APRIL 12, 2011
DELAWARE INN OF COURTS PRESENTATION:

SO, YOU WANT TO BE AN ESTATE PROFESSIONAL?[1]

A/K/A "LAWYERS, GUNS AND MONEY!"[2]

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1 Edited by Larry Kotler and Robert Mallard.

2 "I was gambling in Havana, I took a little risk, Send lawyers, guns and money, Dad, get me out of this." From the song "*Lawyers, Guns and Money*" by Warren Zevon, 1978.

I. STANDARDS FOR RETENTION OF PROFESSIONALS:[3]

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3. What is a "disinterested person?" and
4. 11 U.S.C. § 327(e) and "special counsel."

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   a. What are "reasonable terms and conditions of employment?"

D. "Jay Alix" Protocol:

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[3] The materials and accompanying presentation were prepared by Sommer Ross, Jeffrey Drobish, Kimberly Brown, Aaron Stulman, Marla Eskin, Joseph McMahon, Richard Riley and Steven Kortanek.

E. "Ordinary Course" Professionals:

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B. Case Summaries:

1. *In re AbitibiBowater, Inc.*;
2. *In re Trico Marine Services, Inc.*;

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[4] The materials and accompanying presentation were prepared by Donna Harris, Russell Silberglied, Cory Kandestin, Kathleen Murphy, Marc J. Phillips and Timothy Reiley.

3. *In re Agent Orange Product Liability Litigation MDL No. 381*;

4. *Miller v. Sun Capital Partners (In re IH-1, Inc.)*;

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1. *In re PWS Holding Corp.*, 228 F.3d 224 (3d Cir. 2000);

2. *In re Washington Mutual*, Ch. 11, Case No. 08-12229;

3. *In re Metromedia Fiber Network, Inc.*, 416 F.3d 136 (2d Cir. 2005);

4. *In re Motor Liquidation Co.*, 2011 Bankr. LEXIS 684 (Bankr. S.D.N.Y. March 7, 2011);

5. *In re Pilgrim's Pride*, 2010 Bankr. LEXIS 72 (Bankr. N.D. Tex. Jan. 14, 2010); and

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[5] The materials and accompanying presentation were prepared by Yosef Ibrahimi, Howard Cohen, Evelyn Meltzer, Natalie Ramsey, John Schanne, Michael Custer, and Joseph Argentina.

6. *In re Lowenschuss*, 67 F.3d 1394 (9th Cir. 1995).

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1. Case Summary: *Miller v. Sun Capital (In re IH 1, Inc., et al.)*, 441 B.R. 742 (Bankr. D. Del 2011);

C. Class Gifting/Plan Trust Issues.[7]

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[6] The materials and accompanying presentation were prepared by Ronald Gellert, Lisa Coggins, Shelley Kinsella, Henry Jaffe, Jane Leamy and Zeke Allison.

[7] The materials associated with the Class Gifting/Plan Trust discussion will be handed out at the April 12, 2011 presentation.

STANDARDS FOR RETENTION OF ESTATE PROFESSIONALS AND ISSUES REGARDING SAME

Standards for Retention of Professionals

Retention of Debtor Professionals

- Bankruptcy Code section 327(a) provides for the retention of counsel by a trustee or the debtor.
  - Specifically, section 327(a) states:

    "the trustee [or the debtor], 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 [or debtor] in carrying out the trustee's [or debtor's] duties under this title."

Adverse Interest

- Under Third Circuit precedent, section 327(a) mandates disqualification where there is an actual conflict of interest, but gives the Bankruptcy Court broad discretion in disqualifying an attorney where a potential conflict exists.
  - *See, e.g., In re Jade Mgmt. Servs.*, 386 Fed. Appx. 145, 148 (3d Cir. 2010); *In re Pillowtex, Inc.*, 304 F.3d 246, 251-52 (3d Cir. 2002); In *re Marvel Entm't Group, Inc.*, 140 F.3d 463, 477 (3d Cir. 1998).

- The Third Circuit has explained that "[d]istinguishing between potential and actual conflicts is a flexible enterprise, and necessarily is one that is governed by the factual niceties of each particular case. Generally, however, a conflict is actual, and hence per se disqualifying, if it is likely that a professional will be placed in a position permitting [him or her] to favor one interest over an impermissibly conflicting interest." *In re Jade Mgmt. Servs.*, 386 Fed. Appx. at 148 (internal quotations and citations omitted).

Disinterested Person

- Bankruptcy Code section 101(14) defines a "disinterested person" as a person that

  (A) is not a creditor, an equity security holder, or an insider;

  (B) is not and was not, within 2 years before the date of the filing of the petition, a director, officer, or employee of the debtor; and

  (C) does not have an interest materially adverse to the interest of the estate or of any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor, or for any other reason.

Retention of Committee Professionals

- Bankruptcy Code section 1103 provides for the retention of professional persons by a committee. Specifically, section 1103(a) states that:
  - "At a scheduled meeting of a committee appointed under section 1102 of this title, at which a majority of the members of such committee are present, and with the court's approval, such committee may select and authorize the employment by such committee of one or more attorneys, accountants, or other agents, to represent or perform services for such committee."

- Further, section 1103(b) provides that:
  - "An attorney or accountant employed to represent a committee . . . may not, while employed by such committee, represent any other entity having an adverse interest in connection with the case. Representation of one or more creditors of the same class as represented by the committee shall not per se constitute the representation of an adverse interest."

