CONFIRMATION AND ISSUES REGARDING SAME

I. CONFIRMATION ISSUES:

A. What is Indemnification, Contribution and Exculpation?

Indemnity, contribution and exculpation are different methods of reaching similar, but not identical, results. In general: (i) indemnity means that, if a third party sues a professional based on the professional's services to the client, the client will pay to defend the professional and will pay any judgment against the professional; (ii) contribution means that, if a third party sues both a professional and the professional's client based on the professional's services to the client, the client will contribute some or all of the professional's costs to defend and to satisfy any judgment against the professional and (iii) exculpation means that the client agrees not to sue the professional based on the professional's services to the client. Under each of these arrangements, the client bears some or all of the financial consequences of the professional's actions. *See In re Metricom, Inc.*, 275 B.R. 364, 368 (Bankr. N.D. Cal. 2002).

B. In the Beginning

Historically, bankruptcy professionals had been paid according to notions of "economy of the estate," under which professionals compensation lagged behind that of professionals in non-bankruptcy contexts. The legislative history accompanying the 1978 amendments to the Bankruptcy Code expressed Congress's intent that bankruptcy professionals be employed on terms similar to those that applied outside of bankruptcy.

Notwithstanding the "market approach" to retentions embodied in the bankruptcy code, in the years following such amendments bankruptcy courts were often troubled by the indemnification of professionals. Bankruptcy courts disallowed indemnification provisions citing to the apparent inconsistency between indemnification and the financial advisor's professional and fiduciary duties. Other bankruptcy courts discounted the extent to which market practices should dictate the "reasonableness" of the terms of professionals retained in bankruptcy. Still other bankruptcy courts asserted that financial advisors carry or should carry liability insurance to cover their risks and that the cost of such insurance is already reflected in their fees.

Overtime, however, bankruptcy courts started to become more receptive to indemnification provisions. These courts began to hold that nothing in the bankruptcy code prohibited a court from approving indemnification provisions that covered, among other things, acts and omissions constituting ordinary negligence. *In re Joan and David Halpern*, 248 B.R. 43, 46-47 (Bankr. S.D.N.Y. 2000) *aff'd*, 2000 U.S. Dist. LEXIS 17589 (S.D.N.Y.) ("[T]he idea that a fiduciary cannot be indemnified for negligence, or that such indemnification is contrary to public policy, is just plain wrong. The common law has carved out clear exceptions to indemnity, such as bad faith, breach of trust, dishonesty, self-dealing, and willful, reckless or grossly negligent misconduct, leaving the rest to the parties' agreement"); *In re DEC Int'l, Inc.*, 2002 WL 1974438, *3, *6 (D. W.D. Wisc. 2002) ("Inappropriate or not, the question is whether the [indemnification] provision is illegal under the bankruptcy act....Whatever reservations I might have about broad ranging indemnification agreements, I cannot say that they are unreasonable as a matter of law."); *In re Comdisco, Inc.*, 2002 U.S. Dist. LEXIS 17994 (N.D. Ill.

2002) (affirming bankruptcy court's determination that indemnification of debtor's financial advisor was reasonable; no per se rule prohibiting such provisions).

Notwithstanding some courts reluctance to approve indemnification provisions, turnaround managers and other professionals regularly demanded indemnification provisions in their retention agreements. *In re Merry-Go-Round Enters.*, 244 B.R. 327 (Bankr. D. Md. 2000) served as a "wake up call" for bankruptcy specialists that a court's unwilling to approve such provisions could have serious financial repercussions. There, after conversion to a chapter 7 liquidation, the trustee brought a $4 billion fraud, negligence and malpractice case against Ernst & Young for its role in the bankruptcy proceedings of Merry-Go-Round. The lawsuit settled on the eve of trial for $185 million. It is not surprising that not long after this case, the issue of indemnification provisions was brought to the attention of the Third Circuit Court of Appeals.

C. The Third Circuit Court of Appeals Addresses Indemnification

In *In re United Artist Theatre Co.*, 315 F.3d 217 (3d Cir. 2003) the Third Circuit Court of Appeals became the first federal appellate court to address the permissibility of indemnification provisions in the engagement of professionals in a bankruptcy case.

Issue: In 2000, United Artists Theatre Co. and its affiliates filed chapter 11 bankruptcies in Delaware. In connection with their bankruptcy pleadings, the debtors sought to retain Houlihan Lokey Howard & Zukin ("HL") as their financial advisors. As part of its retention agreement, HL sought to have the debtors indemnify it for claims of negligence (as opposed to gross negligence) that might be asserted against it. The U.S. Trustee objected to the indemnification provisions, arguing they were *per se* unreasonable under section 328 and 330. The U.S. Trustee argued that allowing professionals to obtain indemnity for their own negligence cannot be reasonable since it would encourage a standard that is both lax and inconsistent with their fiduciary obligations to creditors. HL countered that failure to approve the indemnification would lead to "Monday-morning quarterbacking" and second-guessing by courts of mistaken decisions that seemed attractive at the time. This, HL argued, would cause a disservice to the debtor's estate because financial advisers would then be constrained and overly cautious in their advice.

Holding: Writing for the Court, Judge Ambro rejected the U.S. Trustee's position and held that an agreement requiring the Debtor to indemnify a financial adviser for its negligence was reasonable. The Court referenced section 330, which uses a "market-driven" approach in determining the reasonableness of compensation for professionals employed by the estate. In the Court's view, section 330, however, does not automatically make market place indemnification provisions "reasonable" under section 328. Instead, the Court borrowed from Delaware corporate law and based the reasonableness determination on "traditional negligence/gross negligence analysis," an approach that examines the level of care used by the financial adviser in the process of obtaining results rather than the results themselves. The Court indicated that Delaware law tolerates ordinary negligence and requires that corporate fiduciaries not be grossly negligent.

Critical of distinctions between "negligence" and "gross negligence" in the area of corporate governance, the Court recognized that Delaware courts resolved this "negligence conundrum" by focusing on the process by which boards reach decisions rather than the final result of those decisions. In Delaware, a finding of gross negligence, therefore, is appropriate when a board fails to inform itself of all material information reasonably available. The Court likened HL's role with that of a director, which, while not a surety of success, can be held accountable for not advising with the level of care or loyalty expected. As such, the Court held that the indemnification provision was reasonable. In so ruling, the Court set forth two caveats. First, it ruled that HL's attempt to supplement the retention agreement with a provision indemnifying it for even gross negligence, if not solely the cause of damages, would violate public policy. Second, the Court ruled that it would be improper for HL to be indemnified not only for acting in its professional capacity, but for breach of its contract with the debtor.

