good cause for withdrawal exists.

(c) A lawyer must comply with applicable law requiring notice to or permission of a tribunal when terminating a representation. When ordered to do so by a tribunal, a lawyer shall continue representation notwithstanding good cause for terminating the representation.

Rule 1.16(c) is operative here. Although the circumstances are unusual, the court does not have to permit NY Law to withdraw. See, e.g., In re Living Hope Southeast, LLC, 509 B.R. 629, 636 (Bankr. E.D. Ark. 2014).

The case could fit under either Rule 1.16 (a)(1) or under (b). Rule 1.16(a)(1) is particularly broad. Rule 1.16(b)(4) is also broad, but does not require the violation of a particular rule or law.

For additional relevant authority, see Hon. Stacey G.C. Jernigan, *Motions to Withdraw as Attorney: Why Breaking Up Is Sometimes Hard to Do*, ABI Journal, September 2012, at 50.

Question 8 – Answer 2

Ghostwriting Papers
The Ethical Obligations of Counsel

Ghostwriting occurs when an attorney prepares documents for filing for a party who would otherwise appear unrepresented in litigation. Courts have held that this practice violates Federal Rule of Bankruptcy Procedure 9011. See In re Futch, No. 09-01841, at 4 (Bankr. S.D. Miss. 2011). Many courts disapprove of ghostwriting because it creates the incorrect impression that the client drafted the pleading, a fact which often allows a judge to apply a more liberal construction of the rules governing pleadings. Ghostwriting may also create an unfair disadvantage for the opposing party. Further, ghostwriting may be a violation of the lawyer's duty of candor to the court because the drafting attorney has intentionally omitted his name from the work product to present the work as that of another. In re Stroeker, No. 09-52079-NPO, at 3 (Bankr. S.D. Miss. 2009). The ABA, however, has stated that ghostwriting may be a permissible form of limited representation under Model Rule 1.2(c). See In re Fengling Liu, 664 F.3d 367, 370 (2d Cir. 2011).

Relevant cases discussing ghost writing and the relevant ethical concerns include the following:

1. In re Fengling Liu, 664 F.3d 367 (2d Cir. 2011) – In this case, the Second Circuit Court of Appeals declined to adopt the recommendation of the Committee on Attorney Admissions and Grievances because they found that the attorney's ghostwriting on behalf of *pro se* litigants did not constitute sanctionable misconduct. The Circuit Court found that the petitions prepared by an attorney on behalf of the *pro se* litigants were simple and straightforward and unlikely to lead to any prejudice for the opposing party. There was also no evidence that the attorney sought to obtain an unfair advantage in the proceeding through the use of ghostwriting.

   The Court also noted that based on a 2007 American Bar Association opinion, the practice of ghostwriting is likely a form of permissible limited representation under Rule 1.2(c). The Court ultimately ruled that it was improper to impose sanctions for ghostwriting because there was no rule or precedent in the jurisdiction prohibiting the practice such that the attorney should have been aware that the practice was prohibited.

2. In re Smith, No. 12-11603, 2013 WL 1092059 (Bankr. E.D. Tenn. 2013) – In this case, the Court ruled that an attorney who had prepared bankruptcy petitions on behalf of a client who filed the petition *pro se* due to the attorney's inability to use the electronic case filing system had violated the ethical rules. See id. at 2. The Court ruled that her nondisclosure of authorship of the petition was a violation of her duty of candor to the tribunal because she had told the client to file the petition *pro se* since she had not yet been reinstated to practice and, therefore, could not comply with the court's electronic case filing requirement. See id. at 5.

3. In re Hood, 727 F.2d 1360 (11th Cir. 2013) – In this case, the Eleventh Circuit Appeals Court ruled that a law firm whose employee had transcribed answers onto a pre-printed Chapter 13 petition based on the client's answers which was then filed *pro se* did not constitute impermissible ghostwriting because the law firm did not draft the document for the client within the meaning of the Florida Bar Regulation. See id. at 1364. The Court followed the reasoning in In re Fengling Liu and ruled that there was no evidence of fraudulent intent and that providing assistance to a client in completing a publicly available, pre-printed form was not sanctionable conduct. See id. at 1365.

4. Duran v. Carris, 238 F.3d 1268 (10th Cir. 2001) – In contrast to In re Fengling Liu, the Tenth Circuit Appeals Court has a much more restrictive view on ghostwriting. In Duran, the Court ruled that the attorney was subject to sanctions for providing substantial

legal assistance to a client without signing his name because this conduct afforded the client the benefit of the Court's liberal construction of his *pro se* pleadings and improperly shielded the attorney from responsibility and accountability for his actions and conflicted with Fed. R. Civ. P. 11(a).