Retention of Special Counsel

- Bankruptcy Code section 327(e) provides for the retention of special counsel. Specifically, section 327(e) states that:
  - "The trustee [or the debtor], with the court's approval, may employ, for a specified special purpose, other than to represent the trustee [or the debtor] in conducting the case, an attorney that has represented the debtor, if in the best interest of the estate, and if such attorney does not represent or hold any interest adverse to the debtor or to the estate with respect to the matter on which such attorney is to be employed."

STANDARDS FOR PROFESSIONAL COMPENSATION

Section 330 v. Section 328

11 U.S.C. § 330

- Section 330 of the Bankruptcy Code provides that bankruptcy courts may award "reasonable compensation for actual, necessary services" and authorizes "reimbursement for actual, necessary expenses." 11 U.S.C. §330(a)(1).
- Hindsight review: fees are to be applied for *after* a professional has rendered the relevant services.

11 U.S.C. § 330

- In determining the amount of reasonable compensation to be awarded to a professional person, courts shall consider the nature, the extent, and the value of such services, taking into account all relevant factors.

Section 330 "Reasonable" Factors

- time spent;
- rates charged;
- whether the services were necessary to the administration of, or beneficial at the time at which the service was rendered ;
- 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;

Section 330 "Reasonable" Factors

- whether the person is board certified or otherwise has demonstrated skill and experience in the bankruptcy field; and
- 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).

11 U.S.C. § 328

- If a professional desires some assurance that it will be paid according to its fee arrangement with its client and not have its fees subject to a subsequent determination as to the "necessity" and "reasonable value of its services" under § 330, it may apply for approval of its fee arrangement under section 328 of the Bankruptcy Code

11 U.S.C. § 328

- "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*, including on a retainer, on an hourly basis, on a fixed or percentage fee basis, or on a contingent fee basis. Notwithstanding such terms and conditions.
  11 U.S.C. § 328(a) (emphasis added).

PRACTICE TIPS

- How a court determines reasonableness under §330(a)(3) depends on how a professional was initially retained by the court.
- Engagement Letter, Retention Application and Retention Order may specify review under §328(a) or §330. Court is bound by those standards unless stating under what section review will occur in the retention order – craft documents carefully!

[redacted]

- You must explicitly say that the payment of fees are not subject to review under §330 – failure to do so means that the fees will be reviewed for reasonableness by the court.
- U.S. Trustee likely to object to maintain "reasonableness" review.
- Approval of section 328 applications with caveat -- allowing some "back-end" review under section 330 appears to make courts more comfortable in approving a fee arrangement.

Jay Alix Protocol

Jay Alix Protocol

- General Background:
  - Refers to the terms of an agreement reached between the United States Trustee for the District of Delaware and Jay Alix & Associates in the *Safety-Kleen* bankruptcy case in 2001.
  - Recognizes an inherent conflict between duties of an advisor and the duties of staff serving as officers of the debtor.
  - For this reason, the Jay Alix Protocol precludes an advisory firm from acting in both capacities in a single bankruptcy case (the "one hat" policy).

Jay Alix Protocol

- Scope
  - Covers engagements where individuals are to serve as
    - Chief Executive Officers,
    - Presidents,
    - Chief Operating Officers,
    - Chief Restructuring Officers,
    - Chief Information Officers, etc., or
    - any officer provided for in a debtor's bylaws

Jay Alix Protocol

- Specific Terms - "One Hat" Policy
  - Advisor cannot seek to be retained as more than one of the following in the same case:
    - crisis manager retained under Sec. 363,
    - financial advisor retained under Sec. 327,
    - claims agent/claims administrator or
    - an investor/acquirer.
  - After accepting an engagement in one of these capacities, an entity is prohibited from accepting another engagement for the same or affiliated debtors in another capacity.

Jay Alix Protocol

- Specific Terms - Retention & Reporting
  - Retention to be sought under Sec. 363
  - Must disclose names and positions of officers and temporary staff
  - Persons serving as officers must be approved by independent board
  - Must disclose, *inter alia*, potential conflicts/relationships & prior history w/ debtor, including any prepetition involvement in decision to engage the advisor
  - Must file a monthly staffing report, including disclosure of full- and part-time status

Jay Alix Protocol

- Specific Terms - Compensation
  - Fee applications not required, but –
  - Quarterly reports of compensation earned must be filed and made subject to objections ("negative notice" procedure)
  - "Success fees or other back-end fees shall be approved by the Court at the conclusion of the case on a reasonableness standard and shall not be pre-approved under section 328(a)."

Jay Alix Protocol

- Specific Terms – Other Restrictions
  - Indemnification permitted only to the extent and on terms provided to other officers of debtor
  - For a period of three years after the conclusion of the engagement, any affiliated investor shall not make investments in the debtor or reorganized debtor

DEBTORS' RETENTION OF ORDINARY COURSE PROFESSIONALS

OCP RETENTION

- Ordinary Course Professionals ("OCP") are those professionals that assist the Debtors and their business in the ordinary course (attorneys, accountants, consultants); normally do not provide bankruptcy services
- A "First Day" OCP Motion is common to authorize the continued retention and payment of OCP; however, retention under 327 is not required. *See* Elastead v. Nolden

OCP RETENTION

(In re That's Entm't Mktg. Group), 168 B.R. 226, 230-231 (N.D. Cal. 1994) (only retention of professionals whose duties are central to administration of estate requires prior court approval under section 327); In re Madison Mgmt. Group, Inc., 137 B.R. 275, 283-84 (Bankr. N.D. Ill. 1992) (same); In re Riker Indus., Inc., 122 B.R. 964-973 (Bankr. N.D. Ohio 1990) (no need for section 327 approval of fees of

OCP RETENTION

Management and consulting firm that performed only "routine administrative Functions" and whose "services were not central to [the] bankruptcy case"); In re D'Lites of Am., Inc., 108 B.R. 352, 355 (Bankr. N.D. Ga. 1989) (section 327 approval not necessary for "one who provides services to debtor that are necessary regardless of whether petition was filed"); In re Fretheim, 102 B.R. 298, 299 (Bankr.

