AMERICAN BANKRUPTCY INSTITUTE

Central States Bankruptcy Workshop 2021

Skills Track

Unlocking Gating Issues in Potential Debtor Engagements

Sponsored by Faegre Drinker Biddle & Reath LLP

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CONCURRENT SESSION

2021

Unlocking Gating Issues in Potential Debtor Engagements

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Issues To Be Discussed

1) Getting Retained

2) Getting Paid

3) Authority to File

4) Walking Away From a Potential Engagement

GETTING RETAINED

Analyzing Conflicts:
A Necessity for Every Lawyer

Hypothetical #1

New Client (the buyer) asks you to document a transaction where all the terms already have been negotiated. The seller is a corporate client that you also represent, but not in this particular transaction.

- Do you need a conflict waiver in order to handle the engagement for New Client?

Hypothetical #2

Firm Client approaches you to defend it in litigation. The conflict check reflects that plaintiff is a current client of the firm in transactional matters, which you have never worked on.

- Do you need a conflicts waiver in order to take on the new engagement for Firm Client?

Analyzing Conflicts: A Necessity for Every Lawyer

Hypothetical #3

Current Client asks you to defend it in intellectual property litigation brought by Competitor. The conflict report reflects that Firm represented Competitor in intellectual property litigation that ended in 2016.

- Can you take the new engagement for Current Client without a conflict waiver?
- Does your answer change if the litigation ended in 2012? 2007?

Hypothetical #4

You make a pitch to represent Prospective Client in "bet the company" litigation brought against it. Prospective Client decides to hire another firm. Current Firm Client gets served with the complaint as a co-defendant in the same case.

- Can you can take the matter for Current Firm Client?

In re Boy Scouts of America, et al., Case No. 20-10342 (LSS) (Bankr. D. Del. May 29, 2020) (Docket No. 755)

FACTS:

- October 2018- Century retains Sidley re: reinsurance re: Boy Scouts of Americas ("BSA").
- August 2019- Sidley is retained to represent the BSA re: restructuring matters.
- January 2020- Sidley informs Century it is withdrawing from all representations of Century.
- February 18, 2020- BSA files for chapter 11. Century objects to Sidley's retention.

Century's Argument:

Sidley could not satisfy the requirements of Section 327 because it had violated Rule 1.7 by representing two current clients (Century and BSA), without getting a waiver from both parties.

Sidley's Argument:

- Rule 1.9, not Rule 1.7, controls because Century is a former client. As a former client, no waiver was required because the restructuring work is not substantially related to Sidley's previous representation of Century on reinsurance matters.
- Sidley does not represent an adverse interest and is disinterested.
- BSA retained Haynes & Boone to represent it on all insurance matters related to its restructuring and as such Sidley was never adverse to Century.

BSA's Argument

- BSA would be substantially prejudiced if they had to retain new counsel.

Section 3.27(a)- No Violation

- The two-part test in Section 327 is written in the present tense. Representation had ended.

Substantially Related- Maybe but

- Haynes and Boone was handling all insurance matters
- Sidley had an ethical screening wall
- Left for arbitration whether Sidley had violated the Professional Rules of Conduct by representing BSA and Century before the ethical screen was established.

On April 6, 2021 the District Court affirmed the decision.

Maxus Liquidating Trust v. YPF, et al., Case No. 18-50489 (CSS) (Bankr. D. Del. April 6, 2021) (Docket No. 389)

Facts:

- Since its formation, the Trust's lead counsel has been White and Case.
- YPF had been previously been represented by Sidley Austin.
- Jessica Boelter, who was previously a partner at Sidley, lateralled to White and Case on October 1, 2020.
- An ethical screen was implemented on the day Ms. Boelter joined White and Case.
- YPF took the position that due to Ms. Boelter's extensive involvement in the adversary proceeding on behalf of YPF no screen would be adequate. YPF filed a motion to disqualify White and Case.

White and Case fully complied with Rule 1.10(a)(2)

- Ethical screen
- No fees paid to Ms. Boelter
- YPF provided notice of screening procedures

Not an exceptional case for which an ethical screen was insufficient.

- Hours billed (a few hundred) v. amount sought in adversary proceeding ($14 billion).
- Ms. Boelter was not a key strategic advisor who was privy to the deepest and darkest YPF secrets.

On April 21, 2021 YPF appealed the decision.

GETTING PAID

How do you get paid by insolvent clients?

- Ideally, in *advance*.
- "Retainer" is not a helpful term
- Know the rules: Rule 1.5

Model Rule and Different State Approaches to Advance Fees

- Minnesota
- Louisiana
- Delaware
- Illinois – “Dowling” interpretation
- Wisconsin – “the cheese stands alone”

Bankruptcy Code and Rules

- Section 329
- Rule 2016(b)
- Form 2030B
- Statement of Financial Affairs

Issues in consumer bankruptcy cases

- Fee Applications
- Bifurcation of Chapter 7 Fees

AUTHORITY TO FILE

Eligibility to File

For an entity to file for bankruptcy relief, it must be eligible under the Bankruptcy Code or the case could be subject to dismissal.