Judge Alito Concurrence:

Judge Alito specifically states in his concurring opinion that "[t]he opinion of the court, as I understand it, holds only that the 'reasonableness' standard of 11 U.S.C. § 328(a) does not categorically prohibit indemnification of financial advisors ... [T]he court does not hold that Houlihan Lokey's indemnification must be interpreted in accordance with the principals of Delaware corporate law that the opinion of the court discusses." For Judge Alito, Delaware corporate law is relevant only in as much as "this understanding of the circumstances in which it is sensible to hold financial advisors responsible for unsuccessful business decisions helps to explain why indemnification agreements such as the one in this case are not categorically 'unreasonable.'"

Judge Rendell Concurrence:

Judge Rendell, while concurring with the result reached by Judge Ambro, raises several practical concerns arising from the application of the rule proposed by the Opinion of the Court. In her opinion, the subjective test provides no guidance to the bankruptcy court in determining "reasonableness" of indemnification provisions at the time of retention. Instead, the availability of indemnification may only be determined by the initiation of a lawsuit. Moreover, the new test calls into question the enforceability of existing indemnities. In Judge Rendell's view, the "reasonableness" of a financial advisor indemnity would more effectively be determined during the retention process by reference to factors recognized in other opinions, including: (i) whether the financial advisor's retention was in the best interests of the estate; (ii) whether the creditors approved the financial advisor's retention and did not object to the indemnity provisions; (iii) the agreement does not provide for a blanket immunity, but rather contains detailed procedures for determining at a later date whether relief under the indemnity should be granted; (iv) the extent to which indemnification related to pre- versus post-petition services; (v) whether the indemnity was negotiated at

arms-length between sophisticated parties; (vi) whether indemnification provisions are consistent with normal business practice; and (vii) whether the trial court retained discretion to modify the terms of the agreement pursuant to the standard set forth in Section 328 of the Bankruptcy Code.

D. **Limitation of Liability Provisions**

1. *In re Dailey Int'l, Inc.*, 1999 Bankr. LEXIS 2065 (Bankr. D. Del. July 1, 1999)

Issue: The Debtors sought to retain Ernst & Young, L.L.P. ("E&Y") as accountants, auditors, tax advisors and financial advisors. The engagement letter included both an ADR provision and a limitation of liability provision, which provisions were a matter of first impression for the Court. The ADR provision required, *inter alia*, the parties to submit any dispute arising out of the engagement first to mediation and then to binding arbitration rather than having the bankruptcy court adjudicate such matter. The limitation of liability provision sought to limit E&Y's liability for any reason under the engagement letter to its fees. Both the U.S. Trustee and the Committee objected to the provisions

Holding: Judge Walsh held that the ADR provision and the limitation of liability provision were not appropriate terms and conditions for the retention of professionals in bankruptcy pursuant to 11 U.S.C. §§ 327 and 328.

With respect to the ADR provision, the Court explained that such provision denied it the ability to hear potential claims by the Debtors against E&Y related to its retention, matters which were core matters and clearly related to the administration of the estates. Moreover, such claims, in the Court's opinion, would likely involve the meaning and effect of the very contract for E&Y's retention which the Court had sole jurisdiction to approve. The Court went on to explain that the issue was not whether to enforce such clause but whether the Court, acting pursuant to broad administrative authority over reorganizations and claims resolutions, should approve the proposed ADR provision in the first place.

With respect to the limitation of liability provision, the Court began by acknowledging that indemnity provisions are routinely included in engagement letters. The Court noted, however, that the limitation of liability provision sought by E&Y was overreaching and was not consistent with public policy embodied in the Bankruptcy Code. The Court compared the provision to a photo film developer: "No matter what happens to the customer's firm or prints, the developer's liability is limited to the cost of the roll of film. However appropriate that my be in the commercial arena of film processing, I find it inappropriate in the arena of professional services." The Court went on to explain that it was patently clear from §§ 327 and 328 that sophisticated parties are not entitled to dictate the terms and conditions of the engagement of professionals. Rather, those terms and conditions are subject to the approval of the bankruptcy court in making reasoned determinations as to what is in the best interest of the estate. In

the Court' s opinion, the issue in not whether indemnification and other risk allocation provisions should be enforced when present in a valid contract; rather, the issue is whether such provisions should be approved in a professional's retention application in a bankruptcy forum.

CONFIRMATION ISSUES: FACT PATTERN

A contentious Chapter 11 case has finally reached the point of a mostly consensual plan. The plan has the support of the debtors, the committee and the secured creditors. The plan is drafted by debtors' counsel. In addition to the financial terms agreed on by the parties, the plan contains various boilerplate provisions, and includes the following provisions providing for the exculpation and release of, among others, professionals:

> Exculpation: Neither the Debtors, the DIP Lenders, the Creditors' Committee, nor any of their respective members (current and former), officers, directors, employees, counsel, advisors, professionals, or agents, shall have or incur any liability to any holder of a Claim or Equity Interest for any act or omission in connection with, related to, or arising out of the Chapter 11 Cases; negotiations regarding or concerning the Plan, the Plan Documents; the pursuit of confirmation of the Plan; the consummation of the Plan; or the administration of the Plan or the property to be distributed under the Plan.
>
> Release: The Debtors, for themselves and their estates, hereby release the Debtors, the DIP Lenders, the Creditors' Committee, and each of their respective members (current and former), officers, directors, employees, counsel, advisors, professionals, or agents for any and all claims, obligations, debts or causes of action in any way relating to the Chapter 11 Cases, the Plan, negotiations regarding or concerning the Plan, the Plan Documents, the pursuit of the Plan, the consummation of the Plan, the administration of the Plan and the ownership, management, and operation of the Debtors.

However, there is "a fly in ointment, a monkey in the wrench, a pain in the process[1]." During the course of the case, the debtors prosecuted an adversary action against a former vice-president of the debtors. The action sought to set aside certain benefits received by the former vice-president under a buy-out agreement on fraudulent conveyance grounds.

The former vice-president/defendant at issue is the ex-spouse of the debtor's CEO. [He/she] objects to the exculpations and releases of various parties, and seeks to preserve the right to bring malicious prosecution claims against debtors' counsel.

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[1] To paraphrase John McClane from the motion picture *Die Hard*, 1998. "Just a fly in the ointment, Hans. The monkey in the wrench. The pain in the [rhymes with class]."

ISSUES CONCERNING CONFIRMATION: CASE SUMMARIES

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

A. **Definition**: "the act of excusing a mistake or offense"

B. **Issue**: Exculpation of a professional under a plan. In particular, the following provision of the plan was challenged as violating 524(e) and 1103(c):

> [n]one of the Debtors, the Reorganized Debtors, New Bruno's, the Creditor Representative, the Committee or any of their respective members, officers, directors, employees, advisors, professionals or agents shall have or incur any liability to any holder of a Claim or Equity Interest for any act or omission in connection with, related to, or arising out of, the Chapter 11 Cases, the pursuit of confirmation of the Plan, the consummation of the Plan or the Administration of the Plan or the property to be distributed under the Plan, except for willful misconduct or gross negligence, and, in all respects, the Debtors, the Reorganized Debtors, New Bruno's, the Creditor Representative, the Committee and each of their respective members, officers, directors, employees, advisors, professionals and agents shall be entitled to rely upon the advice of counsel with respect to their duties and responsibilities under the plan.