OCP RETENTION

D. Comm. 1989) (only those professionals involved in the actual reorganization effort, rather than debtor's ongoing business, require approval under section 327); In re Pacific Forest Indus., Inc., 95 B.R. 740, 743 (Bankr. C.D. Cal. 1989) (same); In re Babcock Dairly Co., 70 B.R. 691, 692-93)Bankr. N.D. Ohio 1987) (holding that an expert witness was not a "professional person" under section 327 because his

OCP RETENTION

testimony did not measurably affect the Administration of the estate); In re Johns-Manville Corp., 60 B.R. 612, 619 (Bankr. S.D.N.Y. 1989) (only those professionals involved in the actual reorganization effort, rather than debtor's ongoing business, require approval under section 327.

Commonalities

- Notice of disinterestedness to be filed. Normally includes summary of services to be provided.
- OCP may hold prepetition claims. Such a claim does not necessarily render the OCP materially adverse to the debtor.
- If approved, Debtors may pay 100% of fees to each OCP without court approval (i.e. fee applications generally not required)

Commonalities

- OCP Caps – either monthly and/or in the aggregate. If the OCP exceeds the cap, a formal fee application is necessary and it will be subject to 330 review
- Supplemental OCP lists permitted. Debtors may add/remove OCPs at their discretion.
- Periodic disclosure of amounts paid to OCP typical.

Retention Applications

Applications Generally

- The Debtor and Committees must file Applications for Retentions for all Professionals. 11 U.S.C. §327(a).
- A Debtor seeking to employ professional not used to administer the case by filing a Motion to Engage an Ordinary Course Professional.
- The application must be in compliance with 11 U.S.C. 330.

Rule 2014 - Disclosure

Bankruptcy Rule 2014 requires that the application state:

- specific facts showing the necessity for employment;
- name of the person to be employed;
- reasons for the selection;
- the professional services to be rendered;
- any proposed arrangement for compensation; and

Rule 2014 - Disclosoure

- to the best of the applicant's knowledge, all 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.

Rule 2014 - Disclosure

The application must be accompanied by a verified statement of the person to be employed setting forth 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.

Disqualification

- Where actual conflict of interest exists
- Where professional is not disinterested 11 U.S.C. §101(14)

Retention Process

Debtor

- Board Approval – the Petition should include a board resolution authorizing the filing of the case and the engagement of professionals.
- Engagement letter – complying with Delaware requirements.
- Application – includes affidavit in support of application pursuant to Section 327(a); sign by Debtor; statement under Rule 2016; 2014 disclosures.

Debtor

- U.S. Trustee Approval – The U.S. Trustee monitors employment applicants and may file objections. 28 U.S.C. 586(a)(3)(A).
- Court Approval

Committees

- "Pitch" – Professionals seeking to be employment by the committee may meet with the committee members after selection.
- Application – signed by Committee Chair; affidavit in support of application pursuant to Section 327(a); 2014 disclosures.
- U.S. Trustee Approval – The U.S. Trustee monitors employment applicants and may file objections. 28 U.S.C. 586(a)(3)(A)
- Court Approval

United States Trustee Guideline

United States Trustee Guidelines

- The U.S. Trustee Fee Guidelines can be found on the website U.S. Trustee Program website www.justice.gov/ust/.
- The Guidelines focus on the disclosure of information relevant to a proper award under the law and reflect the requirements in 11 U.S.C. 330 and Rule 2016.

United States Trustee Guidelines

- Factors considered in evaluating fees include: whether the services were necessary to the administration of, or beneficial towards the completion of the case at the time they were rendered; whether services were performed within a reasonable time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed; and whether compensation is reasonable based

United States Trustee Guidelines

on the customary compensation charged by comparably skilled practitioners in non-bankruptcy cases.

- The Guidelines set for the information that should be contained in the application.
- The Guidelines attach the Project Categories for billing.

CONFLICT COUNSEL AND ISSUES REGARDING SAME

ISSUES CONCERNING CONFLICTS COUNSEL: FACT PATTERN

Two debtors filed on the same date. Parent-debtor owns 75% of the stock of Sub-debtor. Parent-debtor has two of its directors sitting on the board of Sub-debtor, with the effect that it controls 2/3 of the board's vote. Numerous individual shareholders own the remaining 25% of the stock of Sub-debtor. The remaining board member of Sub-debtor is the CEO of Sub-debtor. CEO signed the bankruptcy petitions and has authority to make ordinary course decisions on behalf of Sub-debtor with respect to the bankruptcy case.

Two affiliates of the debtors did not file for bankruptcy. The first is an operating wholly owned subsidiary of Parent-debtor. The second is a company that is wholly owned by Sub-debtor. All four entities (the two debtors and the two non-debtors) were represented by the same attorneys prior to the Petition Date.

Sub-debtor had loaned $2 million to Parent-debtor nine months prior to the Petition Date. The loan was documented, but Parent-debtor had never made any payments with respect to the loan, either principal or interest. Certain minority shareholders have stated that the loan constitutes a breach of Sub-debtor's fiduciary duties, and caused Sub-debtor to become insolvent. Although the loan documents were drafted by the same pre-petition attorneys that represented all of the affiliates, Parent-debtor and Sub-debtor each signed conflict waivers. A studious associate at the firm has raised the issue of whether Sub-debtor should engage conflicts counsel on matters involving the loan and the minority shareholders.