Any "person" may file a bankruptcy. *See* 11 U.S.C. § 109(a).

A person can be an individual, partnership or corporation. *See* 11 U.S.C. § 101(41).

A "corporation" includes, among other things, a "partnership association organized under a law that makes only the capital subscribed responsible for the debts of such association", and an "unincorporated company or association". *See* 11 U.S.C. § 101(9)(A).

An LLC is not specifically included in the definition of "person" or "corporation", but is generally recognized as a person and corporation eligible for relief under the Bankruptcy Code.

Dissolved Entities

Consult state law to determine if the entity continues its legal existence and/or can wind down its affairs after dissolution.

- If state law permits a dissolved entity to wind up and liquidate its business and affairs, it may still have the authority to file bankruptcy.
- If state law permits a dissolved entity to liquidate but not to reorganize, a chapter 11 reorganization may not be permissible.

Authority to File

The Bankruptcy Code does not expressly address corporate authority to file a voluntary bankruptcy case – it simply states that only an entity that may be a debtor may commence a voluntary bankruptcy case. See 11 U.S.C. § 301(a).

The authority to file is controlled by state law governing the business entity. *Price v. Gurney*, 324 U.S. 100, 106 (1945). The filing of a bankruptcy by an entity must be properly authorized or the bankruptcy court lacks jurisdiction over the entity, and the petition must be dismissed. *Id*. at 106-107. The initiation of bankruptcy proceedings is controlled by those who have the power of management. *Id*. at 104.

This precept of law operates in all corporate cases, including cases filed by an LLC.

The entity's governing documents and controlling state law generally directs this analysis.

Who is Authorized

- Limited Liability Companies
  - Not generally addressed by state law, so review terms of the LLC's governing documents.
  - Note that if the single member of an LLC files a chapter 7 bankruptcy, his/her trustee may be the only person with authority to put the LLC into bankruptcy.
- Corporations
  - Power generally rests with board of directors.
  - To determine whether a bankruptcy petition is a valid corporate action, a court may examine the articles of incorporation, bylaws, corporate resolutions, board meeting minutes, and state law.
  - Any corporate resolution authorizing a voluntary bankruptcy petition must originate at a validly held meeting of directors and be approved by the proper number of such directors.
- Partnerships
  - 11 U.S.C. § 303(b)(3)(A) provides that an involuntary bankruptcy case against a general partnership may be commenced by fewer than all of the general partners, but there is no counterpart provision regarding the commencement of a voluntary case by a general partnership. See Advisory Committee Notes to Bankruptcy Rule 1004.
  - Review applicable state law or the governing partnership documents.
  - Note that a bankrupt general partner might not have the authority to put the partnership into bankruptcy under applicable state law.

Ratification

If the entity's bankruptcy petition was not properly authorized, ratification of the filing by those with authority, depending on the circumstances, may save the case from dismissal.

Acts which may constitute ratification can include, e.g., participating in the case without or before objecting to the filing, a subsequent vote and resolution of the board of directors, or consent resolution of the required amount of owners.

But relying on post-filing ratification to authorize the filing after the fact is risky.

In re Zaragosa Properties, Inc., 156 B.R. 310, 313 (Bankr. M.D. Fla. 1993);

In re Stavola/Manson Elec. Co., Inc., 94 B.R. 21, 24-25 (Bankr. D. Conn. 1988).

The Right to File

Pre-Bankruptcy Waivers & Bargaining Away Corporate Control

The right to file a bankruptcy case is a fundamental right that cannot be waived, although this notion is not specifically expressed anywhere in the Bankruptcy Code.

Bankruptcy courts generally don't enforce contractual provisions that prohibit an entity from seeking bankruptcy relief due to being against federal public policy.

However, pre-bankruptcy restrictions in an entity's governing documents regarding bankruptcy rights can sometimes be enforceable. For example, where the governing document gives a lender an explicit voice in the entity's filing of a bankruptcy petition, it may be enforced if the lender is acting in its capacity as a member/owner instead of a creditor.

Receiverships

Sometimes a court removes officers and directors of an entity from their positions and vests their authority in a receiver, and that receiver may then have the ability to file a bankruptcy petition on behalf of the entity.

Whether the receiver has sole authority to put the entity into bankruptcy may be dependent on whether the receivership order places the receiver in control of the operations and management of the entity itself, and not just the entity's property.