C. **Holding**: the Court held that the quoted provision (referred to in the decision as a release provision, but in fact written as exculpation) was appropriate, authorized by section 1103(c) and did not violate 524(e). Specifically, the Court found that:

> [Section 1103(c)] has been interpreted to imply both a fiduciary duty to committee constituents and a limited grant of immunity to committee members, *see In re L.F. Rothschild Holdings, Inc.*, 163 B.R. 45, 49 (S.D.N.Y.1994); *In re Drexel Burnham Lambert Group, Inc.*, 138 B.R. 717, 722 (Bankr.S.D.N.Y.1992), *aff'd*, 140 B.R. 347 (S.D.N.Y.1992); *In re Tucker Freight Lines, Inc.*, 62 B.R. 213, 216, 218 (Bankr.W.D.Mich.1986); Lawrence P. King, *Collier on Bankruptcy* ¶ 1103.05 [4], 1103-32-33 (15th ed. rev.1996) ("[A]ctions against committee members in their capacity as such should be discouraged. If members of the committee can be sued by persons unhappy with the committee's performance during the case or unhappy with the outcome of the case, it will be extremely difficult to find members to serve on an official committee.").
>
> This immunity covers committee members for actions within the scope of their duties. The committee members and the debtor are

> entitled to retain professional services to assist in the reorganization. In *Pan Am Corp. v. Delta Air Lines, Inc.*, 175 B.R. 438, 514 (S.D.N.Y.1994), it was held that committee members and those professionals who provide services to the debtor with respect to reorganization, or to the committee members in their capacity as committee members, however, do remain liable for willful misconduct or *ultra vires* acts.
>
> We agree with this interpretation of *§ 1103(c)* and hold that it limits liability of a committee to willful misconduct or *ultra vires* acts. The release in Paragraph 58 sets forth the appropriate standard for liability that would apply to actions against the committee members and the entities that provided services to the Committee in the event that they were sued for their participation in the reorganization. It does not affect the liability of another entity on a debt of the debtor within the meaning of *§ 524(e)*.

PWS Holding Corp., 228 F.3d at 246-47 (footnote omitted).

II. RELEASE OF PROFESSIONALS UNDER A PLAN

A. ***In re Washington Mutual, Inc.***, Chapter 11 Case No. 08-12229 (MFW)

1. **Definition**: A contractual agreement by which one individual assents to relinquish a claim or right under the law to another individual against whom such claim or right is enforceable.

2. **Issue**: The following provision appeared in the plan:

> Except as otherwise expressly provided in the Plan, the Confirmation Order, or the Global Settlement, on the Effective Date, for good and valuable consideration, each of the Debtors and the Reorganized Debtors on its own behalf and as representative of its respective estate, and each of its respective Related Persons, and on behalf of the Liquidating Trust, the Liquidating Trustee, the Liquidating Trust Beneficiaries and the Disbursing Agent, and each of their respective Related Persons, shall be deemed to have and hereby does irrevocably and unconditionally, fully, finally and forever waive, release, acquit, and discharge the Released Parties[1]

[1] "Released Parties" was defined in §1.160 of the Plan as "collectively, each of the WMI Entities, WMB, each of the Debtors' estates, the Reorganized Debtors, the Creditors' Committee and each of its members in their capacity as members of the Creditors' Committee, the Trustees, the Liquidating Trust, the Liquidating Trustee, the JPMC Entities, the Settlement Note Holders, the FDIC Receiver and FDIC Corporate, and each of the foregoing parties' respective Related Persons."

and each of their respective Related Persons[2], from any and all Claims or Causes of Action that the Debtors, the Reorganized Debtors, the Liquidating Trust, the Liquidating Trustee, the Liquidating Trust Beneficiaries, and the Disbursing Agent, and their respective Related Persons, or any of them, or anyone claiming through them, on their behalf or for their benefit, have or may have or claim to have, now or in the future, against any Released Party or any of their respective Related Persons that are Released Claims or otherwise are based upon, relate to, or arise out of or in connection with, in whole or in part, any act, omission, transaction, event or other circumstance relating to the Debtors, the Affiliated Banks, or any of their respective Related Persons, taking place or existing on or prior to the Effective Date, and/or any Claim, act, fact, transaction, occurrence, statement, or omission in connection with or alleged or that could have been alleged in the Related Actions, including, without limitation, any such claim, demand, right, liability, or cause of action for indemnification, contribution, or any other basis in law or equity for damages, costs or fees.

3. **Holding**: The plan's release provisions were generally objected to as being overly broad. Judge Walrath addressed the issue of releases as they relate to a debtor's release, among others, the debtor's attorneys, in a chapter 11 plan. While the Court noted that the Third Circuit had not articulated a test for when releases by debtors are inappropriate, the Court found the release had to be analyzed on an individual basis for each beneficiary of the release under the *Master Mortgage* factors identified by the Court in *In re Zenith Elecs. Corp.*, 241 B.R. 92, 110 (Bankr. Del. 1999) (citing I*n re Master Mortgage Inv. Fund Inc.*, 168 B.R. 930, 937 (Bankr. W.D. Mo. 1994)). Those factors are: (1) an identity of interest between the debtor and non-debtor such that a suit against the non-debtor will deplete the estate's resources; (2) a substantial contribution to the plan by the non-debtor; (3) the necessity of the release to the reorganization; (4) the overwhelming acceptance of the plan and release by creditors and interest holders; and (5) the payment of all or substantially all of the claims of the creditors and interest holders under the plan. *Id.* at 110.

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[2] "Related Persons" was defined in §1.158 in the Plan as "[w]ith respect to any Entity, such predecessors, successors and assigns (whether by operation of law or otherwise) and their respective present and former Affiliates and each of their respective current and former members, partners, equity holders, officers, directors, employees, managers, shareholders, partners, financial advisors, attorneys, accountants, investment bankers, consultants, agents and *professionals* (including, without limitation, any and all professionals retained by WMI or the Creditors' Committee in the Chapter 11 Cases either (a) pursuant to an order of the Bankruptcy Court other than ordinary course professionals or (b) as set forth on Schedule 3.1(a) to the Global Settlement Agreement)…".