On the Petition Date, Parent-debtor and Sub-debtor sought to hire the firm it had been using previously as its bankruptcy counsel. That firm disclosed in its retention application that it currently represents the two non-debtor affiliates, although different individuals are working on the non-debtors' business matters than are working on the bankruptcy cases. It is not clear as of the Petition Date whether the non-debtors are creditors of either of the debtors. The OUST has filed an objection to the firm's retention application on the basis that it cannot represent both the debtor and non-debtor affiliates simultaneously.

Bankruptcy counsel further disclosed that it represents a few other creditors, including Widget Corp. Widget Corp. is s significant creditor of Sub-debtor, but the amounts owed are just short of placing Widget Corp. on Sub-debtor's list of Top 20 creditors. Two months after the Petition Date, Widget Corp. asserts a reclamation demand, and files a motion for immediate payment of administrative claim. Widget Corp. further asserts in its motion that debtor's counsel must recuse itself from the matter due to the conflict.

During the bankruptcy case, CEO instituted a sales incentive program to provide bonuses to certain employees if they reached specific sales goals. CEO is entitled to receive bonuses under this program. The program is similar to a pre-petition program that was in place, in which CEO, CFO and other officers received significant bonuses within the one year before the bankruptcy filing. CEO does not want to retain separate counsel to address these matters, and instead wants to rely on debtor's counsel.

ISSUES CONCERNING CONFLICT COUNSEL: CASE SUMMARIES

1. *In re AbitibiBowater, Inc.*, Case No. 09-11296-KJC (Bankr. D. Del.)

Issue: Aurelius Capital Management, LP and Contrarian Capital Management, LLC (collectively, the "Objectors")[1] objected (D.I. 2427) to the Debtors' application (the "Application") (D.I. 2301) to employ a certain special advisor ("Advisor") for debtor Bowater Canada Finance Corporation ("BCFC").[2] Specifically, the Objectors alleged that BCFC had issued certain unsecured notes (the "Notes") guaranteed by Bowater Incorporated ("Bowater"). The Objectors averred that the Notes constituted BCFC's only material liabilities and that BCFC's only material assets were claims against its codebtors, BCFC's board of directors and BCFC's officers. Because BCFC was a financing vehicle without access to cash, the Application had provided that Bowater would fund Advisor's fees and expenses. Accordingly, the Objectors contended that, pursuant to the Application, Advisor would not be charged with maximizing the value of the BCFC estate.

Result: On June 22, 2010, the Court requested certain modifications to the proposed order and overruled the Objectors' remaining objections to the Application. Specifically, pursuant to the Court's order (D.I. 2614), Advisor was charged with, *inter alia*, (i) investigating claims against BCFC's board of directors; (ii) determining whether conversion of BCFC's case to chapter 7 was appropriate and in BCFC's best interests; and (iii) investigating causes of action related to the Notes.

2. *In re Trico Marine Services, Inc.*, Case No. 10-12653-BLS (Bankr. D. Del.)

Issue: The Debtors filed certain applications (the "Applications") to retain certain counsel. The Official Committee of Unsecured Creditors (the "Committee") objected (D.I. 230) to the Applications due to certain counsel's having previously represented the firm *and* certain non-debtor subsidiaries. *See also* D.I. 231 (joinder of the Second Lien Noteholders to the Committee's limited objection). The Debtors responded that the situation did not represent an impermissible conflict *per se*. *See* D.I. 241. Rather, the Debtors stated, appropriate action should be taken at the time that such conflicts actually arose.

Result: The Court overruled the objections and granted the Applications. *See* D.I. 262, 263 and 264.

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[1] Each defined term herein is defined only with respect to a particular case summary.

[2] Wilmington Trust Company also objected to the limited scope of Advisor's retention. *See* D.I. 2425.

3. *In re Project Orange Associates, LLC*, 431 B.R. 363 (Bankr. S.D.N.Y. 2010)

Issue: Prepetition, the Debtor entered into a long-term maintenance agreement with General Electric ("GE") with respect to certain equipment. The Debtor alleged that GE's performance was deficient; an arbitrator disagreed and awarded GE more than four million dollars. GE and the Debtor, postpetition, attempted to stipulate to the value of GE's secured claim (but not the unsecured portion thereof). The Debtor also, however, sought to retain DLA Piper as its bankruptcy counsel. DLA Piper obtained a conflicts waiver from GE in which DLA Piper stated, among other things, that it would not bring any litigation or threaten any litigation for the recovery of monetary damages from GE or its affiliates or for any equitable relief against GE or any of its affiliates. DLA Piper also argued that the GE affiliate pursuing recovery against the Debtor was not a client of the firm; rather, such GE affiliate was a client of another entity and DLA Piper did work primarily for a different GE affiliate

Result: The Bankruptcy Court did not approve DLA Piper's retention. The conflicts waiver treated the GE affiliates as one entity; the Bankruptcy Court consequently did the same. DLA Piper also argued that the terms of the stipulation, as well as the conflicts waiver, permitted DLA Piper to proceed. The Court pointed out that the stipulation had not been approved by the Bankruptcy Court. Moreover, the Stipulation did not resolve the remaining issues between the parties: it bound GE to repair and return certain equipment and did not resolve its unsecured claim. The Court opined that "GE and Project Orange remain wholly adverse" until these issues were resolved.[3] In addition, the terms of the waiver limited DLA Piper's ability to act in the best interests of the Debtor regarding GE. In any event, even given the use of conflicts counsel, the Bankruptcy Court held that DLA Piper could not represent the Debtor. GE, the largest unsecured creditor, was central to the case.