In most instances, neither a state court injunction nor the pendency of a state receivership can bar the filing of an otherwise permitted bankruptcy due to the grant of the exclusive bankruptcy jurisdiction to the federal courts and the constitutional principle of supremacy.

The receiver may be considered a "custodian" under 11 U.S.C. § 101(11), and required to deliver property in his or her possession, custody or control to the trustee and file an accounting of any property that had come into his or her possession under 11 U.S.C. § 543.

WALKING AWAY FROM A POTENTIAL ENGAGEMENT

Who is My Client? Who is Not My Client?

Debtor-in-Possession ("DIP")	-DIP must fulfill rights, powers, and duties of trustee 11 U.S.C. § 1107 -Attorney represents the DIP
Closely held members or shareholders of DIP	-Not client
Creditors	-Not client: but may owe some degree of duty to creditors
Bankruptcy Estate	-Not client: but attorney owes a fiduciary duty to the Estate
Court	-Not client: but duty of candor

Fiduciary Duties of the Debtor-in-Possession

DIP must operate its business while maintaining a fiduciary obligation to its creditors

- -Duty of loyalty and good faith
- -No self-dealing or operations to further private interest

Duty of loyalty extended to directors/officers of DIP to pursue interests of DIP rather than individual's financial or other interests

Fiduciary Duty of DIP Counsel to Creditors

Courts have generally held that DIP counsel generally owes no fiduciary duty to creditors

However....

Part of DIP counsel's fiduciary obligation is to act in the best of the Estate – which includes creditors

Fiduciary Duty of DIP Counsel to Estate

DIP Counsel must balance role as counselor to debtor along with role of officer of court and fiduciary duty to Estate – upon conflict the Estate and Court win

DIP Counsel must advise DIP of its responsibilities under the Code and ensure DIP's compliance

Duties of DIP Counsel

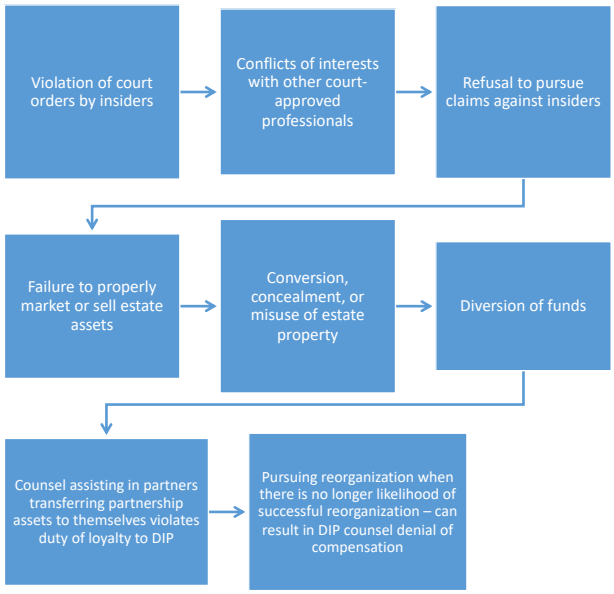
Monitor case and encourage conversion or dismissal with reorganization is not feasible or wrongdoing is taking place. *In*	Duty to disclose debtor's diversion of DIP funds.	Duty to inform Court of DIP breach of fiduciary duties to Estate and creditors.
Duty to maximize the Estate.	Duty to exercise independent professional judgment and disclose any conflicts of interest with Estate.	Supervise sale of property and advise professionals of responsibilities and necessary disclosures.

But wait….

- **Some courts have held that DIP Counsel does NOT owe a fiduciary duty to the Estate or its beneficiaries – fiduciary duty is on DIP**

  -*Hansen, Jones & Leta, P.C. v. Segal,* 220 B.R. 434 (D. Utah 1998).