With respect the release as to directors, officers, and professionals, it was unclear to the Court whether the release was limited only to such professionals' post-petition activity but in any event, the Court found such releases overly broad and unnecessary. Under the *Master Mortgage* test, the Court found there was "no basis whatsoever for the Debtors to grant a release to directors and officers or any professionals of the debtors, current or former." *WaMu*, at p. 71. The Court held that there was no evidence presented of any "substantial contribution" justifying the releases, nor any evidence that the release of such parties was necessary for the reorganization. In addition, the court found that while the plan has been accepted by the many creditor classes, it was not because of any contribution by these parties; it was because the parties were getting paid in full. *Id.* at 71. Indeed, the Court noted that many of these professionals who served in the chapter 11 case were already receiving exculpations and therefore, the releases as to them were unnecessary, duplicative or exceed the limits of what they are entitled to receive. *Id.* at 72. Moreover, the Court noted that one of the exculpation clauses did provide for the standard in this circuit under *PWS* and had to be revised accordingly.

III. THE LAW IN OTHER JURISDICTIONS:

A. Second Circuit law is consistent with the Third Circuit

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

- The plan included releases that permanently enjoined creditors from suing various nondebtors, though none were case professionals;
- The Court acknowledged that under its prior decision in *In re Drexel Burnham Lambert Group, Inc.*, 960 F.2d 285 (2d Cir. 1992), a bankruptcy court may enjoin a creditor from suing a third party "provided the injunction plays an important part in the debtor's reorganization plan."
    - While no case had determined what qualifies as important, such a release is proper only in rare cases;
- Other courts had approved nondebtor releases under various justifications:
    - The estate received substantial consideration for the release;
    - The enjoined claims were channeled to a settlement fund rather than extinguished;
    - The enjoined claims would indirectly impact the debtor's reorganization by way of indemnity or contribution;

- The plan otherwise would provide for full payment of the enjoined claims; and
- The affected creditors consented.

- Here there were no unique circumstances present supporting the third party releases, and "[a] nondebtor release in a plan of reorganization should not be approved absent the finding that truly unusual circumstances render the release terms important to success of the plan, focusing on the considerations [above]."

2. *In re Motor Liquidation Co.*, 2011 Bankr. LEXIS 684 (Bankr. S.D.N.Y. Mar. 7, 2011)[3]

- Very recent case applying *Metromedia* in context of release and exculpation provisions within a plan;
- The court found the debtor's releases unobjectionable, but the exculpation provision impermissible under *Metromedia* and its progeny;
- **Exculpation Provision:**
  - The exculpation provision provided that various individuals and entities, including case professionals, would not "have or incur any liability to any holder of a Claim or Equity Interest for any act or omission in connection with, related to, or arising out of the Chapter 11 Cases," including consummation of the plan or administration of the plan;
  - The provision also expressly carved out actions constituting willful misconduct, gross negligence, fraud, malpractice, and other particularly egregious conduct;
  - With respect to third party releases, the court noted that the Code does not explicitly state that such provisions are impermissible, but "[a]lthough (since the Code is silent on the matter) third-party releases aren't 'inconsistent with the applicable provisions of this title [per section 1123(b)(6)],' the Second Circuit has ruled that they're permissible only in rare cases, with appropriate consent or under circumstances that can be regarded as unique ... But where those circumstances haven't been shown, third-party releases can't be found to be 'appropriate.'"

[3] "I well recognize how hard the Debtors, the Chapter 11 Fiduciaries, and their professionals worked on this case, and how, with thousands of disappointed creditors and stockholders out there to second guess their actions, they would like to be protected for their good faith actions in maximizing value and bringing this case to a successful conclusion. But I'm constrained by existing law to put some limits on their protection." *In re Motor Liquidation Co.*, 2011 Bankr. LEXIS 684 (Bankr. S.D.N.Y. Mar. 7, 2011).

- Because none of the qualifying circumstances for third-party releases as articulated in *Metromedia* were present, the court found that exculpation provision was invalid;
- However, the *Motors Liquidation* court gave guidance as to how a plan mechanism could provide for a gate-keeping function for creditor claims against third-parties:
    - "[The exculpation provision] may include language, if Plan Supporters wish, requiring third-party claims of the type now covered to be first brought before me, for a threshold inquiry to confirm that they actually belong to the third-party, and don't belong, instead, to the Estate. And it may further provide, if Plan supporters wish, that, subject to any applicable subject matter jurisdiction limitations, I'll at least initially have exclusive jurisdiction to be the forum for any covered litigation brought by any creditor or equity security holder, so long as I'm free to abstain and consider whether that litigation would be better conducted elsewhere."
- **Release Provision:**
    - Under the release provision, the Debtors proposed to release various individuals and entities, including post-Commencement Date professionals, from claims assertable on behalf of, or derivative from the Debtors, "in any way relating to the Debtors, the Chapter 11 Cases, the Plan, negotiations regarding or concerning the Plan, and the ownership, management, and operation of the Debtors."
    - The provision expressly carved out actions constituting willful misconduct, *ultra vires* acts, claims arising out of express contractual obligations with respect to a loan or advance, and certain professional duties of counsel;
    - With respect to these proposed releases, the court found that the "[r]eleases by [the] estates involve a give-up of potential rights that are owned by the estate, and are perfectly permissible in a plan, either as parts of plan settlements or otherwise, though the court must satisfy itself (at least if anyone raises the issue) that the give-up is an appropriate exercise of business judgment, and, possibly, in the best interests of the estate." The court noted that in many cases these will be authorized under section 1123(b) of the Bankruptcy Code, covering matters that may be included in a plan.

B. Other Circuits that have addressed the issue of Professional Releases/Exculpation Under Plan Differ From Third Circuit

1. Fifth Circuit:

- ***In re Pilgrim's Pride,* 2010 Bankr. LEXIS 72 (Bankr. N.D. Tex., Jan. 14, 2010)**
  - *In re Pacific Lumber Co.*, 584 F.3d 229 (5th Cir. 2009), the plan included an exculpation provision barring claims against the plan proponents (creditors of the debtor), the reorganized debtors, and the creditors' committee (other than claims for willful misconduct and gross negligence) relating to proposing, implementing, and administering of the plan.
    - In *Pacific Lumber*, the plan proponents had contributed $580 million to fund distributions under the plan and the secured lender/proponent converted its $160 million claim to equity;
    - Relying on section 524(e) of the Bankruptcy Code, providing that a "discharge of a debt of the debtor does not affect the liability of any other entity on ... such debt," the *Pacific Lumber* court found the exculpation provision was inappropriate to anyone other than the committee;
      - The provision was appropriate as to the committee because section 1103(c) implies that members of the committee have qualified immunity for actions taken within the scope of their duties;
  - Applying *Pacific Lumber* holding to the facts before it, the *Pilgrim's Pride* court declined to approve releases and exculpations of debtors' employees, officers, directors, and professionals, even though the plan paid creditors in full in cash and there was no indication of bad faith;
    - However, as in *Pacific Lumber*, the court permitted exculpation of the committee under section 1103.