5. ABA Standing Comm. on Ethics & Prof'l Resp., Form Op. 07-446, Undisclosed Legal Assistance to Pro Se Litigants (2007) (finding that providing undisclosed legal assistance to *pro se* litigants constituted a form of limited representation, pursuant to ABA Model Rule of Professional Conduct 1.2(c), which states that "[a] lawyer may limit the scope of the representation [of a client] if the limitation is reasonable under the circumstances and the client gives informed consent.")

Question 9 – Answer 1

Creditors' Committee Issues
Potential for Payment of Committee Members' Professionals by Estate

Recently, members of creditors' committees have sought out opportunities to obtain reimbursement from bankruptcy estates for the fees incurred by their own counsel. It is well established that fees incurred by counsel to any official committee of unsecured creditors employed under 11 U.S.C. § 327 may request allowance of fees per 11 U.S.C. § 328. Counsel to individual committee members, however, are not employed under § 327 and, therefore, are not entitled to file applications under § 328. The law is currently developing regarding the circumstances under which counsel to a committee member may be paid from the estate as an administrative expense under 11 U.S.C. § 503.

Some recent decisions include the following:

1. In re Lehman Bros., 508 B.R. 283 (S.D.N.Y. 2014) – In this case, members of the official committee of unsecured creditors hired their own attorneys who then sought payment under the reorganization plan. To achieve this goal, the committee members included a specific plan section which allowed individual members' reasonable professional fee expenses to be included as administrative expense claims and which required the debtor to pay those claims in full. See id. at 287. On appeal, however, the District Court found that plan provision to be invalid. The District Court found that that § 503(b)(4) of the Bankruptcy Code expressly addresses professional fee administrative expenses and does provide for professional fees incurred by a committee member. See id.

   The District Court remanded the matter to the Bankruptcy Court to evaluate whether the individual members of the committee qualified under 11 U.S.C. § 503(b)(3)(D) by virtue of having made a "substantial contribution" to the bankruptcy case to allow for their professional fees to be paid under § 503(b)(4). See id. at 296.

2. In re Spansion, Inc., No. 09-10690, 2014 WL 1928632 (Bankr. D. Del. 2014) – In this case, individual committee members sought payment for professional fees and expenses

incurred on the basis of substantial contributions made in connection with the bankruptcy proceeding. See id. at *1. While "substantial contribution" is not defined in the Bankruptcy Code, it has been held to apply only if a contribution results in "actual and demonstrable benefit to the debtors' estates and the creditors." Id. at *2.

The Court ruled that the Ad Hoc Convert Committee did substantially contribute because they assisted in determining the debtor's enterprise value by aggressively looking at the methodology and presumptions of the debtors' experts. See id. at *3. In contrast, however, the Ad Hoc Equity Committee failed to substantially contribute because they played virtually no role in determining the value of the assets. See id. Thus, the Court allowed an award of professional fees to attorneys hired by the Ad Hoc Convert Committee, but not to those hired by the Ad Hoc Equity Committee. See id. at *3-4.

3. The relevant Bankruptcy Code sections at issue include:

   a. 11 U.S.C. § 327(a) – "Except as otherwise provided in this section, the trustee, with the court's approval, may employ one or more attorneys, accountants, appraisers, auctioneers, or other professional persons, that do not hold or represent an interest adverse to the estate, and that are disinterested persons, to represent or assist the trustee in carrying out the trustee's duties under this title."

   b. 11 U.S.C. § 328(a) – "The trustee, or a committee appointed under section 1102 of this title, with the court's approval, may employ or authorize the employment of a professional person under section 327 or 1103 of this title, as the case may be, on any reasonable terms and conditions of employment . . . ."

   c. 11 U.S.C. § 503(b)(3)(D) – "After notice and a hearing, there shall be allowed, administrative expenses, other than claims allowed under section 502(f) of this title, including . . . the actual, necessary expenses, other than compensation and reimbursement specified in paragraph (4) of this subsection, incurred by . . . a creditor, an indenture trustee, an equity security holder, or a committee representing creditors or equity security holders other than a committee appointed under section 1102 of this title, in making a substantial contribution in a case under chapter 9 or 11 of this title . . . ."

   d. 11 U.S.C. § 503(b)(4) – "After notice and a hearing, there shall be allowed, administrative expenses, other than claims allowed under section 502(f) of this title, including . . . reasonable compensation for professional services rendered by an attorney or an accountant of an entity whose expense is allowable under subparagraph (A), (B), (C), (D), or (E) of paragraph (3) of this subsection . . . ."