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[3] The Court further noted that:

> During the June 7, 2010 hearing, counsel presented a proposed settlement between the Debtor and BP regarding the delivery of natural gas needed to operate the Debtor's Turbines. No objections were filed to the proposed settlement. The Court indicated that it would approve the settlement. Later in the hearing, however, almost in passing, counsel acknowledged that it could not be adverse to BP, an existing client of DLA Piper. The U.S. Trustee then questioned how DLA Piper could negotiate and present the settlement if it cannot be adverse to BP. Counsel then responded that it had identified BP as a conflict party in exhibits to its retention application, as if the disclosure could cure the conflict. The Court withdrew its approval of the settlement, which has since been resubmitted by Golenbock, Debtor's conflict counsel. Identifying conflicts does not involve a game of "gotcha," where disclosure of a conflict party in one schedule excuses counsel from the consequences of a conflict if no one finds the earlier disclosure and objects.

Id. at 374 n.10.

4. *George L. Miller, Chapter 7 Trustee v. Sun Capital Partners, Inc. (In re IH 1, Inc.)*, 441 B.R. 742 (Bankr. D. Del. 2011).

Issue: Chapter 7 trustee brought adversary proceeding against Sun Capital Partners, Inc. ("Sun Capital") and some of Sun Capitals officers and board members (collectively, the "Individual Defendants"). Sun Capital and the Individual Defendants were represented by Kirkland & Ellis LLP ("Kirkland") in the adversary proceeding with the chapter 7 trustee. The chapter 7 trustee sought to disqualify Kirkland from representing Sun Capital due to Kirkland's pre-petition representation of the Debtors on matters substantially related to the adversary proceeding.

Result: The Court denied the chapter 7 trustee's motion with respect to Sun Capital but granted the motion with respect to the Individual Defendants. The court found that the adversary proceeding was substantially related to the pre-petition work Kirkland had done for the Debtors, but that the Debtors' had consented to Kirkland's representation of Sun Capital, its affiliates and portfolio companies, but not the Individual Defendants. In the engagement letter executed by the Debtors, Kirkland disclosed its representation of Sun Capital and the Debtors consented to the representation. The court concluded the opinion by noting that "Kirkland may find itself in the awkward position of being a fact witness if [the chapter 7 trustee] elects to waive the attorney/client privilege as a chapter 7 trustee is entitled to do.").[4]

5. *In re Washington Mutual, Inc.*, 2011 WL 57111, at *1 (Bankr. D. Del. Jan. 7, 2011).

Issue: Objectors to the Debtors' proposed plan of reorganization argued that Debtors' counsel did not negotiate a settlement agreement related to the plan in good faith because the Debtors' counsel's firm also represented JP Morgan Chase ("JPMC"), another party to the settlement agreement, in matters unrelated to the Debtors' bankruptcy proceeding.

Result: The Court denied the plan objectors conflict argument because Debtors' counsel had disclosed in its retention application that its firm represented JPMC and disclosed that it could be adverse to JPMC for certain matters but not for others. In matters in which Debtors' counsel could not be adverse to JPMC, Debtors' counsel agreed to, and eventually did, hire conflicts counsel. The court went on to comment that "the Court personally observed the actions of the Debtors' professionals and finds no evidence that they failed to represent adequately the interests of the estate."[5]

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[4] *In re IH 1, Inc.*, 441 B.R. at 748.

[5] *In re Washington Mutual, Inc.*, 2011 WL 57111, at *5-6.

6. *In re Enron Corp.*, 2002 WL 32034346, at *1 (Bankr. S.D.N.Y. May 23, 2002)

Issue: A creditor sought disqualification of Milbank, Tweed, Hadley & McLoy LLP ("Milbank Tweed") as counsel to the official committee of unsecured creditors (the "Committee") because Milbank Tweed allegedly had undisclosed connections with the Debtors, creditors and other Committee members.

Result: The Court denied the motion because Milbank Tweed mitigated its conflicts by limited the scope of its representation of the Committee to matters in which Milbank Tweed did not have a conflict of interest and retaining conflicts counsel. The Court went on to state that "[t]here is no basis in this record to question the adequacy of this procedure or the internal ethical walls established at Milbank. Conflicts counsel, limited engagement agreements, and ethical walls have been acceptable procedures to address conflict of interest issues."[6] The court further noted that "this has been done in numerous large bankruptcy cases, including this one with respect to certain limitations placed upon the representation by Debtors' counsel."[7]

7. *In re JMK Construction Group, Ltd.*, 441 B.R. 222 (Bankr. S.D.N.Y. 2010)

Issue: United States Trustee objected (the "Objection") to retention application of law firm that attempted to represent a construction company, its principals and other associated individuals in separate bankruptcies because the debtors maintained a continuing right to contribution from each (based upon a pre-petition judgment entered in a state court action) and had inter-debtor claims for repayment of pre-petition loans.

Result: The Court sustained the Objection: (i) due the continuing right of contribution each debtor maintained against the other debtors as joint tortfeasors regarding the pre-petition state court judgment; and (ii) the inter-debtor claims both precluded the law firm from representing the construction company and its principals. The Court concluded that the law firm was limited to representing only one debtor.

II SECONDARY SOURCES

Ronald D. Rotunda, *Resolving Client Conflicts by Hiring "Conflicts Counsel"*, 62 HASTINGS LAW JOURNAL 677, 696 (2011)

[6] *In re Enron*, 2002 WL 32034346, at *11.