2. Ninth Circuit:

- ***In re Lowenschuss,* 67 F.3d 1394 (9th Cir. 1995)**
  - While not specifically addressing the issue of professional releases, the Court found that section 524(e) of the Bankruptcy Code specifically and without exception

precludes bankruptcy courts from discharging the liabilities of non-debtors, and therefore a "Global Release" in the plan for non-debtor individuals and entities was invalid

IV. ADDITIONAL ETHICAL ISSUES RELATED TO PROFESSIONAL RELEASES

A. The Delaware Rules Of Professional Conduct

- A Lawyer may not prospectively limit malpractice liability unless the client is independently represented. *See* Del. Prof. Cond. R. 1.8 (h)(1) ("[A lawyer shall not:] make an agreement prospectively limiting the lawyer's liability to a client for malpractice unless the client is independently represented in making the agreement...")

- Nor may a lawyer settle a malpractice claim or potential malpractice claim, unless the client is told in writing that he or she may want to consult independent legal counsel and are given the opportunity to do so. *See* Del. Prof. Cond. R. 1.8 (h)(1) ("[A lawyer shall not:] settle a claim or potential claim for such liability with an unrepresented client or former client unless that person is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel in connection therewith.")

- Delaware Lawyers' Rule of Professional Conduct 1.8(h) is identical to ABA Model Rule of Professional Conduct 1.8(h). Every other state has a similar ethical rule and most are patterned on the ABA Model Rule.

B. The Terms of Plan Releases Often Operate to Settle Malpractice Claims

- Plan releases and exculpation provisions are often drafted with broad language that both limits and settles/releases any malpractice liability. Plans common provide that "Neither the Debtor .... Nor any of their ... attorneys ... shall have or incur any liability to any Creditor ... or any other party in interest ... for any act or omission in connection with, relating to or arising out of the chapter 11 Cases ... except for their willful misconduct.... On the Effective Date, each of the Debtors and Reorganized Debtors shall be deemed to have settled, released and waived any and all claims ... against any ... attorney of any Debtor servicing in such capacity immediately prior to the Effective Date." *See* First Amended Joint Plan or Reorganization Under Chapter 11 of the Bankruptcy Code, *In re APF, Co.*, No. 98-1596-PJW (Bankr. D. Del. May 27, 1999);

- Such broad release appears to trigger both elements of Rule 1.8(h). A broad release would run afoul of Rule 1.8(h)(1) to the extent it serves as a prospective release that applies to any act or omission in connection with the chapter 11. It also runs afoul of Rule 1.8(h)(2) to the extent it purports

to deem settled any claims or potential claims against the Debtor's attorneys.[4]

[4] Additional Resources: *Unethical Protection? Model Rule 1.8(h) and Plan Releases of Professional Liability*, 83 Am. Bankr. L.J. 481 (2009).

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	)	Chapter 11
APPLESEED'S INTERMEDIATE HOLDINGS LLC, *et al.*,[1]	)	Case No. 11-10160 (KG)
Debtors.	)	Jointly Administered
	)	**Related to Docket No. 138**

ORDER AUTHORIZING THE EMPLOYMENT AND RETENTION OF MOELIS & COMPANY LLC AS FINANCIAL ADVISOR AND CAPITAL MARKETS ADVISOR TO THE DEBTORS *NUNC PRO TUNC* TO THE PETITION DATE

Upon the application (the "***Application***")[2] of the Debtors, for entry of an order (this "***Order***") pursuant to sections 327(a) and 328 of the Bankruptcy Code, Rules 2014(a) and 2016 of the Bankruptcy Rules and Rules 2014-1, 2016-1 and 2016-2 of the Local Rules, authorizing the Debtors to retain and employ Moelis & Company LLC ("***Moelis***") as their financial advisor and capital markets advisor in accordance with the terms and conditions set forth in the Engagement Letter, attached hereto as **Exhibit 1**, *nunc pro tunc* to January 19, 2011 (the "***Petition Date***"), all as more fully described in the Application and the Dermont Declaration;

1 The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's federal taxpayer-identification number, are: Appleseed's Intermediate Holdings LLC (6322); Appleseed's Acquisition, Inc. (5835); Appleseed's Holdings, Inc. (9117); Arizona Mail Order Company, Inc. (6359); Bedford Fair Apparel, Inc. (3551); Blair Credit Services Corporation (5966); Blair Factoring Company (4679); Blair Holdings, Inc. (0022); Blair International Holdings, Inc. (8962); Blair LLC (1670); Blair Payroll, LLC (1670); Draper's & Damon's Acquisition LLC (1760); Draper's & Damon's LLC (2759); Fairview Advertising, LLC (2877); Gold Violin LLC (0873); Haband Acquisition LLC (8765); Haband Company LLC (8496); Haband Oaks, LP (8036); Haband Online, LLC (1109); Haband Operations, LLC (2794); Johnny Appleseed's, Inc. (5560); Linen Source Acquisition LLC (2920); LM&B Catalog, Inc. (5729); Monterey Bay Clothing Company, Inc. (2076); Norm Thompson Outfitters, Inc. (8344); NTO Acquisition Corporation (0995); Orchard Brands Insurance Agency LLC (4858); and Wintersilks, LLC (0688). The Debtors' main corporate address is 138 Conant Street, Beverly, Massachusetts 01915.

2 Capitalized terms used but not otherwise defined herein shall have the meanings set forth in the Application.

and the Court having jurisdiction to consider the Application and the relief requested therein in accordance with 28 U.S.C. §§ 157 and 1334; and consideration of the Application and the relief requested therein being a core proceeding pursuant to 28 U.S.C. § 157(b)(2); and venue being proper in this Court pursuant to 28 U.S.C. §§ 1408 and 1409; and due and proper notice of the Application being adequate and appropriate under the particular circumstances; and a hearing having been held to consider the relief requested in the Application (the "***Hearing***"); and upon consideration of the First Day Declaration, the Dermont Declaration, the record of the Hearing and all proceedings had before the Court; and the Court having found and determined that the relief sought in the Application is in the best interests of the Debtors' estates, their creditors and other parties in interest, and that the legal and factual bases set forth in the Application and the Dermont Declaration establish just cause for the relief granted herein; and any objections to the requested relief having been withdrawn or overruled on the merits; and the Court being satisfied based on the representations made in the Application and the Dermont Declaration that (a) Moelis does not hold or represent an interest adverse to the Debtors' estates and (b) Moelis is a "disinterested person" as defined in section 101(14) of the Bankruptcy Code as required by section 327(a) of the Bankruptcy Code, Bankruptcy Rule 2014 and Local Rule 2014-1; and after due deliberation and sufficient cause appearing therefor, it is hereby ORDERED:

1. The Application is granted to the extent provided herein, *nunc pro tunc* to the Petition Date.

2. In accordance with sections 327(a) and 328(a) of the Bankruptcy Code, Bankruptcy Rules 2014(a) and 2016 and Local Rules 2014-1, 2016-1 and 2016-2, the Debtors are authorized to employ and retain Moelis in accordance with the terms and conditions set forth

in the Engagement Letter, to pay fees and reimburse expenses[3] and to provide indemnification, contribution and/or reimbursement to Moelis on the terms and at the times specified in the Engagement Letter, *nunc pro tunc* to the Petition Date.