Answer Key

Question 10 – Answer 1

Fee Applications
Requirements and Scrutiny by Bankruptcy Court

This hypothetical addresses best practices for preparation of and filing of fee applications. The compensation of professionals retained under 11 U.S.C. § 327 is subject to the review and approval of the Bankruptcy Court. Estate professionals are entitled to "reasonable compensation for actual, necessary services" and "reimbursement for actual, necessary expenses." 11 U.S.C. § 330(a)(1). When reviewing fee applications of estate professionals, courts look to 11 U.S.C. § 330(a) to determine what constitutes "reasonable compensation." 11 U.S.C. § 330(a)(3). That provision directs bankruptcy courts to "consider the nature, the extent, and the value of such services, taking into account all relevant factors, including –

(A) the time spent on such services;

(B) the rates charged for such services;

(C) whether the services were necessary to the administration of, or beneficial at the time at which the service was rendered toward the completion of, a case under this title;

(D) whether the services were performed within a reasonable amount of time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed;

(E) with respect to the professional person, whether the person is board certified or otherwise had demonstrated skill and experience in the bankruptcy field; and

(F) whether the compensation is reasonable based on the customary compensation charged by comparably skilled practitioners in cases other than cases under this title."

11 U.S.C. § 330(a)(3).

Generally, courts will require that professionals demonstrate that their fees and expenses are reasonable and not exorbitant. For example, in <u>In re ACT Mfg.</u>, 281 B.R. 468 (Bankr. D. Mass. 2002), the Bankruptcy Court denied portions of various professionals' fee applications in a Chapter 11 case, including (1) full time spent on fee applications, conflict checks and administrative functions, (2) non-billable time spent pre-engagement, (3) duplicative work performed by an unreasonable number of legal associates, and (4) excessive travel expenses. Further, the Court called on professionals to reduce costs by using electronic transmission devices in lieu of hard copies sent by messenger service. Further, courts have denied portions of professionals' fee applications as overhead costs and not properly compensable, including time spent by summer associates. <u>See</u> <u>In re New Bos. Coke Grp.</u>, 299 B.R. 432 (Bankr. E.D. Mich. 2003); <u>In re Malden Mills Indus.</u>, 281 B.R. 493 (Bankr. D. Mass. 2002). Recently, the

Answer Key

Bankruptcy Court for the Middle District of Pennsylvania in In re Rohrbaugh, No. 1:14-bk-00193-MDF (Bankr. M.D. Pa. Oct. 1, 2014), denied debtor's counsel's motion for reconsideration of a ruling reducing his award of compensation for certain unnecessary and unreasonable fees. For example, the Court held that entries of 6-minute and 12-minute intervals spent listening to and leaving voice mail messages were unreasonable. Rohrbaugh, slip. op. at 3, 11, 12. As grounds thereof, the Court indicated that "[i]n making a fee determination, a bankruptcy court must take into consideration whether the professional exercised 'reasonable billing judgment.'" Id. at 11 (quoting In re Smith, 331 B.R. 622, 628 (Bankr. M.D. Pa. 2005) (citing In re Grosswiler Dairy, Inc., 257 B.R. 523, 528 (Bankr. D. Mont. 2000) and citing In re Mednet, 251 B.R. 103 (9th Cir. B.A.P. 2000)).

Relevant cases discussing best practices for fee applications include the following:

1. In re Energy Partners, Ltd., 2009 WL 2970393 (Bankr. S.D. Tex. 2009) – The Bankruptcy Court declined to amend its previous opinion, which denied two investment banking firms' emergency retention motions, which sought an up-front, nonrefundable fee of $500,000 each. In so doing, the Court characterized the requests as "equat[ing] to being a greedy, arrogant hog . . . ." Energy Partners, 2009 WL 2970393 at *9. The Court found the proposed fees to be "facially exorbitant". Id. at *10.

2. In re Bigler, LP, 422 B.R. 638 (Bankr. S.D. Tex. 2010) – The Bankruptcy Court considered if it should approve an application to employ an investment bank firm which required a "tail fee". The Court emphasized "that it will not approve requested terms of retention merely because the terms are routine in the investment banking community. Greater justification needs to be given to obtain approval." Bigler, 422 B.R. at 640. Unlike Energy Partners, the Court in Bigler approved the retention because the "tail fee" request was supported by sufficient justification to approve the terms of the retention. See id. at 645.