[7] *Id.*

III. THE DELAWARE LAWYERS' RULES OF PROFESSIONAL CONDUCT

The Delaware Lawyers' Rules of Professional Conduct ("DLRPC") do not specifically address the retention of conflicts counsel. However, the DLRPC's prohibition on the simultaneous representation of conflicting interests and the lawyer's ability to limit the scope of representation form the need and basis for the retention of conflicts counsel.

The DLRPC provides for, *inter alia*:

(i) a duty to protect the client's confidences and secrets. *See* Rule 1.6(a). This duty also applies to former clients. *See* Rule 1.9(c);

(ii) a duty of loyalty to current clients. *See* Rule 1.7 and cmt. 6;

(iii) if there is a conflict, each affected client may consent to such representation. *See* Rule 1.7(b)(4);

(iv) imputation of the lawyer's individual disqualification to every other lawyer in the same law firm. *See* Rule 1.10; and

(v) a lawyer may limit the scope it its representation if such limitation is reasonable under the circumstances. *See* Rule 1.2(c).

Rule 1.2. Scope of representation

(a) Subject to paragraphs (c) and (d), a lawyer shall abide by a client's decisions concerning the objectives of representation and, as required by Rule 1.4, shall consult with the client as to the means by which they are to be pursued. A lawyer may take such action on behalf of the client as is impliedly authorized to carry out the representation. A lawyer shall abide by a client's decision whether to settle a matter. In a criminal case, the lawyer shall abide by the client's decision, after consultation with the lawyer, as to a plea to be entered, whether to waive jury trial and whether the client will testify.

(b) A lawyer's representation of a client, including representation by appointment, does not constitute an endorsement of the client's political, economic, social or moral views or activities.

(c) A lawyer may limit the scope of the representation if the limitation is reasonable under the circumstances and the client gives informed consent.

(d) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.

COMMENT

[6] *Agreements limiting scope of representation.* -- The scope of services to be provided by a lawyer may be limited by agreement with the client or by the terms under which the lawyer's services are made available to the client. When a lawyer has been retained by an insurer to represent an insured, for example, the representation may be limited to matters related to the insurance coverage. A limited representation may be appropriate because the client has limited objectives for the representation. In addition, the terms upon which representation is undertaken may exclude specific means that might otherwise be used to accomplish the client's objectives. Such limitations may exclude actions that the client thinks are too costly or that the lawyer regards as repugnant or imprudent.

[7] Although this Rule affords the lawyer and client substantial latitude to limit the representation, the limitation must be reasonable under the circumstances. If, for example, a client's objective is limited to securing general information about the law the client needs in order to handle a common and typically uncomplicated legal problem, the lawyer and client may agree that the lawyer's services will be limited to a brief telephone consultation. Such a limitation, however, would not be reasonable if the time allotted was not sufficient to yield advice upon which the client could rely. Although an agreement for a limited representation does not exempt a lawyer from the duty to provide competent representation, the limitation is a factor to be considered when determining the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation. *See* Rule 1.1.

Rule 1.6. Confidentiality of information

(a) A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation, or the disclosure is permitted by paragraph (b).

(b) A lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary:

(1) to prevent reasonably certain death or substantial bodily harm;

(2) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services;

(3) to prevent, mitigate, or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services;

(4) to secure legal advice about the lawyer's compliance with these Rules;

(5) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client; or

(6) to comply with other law or a court order.

COMMENT

[1] This Rule governs the disclosure by a lawyer of information relating to the representation of a client during the lawyer's representation of the client. *See* Rule 1.18 for the lawyer's duties with respect to information provided to the lawyer by a prospective client, Rule 1.9(c)(2) for the lawyer's duty not to reveal information relating to the lawyer's prior representation of a former client and Rules 1.8(b) and 1.9(c)(1) for the lawyer's duties with respect to the use of such information to the disadvantage of clients and former clients.

[2] A fundamental principle in the client-lawyer relationship is that, in the absence of the client's informed consent, the lawyer must not reveal information relating to the representation. *See* Rule 1.0(e) for the definition of informed consent. This contributes to the trust that is the hallmark of the client-lawyer relationship. The client is thereby encouraged to seek legal assistance and to communicate fully and frankly with the lawyer even as to embarrassing or legally damaging subject matter. The lawyer needs this information to represent the client effectively and, if necessary, to advise the client to refrain from wrongful conduct. Almost without exception, clients come to lawyers in order to determine their rights and what is, in the complex of laws and regulations, deemed to be legal and correct. Based upon experience, lawyers know that almost all clients follow the advice given, and the law is upheld.

[3] The principle of client-lawyer confidentiality is given effect by related bodies of law: the attorney-client privilege, the work product doctrine and the rule of confidentiality established in professional ethics. The attorney-client privilege and work product doctrine apply in judicial and other proceedings in which a lawyer may be called as a witness or otherwise required to produce evidence concerning a client. The rule of client-lawyer confidentiality applies in situations other than those where evidence is sought from the lawyer through compulsion of law. The confidentiality rule, for example, applies not only to matters communicated in confidence by the client but also to all information relating to the representation, whatever its source. A lawyer may not disclose such information except as authorized or required by the Rules of Professional Conduct or other law.

[4] Paragraph (a) prohibits a lawyer from revealing information relating to the representation of a client. This prohibition also applies to disclosures by a lawyer that do not in themselves reveal protected information but could reasonably lead to the discovery of such information by a third person. A lawyer's use of a hypothetical to discuss issues relating to the representation is permissible so long as there is no reasonable likelihood that the listener will be able to ascertain the identity of the client or the situation involved.