3. The provisions set forth in the Engagement Letter (and all attachments thereto) are hereby approved, except as otherwise expressly provided herein.

4. The Debtors are authorized to pay Moelis' fees and to reimburse Moelis for its costs and expenses as provided in the Engagement Letter, including in-sourced document production costs, travel costs, meals and the fees, disbursements and other charges of Moelis' external legal counsel.

5. Moelis will file applications for interim and final allowance of compensation and reimbursement of expenses pursuant to the procedures set forth in sections 330 and 331 of the Bankruptcy Code, such Bankruptcy Rules as may then be applicable, from time to time, and such procedures as may be fixed by order of this Court; *provided, however*, that the requirements of the Bankruptcy Code, the Bankruptcy Rules, the Trustee Guidelines and Local Rule 2016-2 are hereby modified such that Moelis' restructuring professionals shall be required only to keep summary time records in one hour increments, Moelis' non-restructuring professionals shall not be required to keep time records, Moelis' professionals shall not be required to keep time records on a project category basis and Moelis shall not be required to provide or conform to any schedules of hourly rates.

6. Moelis shall be compensated in accordance with the terms of the Engagement Letter and, in particular, all of Moelis' fees and expenses in these chapter 11 cases, including the

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[3] Except with respect to the U.S. Trustee, Moelis' fees and expenses are not subject to review under section 330 of the Bankruptcy Code.

Retainer, Monthly Fee, Sale Transaction Fee, Restructuring Fee and Capital Transaction Fee, are hereby approved pursuant to section 328(a) of the Bankruptcy Code. Notwithstanding anything to the contrary herein, the fees and expenses payable to Moelis pursuant to the Engagement Letter shall be subject to review only pursuant to the standards set forth in section 328(a) of the Bankruptcy Code and shall not be subject to the standard of review set forth in section 330 of the Bankruptcy Code, except by the U.S. Trustee. This Order and the record relating to the Court's consideration of the Application shall not prejudice or otherwise affect the rights of the U.S. Trustee to challenge the reasonableness of Moelis' compensation and expense reimbursements under sections 330 and 331 of the Bankruptcy Code. Accordingly, nothing in this Order or the record shall constitute a finding of fact or conclusion of law binding on the U.S. Trustee, on appeal or otherwise, with respect to the reasonableness of Moelis' compensation.

7. The indemnification provisions included in Annex B to the Engagement Letter are approved during the pendency of these cases subject to the following modifications:

a. The Debtors shall have no obligation to indemnify any Indemnified Person (as defined in the Engagement Letter), or provide contribution or reimbursement to any Indemnified Person, for any claim or expense that is either: (i) judicially determined (the determination having become final) to have arisen from the Indemnified Person's gross negligence, willful misconduct, bad faith or self-dealing to which the Debtors have not consented; (ii) for a contractual dispute in which the Debtors allege breach of the Indemnified Person's obligations to maintain the confidentiality of non-public information, unless the Court determines that indemnification, contribution or reimbursement would be permissible pursuant to *In re United Artists Theatre Company, et al.*, 315 F.3d 217 (3d Cir. 2003); or (iii) settled without the Debtors' consent prior to a judicial determination as to the Indemnified Person's gross negligence, willful misconduct, bad faith or uncontested self-dealing but determined by this Court, after notice and a hearing, to be a claim or expense for which such Indemnified Person should not receive indemnity,

contribution or reimbursement under the terms of the Engagement Letter, as modified by this Order.

b. If, before the earlier of (i) the entry of an order confirming a chapter 11 plan in these cases (that order having become a final order no longer subject to appeal) and (ii) the entry of an order closing these chapter 11 cases, any Indemnified Person believes that it is entitled to the payment of any amounts by the Debtors on account of the Debtors' indemnification, contribution and/or reimbursement obligations under the Engagement Letter (as modified by this Order), including, without limitation, the advancement of defense costs, such Indemnified Person must file an application therefor in this Court, and the Debtors may not pay any such amounts to the Indemnified Person before the entry of an order by this Court approving the payment. This subparagraph (b) is intended only to specify the period of time under which the Court shall have jurisdiction over any request for fees and expenses by any Indemnified Persons for indemnification, contribution and/or reimbursement, and not a provision limiting the duration of the Debtors' obligation to indemnify, or make contributions or reimbursements to, Indemnified Persons. All parties in interest shall retain the right to object to any demand by any Indemnified Person for indemnification, contribution and/or reimbursement.

c. Contribution shall not be available to an Indemnified Person under the Engagement Letter if that Indemnified Person's gross negligence, willful misconduct, bad faith or unconsented self-dealing is finally determined by a court or arbitral tribunal to have primarily caused the Losses (as defined in the Engagement Letter); provided that Indemnified Persons shall retain any rights they may have to contribution at common law.

d. Any limitations on any amounts to be contributed by the parties to the Engagement Letter shall be eliminated.

8. The Debtors and Moelis are authorized to take all actions necessary to effectuate the relief granted pursuant to this Order in accordance with the Motion.

9. Notwithstanding the possible applicability of Bankruptcy Rules 6004(h), 7062, 9014 or otherwise, this Order shall be immediately effective and enforceable upon its entry.

10. The Court retains jurisdiction with respect to all matters arising from or related to the interpretation or implementation of this Order.

Date: Feb. 23, 2011
Wilmington, Delaware

Honorable Kevin Gross
United States Bankruptcy Judge

POST-CONFIRMATION AND ISSUES REGARDING SAME

POST CONFIRMATION ISSUES: CASE SUMMARY

In re FRUEHAUF TRAILER CORPORATION, *et al.*, Debtors.
Daniel Harrow, as Successor Trustee of the End of the Road Trust and American Trailer Industries, Inc., Plaintiff,
v.
Chriss Street, Defendant

2010 WL 2109600 (Bkrtcy.C.D.Cal.)

March 5, 2010

United States Bankruptcy Judge Richard M. Neiter

Judge Neiter described this as "a case where a fiduciary lost sight of his mandate to liquidate trust assets for the benefit of the trust's beneficiaries by engaging in unsuccessful business ventures, self-dealing, and violations of the liquidating trust agreement." As a result of this conduct, the trust lost significant sums of money otherwise available for its beneficiaries and delayed their payment through seven years of the trustee's tenure.

This matter arose as an adversary complaint filed by a successor trustee against the former trustee of liquidating trust established pursuant to a chapter 11 debtors' confirmed plan, asserting that liquidating trustee breached his fiduciary duties to the trust and violated the terms of the trust agreement. The liquidating trustee filed a counterclaim for indemnification.