3. In re Aston Baker, 374 B.R. 489 (Bankr. E.D.N.Y. 2007) – The Bankruptcy Court denied portions of an auctioneer's request for reimbursement of legal fees and expenses incurred in connection with an auction of the debtor's real property. Specifically, the Court made adjustments to the fees requested on the grounds that the request included block billing with vague and inadequate time entries and failed to include detailed, specific, itemized documentation of billing.

4. In re Motors Liquidation Co., No. 09-50026, Bench Decision on Pending Fee Issues (Bankr. S.D.N.Y. Nov. 23, 2010) – In this Bench Decision, the Bankruptcy Court ruled that the costs incurred defending fee applications is not necessarily compensable. Nevertheless, the Court noted that it is unfair to penalize professionals for the cost of defending meritless objections and believed that doing so would cause parties to file frivolous objections. The Court determined that it would decide the issue on a case-by-case basis.

Additional relevant authorities include:

<u>**Answer Key**</u>

1. Clifford J. White III, *New Fee Guidelines Enhance Transparency and Promote Market Forces in Billing*, ABI Journal, August 2013, at 22.

2. Profs. Lois R. Lupica and Nancy B. Rapoport, *Best Practices for Working with Fee Examiners*, ABI Journal, June 2013, at 20.

3. Lois R. Lupica and Nancy B. Rapoport, *Final Report of the ABI National Ethics Task Force*, American Bankruptcy Institute (April 21, 2013) at pp. 27-31 (discussing fee application best practices and a framework for pre-approval of terms of retention and compensation under 11 U.S.C. § 328).

4. U.S. Department of Justice, *Guidelines for Reviewing Applications for Compensation and Reimbursement of Expenses Filed Under 11 U.S.C. § 330 for Attorneys in Larger Chapter 11 Cases* (June 11, 2013).

<u>**Question 11 – Answer 1**</u>

Unfinished-Business Rule
Potential Claw-Back of Profits After Law Firm Dissolution

The so-called "unfinished business rule" refers to a cause of action often asserted by trustees of law firms which have filed bankruptcy and are in the process of liquidating. Typically, after a law firm bankruptcy filing, the attorneys of the liquidating firm quickly seek alternate employment, and clients often follow and engage the new firm to complete the unfinished legal work. In those circumstances, trustees of liquidating law firms often allege that the unfinished business of the law firm as of the bankruptcy petition date is an asset of the bankruptcy estate. The trustee then brings claims against the firms now engaged to complete the unfinished legal work. <u>See</u> Paul R. Hage and Patrick R. Mohan, *Is the Unfinished-Business Rule Finished?: Recent Decisions Could Close the Book on Hourly Matters*, ABI Journal, September 2014, at 12 (discussing the history of the "unfinished business rule" and its current status in light of recent decisions limiting its applicability and scope).

The legal theory on which the unfinished business rule rests was first established by the California Court of Appeals in <u>Jewel v. Boxer</u>, 156 Cal. App. 3d 171 (1984). The partnership at issue consisted of four partners who mutually agreed to dissolve their partnership. The partners split into two new partnerships, each taking some of the firm's business. <u>See</u> <u>id.</u> at 175. Disputes arose regarding certain contingency matters which one of the new firms retained and concluded. The California Court of Appeals held that absent a contrary provision in a partnership agreement, a former law firm partner had a duty under the Uniform Partnership Act to account to a dissolved partnership for any profits generated through winding up unfinished partnership business. <u>See</u> <u>id.</u> at 174. Since <u>Jewel v. Boxer</u>, bankruptcy trustees have utilized the theory on behalf of bankruptcy estates with mixed results. <u>See</u> Paul R. Hage and Patrick R. Mohan, *Is the Unfinished-Business Rule Finished?: Recent Decisions Could Close the Book on Hourly Matters*, ABI Journal, September 2014, at 12.

Answer Key

Recent cases discussing unfinished business include:

1. Thelen LLP and Coudert Bros. LLP – After two district courts in New York reached different conclusions regarding the applicability of the unfinished business rule under New York partnership law, the Second Circuit Court of Appeals certified the following two questions to the New York Court of Appeals:

> Under New York law, is a client matter that is billed on an hourly basis property of a law firm, such that, upon dissolution and in related bankruptcy proceedings, the law firm is entitled to the profit earned on such matters as the unfinished business of the firm?
>
> If so, how does New York law define a "client matter" for purposes of the unfinished business doctrine and what proportion of the profit derived from an ongoing hourly matter may the new law firm retain?