[18] *Former client.* -- The duty of confidentiality continues after the client-lawyer relationship has terminated. *See* Rule 1.9(c)(2). *See* Rule 1.9(c)(1) for the prohibition against using such information to the disadvantage of the former client.

Rule 1.7. Conflict of interest

(a) Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

(1) the representation of one client will be directly adverse to another client; or

(2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

(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.

COMMENT

[1] *General Principles.* -- Loyalty and independent judgment are essential elements in the lawyer's relationship to a client. Concurrent conflicts of interest can arise from the lawyer's responsibilities to another client, a former client or a third person or from the lawyer's own interests. For specific Rules regarding certain concurrent conflicts of interest, *see* Rule 1.8. For former client conflicts of interest, *see* Rule 1.9. For conflicts of interest involving prospective clients, *see* Rule 1.18. For definitions of "informed consent" and "confirmed in writing," *see* Rule 1.0(e) and (b).

[2] Resolution of a conflict of interest problem under this Rule requires the lawyer to: 1) clearly identify the client or clients; 2) determine whether a conflict of interest exists; 3) decide whether the representation may be undertaken despite the existence of a conflict, i.e., whether the conflict is consentable; and 4) if so, consult with the clients affected under paragraph (a) and obtain their informed consent, confirmed in writing. The clients affected under paragraph (a) include both of the clients referred to in paragraph (a)(1) and the one or more clients whose representation might be materially limited under paragraph (a)(2).

[3] A conflict of interest may exist before representation is undertaken, in which event the representation must be declined, unless the lawyer obtains the informed consent of each client under the conditions of paragraph (b). To determine whether a conflict of interest exists, a lawyer should adopt reasonable procedures, appropriate for the size and type of firm and practice, to determine in both litigation and non-litigation matters the persons and issues involved. *See also* Comment to Rule 5.1. Ignorance caused by a failure to institute such

procedures will not excuse a lawyer's violation of this Rule. As to whether a client-lawyer relationship exists or, having once been established, is continuing, *see* Comment to Rule 1.3 and Scope.

[4] If a conflict arises after representation has been undertaken, the lawyer ordinarily must withdraw from the representation, unless the lawyer has obtained the informed consent of the client under the conditions of paragraph (b). *See* Rule 1.16. Where more than one client is involved, whether the lawyer may continue to represent any of the clients is determined both by the lawyer's ability to comply with duties owed to the former client and by the lawyer's ability to represent adequately the remaining client or clients, given the lawyer's duties to the former client. *See* Rule 1.9. *See also comments* [5] and [29].

[5] Unforeseeable developments, such as changes in corporate and other organizational affiliations or the addition or realignment of parties in litigation, might create conflicts in the midst of a representation, as when a company sued by the lawyer on behalf of one client is bought by another client represented by the lawyer in an unrelated matter. Depending on the circumstances, the lawyer may have the option to withdraw from one of the representations in order to avoid the conflict. The lawyer must seek court approval where necessary and take steps to minimize harm to the clients. *See* rule 1.16. The lawyer must continue to protect the confidences of the client from whose representation the lawyer has withdrawn. *See* Rule 1.9(c).

[6] *Identifying conflicts of interest: Directly adverse.* -- Loyalty to a current client prohibits undertaking representation directly adverse to that client without that client's informed consent. Thus, absent consent, a lawyer may not act as an advocate in one matter against a person the lawyer represents in some other matter, even when the matters are wholly unrelated. The client as to whom the representation is directly adverse is likely to feel betrayed, and the resulting damage to the client-lawyer relationship is likely to impair the lawyer's ability to represent the client effectively. In addition, the client on whose behalf the adverse representation is undertaken reasonably may fear that the lawyer will pursue that client's case less effectively out of deference to the other client, *i.e.*, that the representation may be materially limited by the lawyer's interest in retaining the current client. Similarly, a directly adverse conflict may arise when a lawyer is required to cross-examine a client who appears as a witness in a lawsuit involving another client, as when the testimony will be damaging to the client who is represented in the lawsuit. On the other hand, simultaneous representation in unrelated matters of clients whose interests are only economically adverse, such as representation of competing economic enterprises in unrelated litigation, does not ordinarily constitute a conflict of interest and thus may not require consent of the respective clients.

[9] *Lawyer's Responsibilities to Former Clients and Other Third Persons.* -- In addition to conflicts with other current clients, a lawyer's duties of loyalty and independence may be materially limited by responsibilities to former clients under Rule 1.9 or by the lawyer's responsibilities to other persons, such as fiduciary duties arising from a lawyer's service as a trustee, executor or corporate director.

[15] Consentability is typically determined by considering whether the interests of the clients will be adequately protected if the clients are permitted to give their informed consent to representation burdened by a conflict of interest. Thus, under paragraph (b)(1), representation is

prohibited if in the circumstances the lawyer cannot reasonably conclude that the lawyer will be able to provide competent and diligent representation. *See* Rule 1.1 (competence) and Rule 1.3 (diligence).

[18] *Informed Consent.* -- Informed consent requires that each affected client be aware of the relevant circumstances and of the material and reasonably foreseeable ways that the conflict could have adverse effects on the interests of that client. *See* Rule 1.0(e) (informed consent). The information required depends on the nature of the conflict and the nature of the risks involved. When representation of multiple clients in a single matter is undertaken, the information must include the implications of the common representation, including possible effects on loyalty, confidentiality and the attorney-client privilege and the advantages and risks involved. *See* Comments [30] and [31](effect of common representation on confidentiality).