Following a bench trial, the Bankruptcy Court held that the liquidating trustee: (1) breached his duty of loyalty and good faith; (2) breached the trust agreement by using trust assets to acquire a bankrupt trailer manufacturer; (3) breached his duty to keep and render accounts; (4) breached his duty to preserve trust assets and pursue claims of the trust; and (5) breached his duty to keep trust assets separate. Additionally, the Bankruptcy Court held that the successor trustee was entitled to money damages as well as a reduction in liquidating trustee's compensation; and that the liquidating trustee was not entitled to indemnification.

BACKGROUND:

On October 7, 1996, Fruehauf Trailer Corporation, Maryland Shipbuilding & Drydock Company, F.G.R. Inc., Jacksonville Shipyards, Inc., Fruehauf International Limited, Fruehauf Corporation, The Mercer Co., Deutsche-Fruehauf Holding Corporation, MJ Holdings, Inc., and E.L. Devices, Inc. (collectively, the "Debtors," and on behalf of their respective creditors and interest holders, collectively, the "Trust Beneficiaries"), filed petitions for relief under chapter 11 of title 11 of the United States Code, §§ 101, *et seq.* (the "Bankruptcy Code"). The Debtors' Amended Joint Plan of Reorganization ("Plan") was confirmed on September 17, 1998. The Plan contemplated the creation of a Delaware common law liquidating trust to liquidate the Debtors' assets

for the benefit of the Trust Beneficiaries. On October 27, 1998, Street and the Debtors entered into a Liquidating Trust Agreement ("Trust Agreement") which created The End of the Road Trust ("Trust").

Trust assets were placed in six special purpose entities: (i) JSI Property Corp.; (ii) Hogan's Creek Realty, Inc.; (iii) Picketsville Realty, Inc.; (iv) Mayport Realty Inc.; (v) JSI Lexington Realty Inc.; and (vi) FrudeMex, Inc. ("*FrudeMex* "). FrudeMex was a Delaware corporation formed for the sole purpose of holding the stock of Fruehauf de Mexico, S.A. de C.V. ("FdM "), a Mexican operating company, and the most valuable asset of the Trust. As trustee, Street became the sole director and President of FrudeMex. At the time the Trust was created, the Trust had an aggregate value of $21 million. In addition, the Pension Transfer Corporation (the "PTC") was created and included in the Trust estate to facilitate the ongoing sponsorship and administration of the Fruehauf Trailer Corporation Employees' defined benefit pension plan ("Pension Plan").

Beginning December 31, 1998, FrudeMex underwent several corporate form and name changes until November 8, 1999, when FrudeMex (then, FDM, Inc.) ultimately changed its name to American Trailer Industries, Inc. ("ATII"). During this time, Street was the sole director of ATII from November 19, 1999 through August 1, 2005.

Defendant acted as trustee for the Trust from October 27, 1998, to August 1, 2005 when Plaintiff took over as successor trustee. As liquidating trustee, Street's duties, responsibilities, limitations and rights as trustee were as set forth in the Trust Agreement. The Plan provided Street with indemnification for "claims arising out of the good faith performance of duties under the Bankruptcy Code or this Plan."

Limitations of the Trust

The express purpose of the Trust was set forth in Paragraph 2.3 of the Trust Agreement as follows:

> "This Liquidating Trust is organized for the sole purpose of conserving and liquidating the Trust Estate for the benefit of the Beneficial Interest holders as herein set out, with no objective to engage in the conduct of a trade or business (although companies whose stock is owned by the Liquidating Trust may operate a business). Pursuant to this express purpose, the Trustee is hereby authorized and directed to take all reasonable and necessary actions to conserve and protect the Trust Estate and to sell, lease or otherwise dispose of the Trust Estate, and to distribute the net proceeds of such disposition ... in as prompt, efficient and orderly fashion as possible...."

Paragraph 5.4.4 further restricted the trustee's powers under the Trust as follows:

> "[t]he Trustee ... shall not at any time enter into or engage in any trade or business, including, without limitation, the purchase of any asset or property (other than such assets or property as

are necessary to preserve, conserve, and protect the Trust Estate and to carry out the purposes of Section Two, Section Seven, and this Section Five) on behalf of the Trust Estate or the Beneficial Interest holders."

There was no implied duty outside of that which was expressly stated in the Trust Agreement. Moreover, Street was required to seek the Trust Advisory Committee's ("TAC") prior approval for certain trust activities such as:

(a) borrowing money in excess of $500,000 or granting liens on any part of the Trust Estate in excess of $500,000;
(b) selling assets of the Trust Estate with a value in excess of $500,000;
(c) modifying the Plan;
(d) initiating and prosecuting litigation, including but not limited to claim objections with expected fees and costs in excess of $250,000;
(e) disposing of or settling any claim of litigation with a potential value to the Liquidating Trust in excess of $500,000; and
(f) foregoing or deferring the annual distribution to Class A Beneficial Interest holders,

Violations of the Trust Agreement

In derogation of the express terms and conditions of the Trust, Street caused the Trust to acquire the assets of a bankrupt trailer manufacturer, American Trailer Manufacturing, Inc. ("ATM") through the formation of ATM Acquisition Corp., n/k/a American Trailer, Inc. between October and November 1999. ATM never became profitable for the Trust.

Testimony revealed ATM was purchased in order for FdM, the Trust's operating company, to have a presence in the United States market by using ATM's trademark. Hence, the two companies engaged in business where ATII would cover ATM's payroll and accounts payable and FdM would sell to and purchase goods from ATM. Neither the TAC nor the Delaware Bankruptcy Court authorized FdM or ATII to engage in such business transactions with ATM. ATM eventually dissolved in 2003. There was no evidence that ATM's trademark was sold. **This unauthorized business relation resulted in a loss to FdM totaling $1,112,350.00!**

Contrary to the express limitations of the Trust, Street also caused FdM and ATII to engage in unauthorized business dealings with an entity called Dorsey Trailer Corporation ("Dorsey"), a bankrupt trailer manufacturer in Alabama that Street caused the Pension Plan to purchase in 2001. The Pension Plan acquired Dorsey as a vehicle to enhance the sales and purchasing power of ATII as Street was increasing the operations of the Trust's assets rather than liquidating them.

Dorsey's acquisition was based on Defendant's desire to establish a business presence in the United States by having a factory and a trademark to use in the United States. Street intended to create a synergistic relationship between Dorsey and FdM from which Dorsey would eventually emerge a profitable public company with Street as its CEO and a substantial shareholder.

Similar to its dealings with ATM, ATII transferred funds to Dorsey to cover Dorsey's expenses (in the aggregate of $913,690.25) as Dorsey had inadequate cash flow to pay for all of its operating costs. Likewise, FdM sold finished goods to Dorsey and purchased materials from Dorsey's suppliers (which FdM paid by transferring funds through Dorsey). Street also caused the Trust to advance additional funds to Dorsey totaling $29,242. ATII also paid for certain travel expenses totaling $126,131 which Street and various ATII employees incurred in providing management services to Dorsey. Neither the TAC nor the Delaware Bankruptcy Court approved the foregoing transactions.