Reportable Misconduct Examples



Faculty

Rachel L. Hillegonds is senior counsel with Miller, Johnson, Snell & Cummiskey, P.L.C. in Grand Rapids, Mich., and is a member of its Business Section, Bankruptcy – Creditors'/Debtors' Rights and Real Estate practice groups. She has been practicing law since 2004. Ms. Hillegonds represents a variety of clients in bankruptcy-related matters, including secured and unsecured creditors, chapter 7 and 11 trustees, chapter 7 nonconsumer and chapter 11 debtors, and creditors' committees. She has defended numerous preference claims brought against creditors in local bankruptcy cases, as well as cases filed in other jurisdictions around the country, and she has represented banks, lessors and lessees, litigants and other creditors in seeking relief from the automatic stay and otherwise protecting their rights, collateral and interests in chapter 7, 11, 12 and 13 cases. Ms. Hillegonds has helped individuals and companies file for bankruptcy protection and navigate through liquidations and reorganizations. She has also assisted bankruptcy trustees in operating chapter 11 cases, and in recovering assets for the benefit of creditors in both chapter 7 and 11 cases. Ms. Hillegonds also has assisted clients in out-of-court workout, receivership and other insolvency matters. For example, she has filed claims for and represented creditors in receiverships, has assisted clients in negotiating forbearance agreements and settlement of debts in an effort to avoid bankruptcy, and has counseled clients in winding down business operations, including matters relating to company debt and the outstanding personal liabilities of business owners. She also has helped clients with residential and commercial real estate acquisitions and sales, eviction and other tenant matters, drafting, reviewing and terminating leases, foreclosures, condominium association documents and navigating unit owner problems, resolving zoning, easement and land use issues, and other real estate matters. Ms. Hillegonds was previously a staff attorney for Chapter 13 Trustee Mary Viegelahn. She is a member of ABI and the Turnaround Management Association, Federal Bar Association for the Western District of Michigan, Grand Rapids Bar Association and State Bar of Michigan. She currently serves on the programming committee for the Turnaround Management Association's West Michigan chapter, and she previously served as the secretary and a member of the FBA Bankruptcy Section steering committee for the Western District of Michigan, and as chair, vice chair, treasurer and board member of its West Michigan chapter. Ms. Hillegonds received her undergraduate degree *cum laude* in 1999 from Hope College and her J.D. *cum laude* in 2004 from Valparaiso University School of Law.

J. David Krekeler is the founder and principal shareholder of Krekeler Strother, S.C. in Madison, Wis., and devotes his practice to debtor/creditor and bankruptcy matters, including the representation of debtors, creditors and even bankruptcy trustees in cases under chapters 7, 11, 12 and 13. He also serves as a receiver in both supplemental and chapter 128 proceedings. Mr. Krekeler is a member of both the Creditor's Rights section and the Bankruptcy and Insolvency section of the Wisconsin State Bar. He is Board Certified in Business Bankruptcy Law by the American Board of Certification. Mr. Krekeler is a past chairman of the Western District Bankruptcy Bar and a member of the National Association of Retail Collection Attorneys. He frequently teaches on debtor/creditor matters and is a past instructor at the University of Wisconsin Law School Lawyering Skills Program. He also trains mediators for the Farm Mediation Program administered by the Department of Agriculture, Trade, and Consumer Protection, and serves on the Department's Consumer Protection Advisory Council. Mr. Krekeler has been listed in *The Best Lawyers in America* every year since 2007, voted one of Madison's Best Bankruptcy Lawyers as published in *Madison Magazine*, and named a Wisconsin Super Lawyer in bankruptcy as published by *Milwaukee Magazine* and *Wisconsin Super Lawyers*

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Evelyn J. Meltzer is a partner with Troutman Pepper Hamilton Sanders LLP in Wilmington, Del., where she focuses her practice on corporate restructuring, bankruptcy and creditors' rights. She provides advice to clients regarding the risks, benefits, challenges and opportunities available in restructuring proceedings, and she has experience representing debtors, creditors' committees, asset-purchasers, landlords, liquidating and litigation trusts, assignees in assignments for the benefit of creditors (ABC), receivers, secured and unsecured creditors, and shareholders in bankruptcy proceedings. Ms. Meltzer has experience serving as counsel for both the debtor and creditor side in bankruptcy-related litigation matters. She is frequently invited to write and speak about current bankruptcy and insolvency issues. Ms. Meltzer is AV-rated for Ethical Standards and Legal Ability by Martindale-Hubbell and co-chairs ABI's Asset Sales Committee. She received the 2016 Melnik Award for an Exceptional IWIRC Member and is admitted to practice in Pennsylvania and Delaware. Ms. Meltzer received her B.A. in political science from Drew University in 1998 and her J.D. in 2001 from Northwestern University School of Law.

Craig E. Stevenson is an equity partner at DeWitt LLP in Madison, Wis., where he practices in the areas of creditors' rights, business bankruptcy and litigation. He represents debtors and creditors in all chapters of bankruptcy, receiverships, workouts, and state and federal litigation, and he handles bankruptcy appeals before the district and circuit courts. As debtor's counsel, Mr. Stevenson has assisted various types of businesses, including dealerships, manufacturers, retailers, restaurants, hotels and farms, as well as individuals, in chapter 11 and 12 cases. He also has handled many complex cases for individuals under chapters 7 and 13, and represents the rights of secured and unsecured creditors in both bankruptcy and nonbankruptcy matters. Mr. Stevenson is a regular presenter at a number of seminars, including those hosted by ABI and the State Bar of Wisconsin. He currently serves on the board of the Bankruptcy, Insolvency and Creditors' Rights Section of the Wisconsin State Bar, and is a past chair of the Western District of Wisconsin Bankruptcy Bar Association. Mr. Stevenson received his B.B.A. *cum laude* from DePauw University and his J.D. from the University of Wisconsin Law School.