[19] Under some circumstances it may be impossible to make the disclosure necessary to obtain consent. For example, when the lawyer represents different clients in related matters and one of the clients refuses to consent to the disclosure necessary to permit the other client to make an informed decision, the lawyer cannot properly ask the latter to consent. In some cases the alternative to common representation can be that each party may have to obtain separate representation with the possibility of incurring additional costs. These costs, along with the benefits of securing separate representation, are factors that may be considered by the affected client in determining whether common representation is in the client's interests.

Rule 1.9. Duties to former clients

(a) A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing.

(b) A lawyer shall not knowingly represent a person in the same or a substantially related matter in which a firm with which the lawyer formerly was associated had previously represented a client:

(1) whose interests are materially adverse to that person; and

(2) about whom the lawyer had acquired information protected by Rules 1.6 and 1.9(c) that is material to the matter;
unless the former client gives informed consent, confirmed in writing.

(c) A lawyer who has formerly represented a client in a matter or whose present or former firm has formerly represented a client in a matter shall not thereafter:

(1) use information relating to the representation to the disadvantage of the former client except as these Rules would permit or require with respect to a client, or when the information has become generally known; or

(2) reveal information relating to the representation except as these Rules would permit or require with respect to a client.

COMMENT

[1] After termination of a client-lawyer relationship, a lawyer has certain continuing duties with respect to confidentiality and conflicts of interest and thus may not represent another client except in conformity with this Rule. Under this Rule, for example, a lawyer could not properly seek to rescind on behalf of a new client a contract drafted on behalf of the former client. So also a lawyer who has prosecuted an accused person could not properly represent the accused in a subsequent civil action against the government concerning the same transaction. Nor could a lawyer who has represented multiple clients in a matter represent one of the clients against the others in the same or a substantially related matter after a dispute arose among the clients in that matter, unless all affected clients give informed consent. *See* Comment [9]. Current and former government lawyers must comply with this Rule to the extent required by Rule 1.11.

[2] The scope of a "matter" for purposes of this Rule depends on the facts of a particular situation or transaction. The lawyer's involvement in a matter can also be a question of degree. When a lawyer has been directly involved in a specific transaction, subsequent representation of other clients with materially adverse interests in that transaction clearly is prohibited. On the other hand, a lawyer who recurrently handled a type of problem for a former client is not precluded from later representing another client in a factually distinct problem of that type even though the subsequent representation involves a position adverse to the prior client. Similar considerations can apply to there assignment of military lawyers between defense and prosecution functions within the same military jurisdictions. The underlying question is whether the lawyer was so involved in the matter that the subsequent representation can be justly regarded as a changing of sides in the matter in question.

[3] Matters are "substantially related" for purposes of this Rule if they involve the same transaction or legal dispute or if there otherwise is a substantial risk that confidential factual information as would normally have been obtained in the prior representation would materially advance the client's position in the subsequent matter. For example, a lawyer who has represented a business person and learned extensive private financial information about that person may not then represent that person's spouse in seeking a divorce. Similarly, a lawyer who has previously represented a client in securing environmental permits to build a shopping center would be precluded from representing neighbors seeking to oppose rezoning of the property on the basis of environmental considerations; however, the lawyer would not be precluded, on the grounds of substantial relationship, from defending a tenant of the completed shopping center in resisting eviction for nonpayment of rent. Information that has been disclosed to the public or to other parties adverse to the former client ordinarily will not be disqualifying. Information acquired in a prior representation may have been rendered obsolete by the passage of time, a circumstance that may be relevant in determining whether two representations are substantially related. In the case of an organizational client, general knowledge of the client's policies and practices ordinarily will not preclude a subsequent representation; on the other hand, knowledge of specific facts gained in a prior representation that are relevant to the matter in question ordinarily will preclude such a representation. A former client is not required to reveal the confidential information learned by the lawyer in order to establish a substantial risk that the lawyer has confidential information to use in the subsequent matter. A conclusion about the possession of such information may be based on the nature of the services the lawyer provided

the former client and information that would in ordinary practice be learned by a lawyer providing such services.

[9] The provisions of this Rule are for the protection of former clients and can be waived if the client gives informed consent, which consent must be confirmed in writing under paragraphs (a) and (b). *See* Rule 1.0(e). With regard to the effectiveness of an advance waiver, *see* Comment [22] to Rule 1.7. With regard to disqualification of a firm with which a lawyer is or was formerly associated, *see* Rule 1.10.

Rule 1.10. Imputation of conflicts of interest

(a) Except as otherwise provided in this rule, while lawyers are associated in a firm, none of them shall knowingly represent a client when any one of them practicing alone would be prohibited from doing so by Rules 1.7 or 1.9, unless the prohibition is based on a personal interest of the prohibited lawyer and does not present a significant risk of materially limiting the representation of the client by the remaining lawyers in the firm.

(b) When a lawyer has terminated an association with a firm, the firm is not prohibited from thereafter representing a person with interests materially adverse to those of a client represented by the formerly associated lawyer and not currently represented by the firm, unless:

(1) the matter is the same or substantially related to that in which the formerly associated lawyer represented the client; and

(2) any lawyer remaining in the firm has information protected by Rules 1.6 and 1.9(c) that is material to the matter.

(c) When a lawyer becomes associated with a firm, no lawyer associated in the firm shall knowingly represent a client in a matter in which that lawyer is disqualified under Rule 1.9 unless:

(1) the personally disqualified lawyer is timely screened from any participation in the matter and is apportioned no part of the fee therefrom; and

(2) written notice is promptly given to the affected former client.

(d) A disqualification prescribed by this rule may be waived by the affected client under the conditions stated in Rule 1.7.

(e) The disqualification of lawyers associated in a firm with former or current government lawyers is governed by Rule 1.11.