See In re Coudert Bros. LLP, 2014 WL 4290547, *1 (2d Cir. September 2, 2014).

The New York Court of Appeals answered the first question in the negative, holding that "pending hourly fee matters are not partnership 'property' or 'unfinished business' within the meaning of New York's Partnership Law. A law firm does not own a client or an engagement, and is only entitled to be paid for services actually rendered." In re Thelen LLP, 2014 WL 2931526, *1 (N.Y. Ct. App. July 1, 2014).

After the New York Court of Appeals issued its decision, the Second Circuit reversed and remanded the Coudert Bros. matter to the district court with instructions to enter judgment for the defendants. Coudert Bros., 2014 WL 4290547 at *1.

2. Heller Ehrman – The dissolution of the firm Heller Ehrman has resulted in multiple decisions on the unfinished business rule and some issues remain pending before the Bankruptcy Court in the Northern District of California at this time. After defaulting on obligations to its lender, Heller Ehrman entered into a dissolution plan which provided for its liquidation and also included a "Jewel waiver". Heller Ehrman v. Davis, Wright, Tremaine LLP, 2014 WL 2609743, *2 (N.D. Cal. June 11, 2014). On appeal, the District Court entered judgment for the defendants because the bankruptcy estate had no property interest in the profits earned by the defendant law firms. See id. The District Court distinguished the Heller case from Jewel both factually and legally. Among other things the Court found Jewel inapplicable because (i) Heller's dissolution was involuntary and, therefore, it had no ability to provide legal services, (ii) clients entered into new engagements with the defendants, (iii) the defendants had no fiduciary duties to the Heller firm, (iv) Heller's matters were hourly fee and not contingency matters, and (v) the partnership law had substantively changed since Jewel was decided. Id. at *4.

3. Howrey LLP – In the Howrey LLP liquidation, the Trustee brought unfinished business actions against firms where Howrey partners departed both prior to firm dissolution and after firm dissolution. In re Howrey LLP, 2014 WL 4435982, *1 (Bankr. N.D. Cal. September 9, 2014). The defendants sought dismissal and urged the bankruptcy court to

follow the recent Heller Ehrman and the Thelen decisions. See id. at *2. Regarding post-dissolution the Court determined that the law at issue (i.e., the District of Columbia) favors application of the unfinished business rule and, therefore, denied the motion to dismiss. Id. at *2-3. The Court did, however, dismiss the fraudulent transfer actions related to the pre-dissolution matters because the matters at issue were not property of the estate as of the petition date. Id. at *3. In addition, the Court found that the pre-dissolution defendants had no duty to provide an equitable accounting regarding unfinished business. Id. at *3-4. Finally, regarding pre-dissolution matters, the Court denied the request to dismiss unjust enrichment claims brought by the Trustee.

Additional relevant authorities include:

1. Paul R. Hage and Patrick R. Mohan, *You Can't Take Them With You:* Coudert Brothers *and the Application of the Unfinished-Business Rule to Dissolved Law Firms*, ABI Journal, August 2012, at 14.

2. Valerie P. Morrison and Dylan G. Trache, Jewel v. Boxer*: The Unfinished Business of Bankruptcy Law Firms*, ABI Journal, April 2012, at 28.

Question 12 – Answer 2

Counsel Risk/POC Issues
Attorney Risk When Signing Client's Proof of Claim Form

Signing the proof of claim is an assertion of personal knowledge and waives the privilege with respect to the representations in the proof of claim. In re Rodriguez, No. 10-70606, AP No. 11-07012, 2013 WL 2450925 (Bankr. S.D. Tex. June 5, 2013).

Discovery will go to facts supporting the claim and whether the attorney was aware of them when claim arose. Questions about legal research and lawyer's thoughts do not have to be answered because they are protected under the work product doctrine.

Don't do it, and don't let client's General Counsel sign the proof of claim. This is an avoidable problem.

The result should not be shocking considering that the Seventh Circuit Court of Appeals has held that "[w]hen information is disclosed for the purpose of assembly into a bankruptcy petition and supporting schedules, there is no intent for the information to be held in confidence because the information is to be disclosed on documents publicly filed with the bankruptcy court." United States v. White, 950 F.2d 426 (7th Cir. 1991).