Dorsey never became profitable. In September 2004, Dorsey again filed a chapter 11 petition in Alabama. FdM filed a claim in Dorsey's bankruptcy case in the sum of $2,681,363 and ATII filed a claim in the sum of $500,000. No payments were made on account of these claims. **The aggregate of the Trust's losses related to Dorsey amounted to $3,336,736.**

In its decision, the Court found that the Street's purported justification for engaging in business with these entities was to create a business presence in the United States for Fruehauf de Mexico, which was contradictory to the express purpose of the Trust to liquidate Trust assets for its beneficiaries. Not only did these actions violate the express purpose of the trust but, in reality, significantly depleted Trust funds to which Trust Beneficiaries would have been entitled.

Improper Accounting

The extent of Defendant's improper accounting and Defendant's failure to keep adequate books and records during his term as trustee was revealed during trial testimony. Street tried to assign blame for the inaccurate accounting on his bookkeeper, Ms. Dolan. However, while Ms. Dolan was responsible for managing the Trust's books and records, the Court noted that Street, himself, oversaw all of the management activities of the Trust including, without limitation, the information that was placed in the Trust's books and that Street also was provided regularly with financial reports of the Trust. As such, the Court found that Street had full knowledge of any inadequacies in such statements.

The Court also took special note of Defendant's creation of a separate set of books. This lack of proper documentation further evidenced Street's improper record-keeping as the Trust's fiduciary.

The absence of proper books and records also prevented ATII's and FdM's accountants from opining on the consolidated financial statements that would have enabled ATII to save over $1.5 million in taxes. In addition the improper records also became a major obstacle to selling FdM.

Street's Compensation as Trustee and Self-Dealing

The Court adopted the decision of Judge Peter J. Walsh, as contained in his Memorandum of Decision dated September 17, 2008, which found that the Disclosure Statement, Plan and Trust Agreement were the sole governing documents for Defendant's compensation.[1] As such, Judge Walsh invalidated the provisions of the purported employment agreement with the Trust and the purported employment agreement with FrudeMex to the extent that they contradicted the Trust's express language.

As disclosed in the Disclosure Statement, Street was entitled to receive an annual salary of $200,000 for serving as trustee and $50,000 for serving as Chairman and CEO of FdM. He was also entitled to receive "all reasonable out-of-pocket expenses incurred in the performance of his duties." As the Chairman and CEO of FdM, he was provided with "all fringe benefits and perquisites that [were] provided to senior executives of FdM, ... all employee benefit plans, programs and arrangements...." In violation of the terms of his compensation, Street paid himself an additional $242,544 during his term from 1998-2005.

Similarly, FdM reimbursed Street for his personal expenses and charitable contributions in violation of the authorized terms of his compensation. The record demonstrated that Defendant's company credit card was used for both work and personal expenses. **Because of these reimbursements, the Trust lost an additional $203,754.**

In addition to paying for his personal expenses, testimony revealed that Street also permitted his own companies, Street Asset Management Co. and Chriss Street and Co., to use Trust assets, such as office space, telephone numbers, e-mails, and personnel, without reimbursing the Trust for their use.

Other Acts of Mismanagement

In addition to the aforementioned, Street also caused the Trust's fiduciary liability and director and officer liability policies to be changed into "runoff" status which made it difficult for the successor trustee to obtain standard (non-runoff) coverage without paying a substantially higher premium.

Second, Street also neglected certain adversary proceedings that were pending at the onset of the Trust. As a result of this neglect, these proceedings became stale and made it difficult for the successor trustee to revive and litigate the Trust's remaining claims.

Third, Street also destroyed certain files contained in an Apple computer the Trust owned by reformatting the hard drive causing all information therein to be erased.

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[1] Subsequent to this decision, Judge Walsh transferred the matter to California.

Lastly, evidence also demonstrated that Street attempted to derail the sale of FdM on two occasions. American Capital Services ("ACS") initially expressed interest in purchasing FdM in 2004. Subsequent to expressing an interest, ACS encountered difficulty in dealing with Street and *vice versa*. Street also unreasonably withheld an essential environmental report which ultimately led to ACS withdrawing its expression of interest. In 2005, ACS renewed its interest in purchasing FdM. However, tax problems emerged that caused the sale to fall apart—problems which were ultimately the result of Street failing to effectuate the timely filing of consolidated tax returns.

HELD:

Trust Law not Corporate Law Applies

The Court found that the laws of the State of Delaware and common law on trusts governed the Trust Agreement and the disposition of the proceeding. Under trust law, the Court found that the burden to justify the upholding of a transaction by an interested trustee rests on the fiduciary and not the beneficiary. *Id.* (citing *Stegemeier v. Magness,* 728 A.2d 557, 563 (1999)).

In so finding, the Court rejected Street's argument that the "business judgment rule" applied to the liquidating trust and noted that when reviewing allegations of self-dealing, the standards of trust law and corporation law are different. *Id.* (citing *Stegemeier,* 728 A.2d at 562). Unlike corporate law, self-dealing on the part of a trustee is virtually prohibited under trust law. *Id.* at 563. Accordingly, the Court held Street to a higher standard of complete loyalty than that imposed upon a director or officer of a corporation and rejected the lesser standard of the "business judgment rule."

The Court then found that Street failed to meet the higher standard when he (i) allowed the depletion of Trust assets by facilitating the transactions among FdM, the Trust, ATII, ATM and Dorsey for which the Trust, ATII and FdM were never reimbursed; (ii) purchased companies with the ultimate intent of creating a public trailer conglomerate for which he could serve as the CEO and a major shareholder; (iii) permitted the payment of his personal expenses without justification; (iv) risked losing the Fruehauf license by not paying royalties; (v) hindered the sale of FdM; (vi) engaged in improper accounting of books and records; and (vii) created obstacles that made it difficult to replace him as trustee in an effort to keep his position.

Defendant breached his duty of loyalty and good faith

The Court then found that Street breached his duty of loyalty when he permitted the Pension Plan to acquire Dorsey knowing that the Trust would have to provide funds and management to Dorsey. The Court observed that the Dorsey acquisition was part of a scheme involving the Trust, ATII and FdM to do business with Dorsey in order to establish a new trailer company—a company in which Street would become the CEO. The transactions among those entities were not a

fair equivalent exchange, but instead, caused the Trust to lose money.

Street also breached his duty of loyalty when he permitted intercompany transfers between the ATM and FdM, for which no equivalent exchange occurred, causing FdM to lose $1,112,350, and when he allowed Trust assets to be diverted to pay for his personal expenses and to pay his salary in excess of that authorized.

Defendant breached the Trust Agreement

The Count held that Street breached the Trust Agreement[2] when he affirmatively recommended to the TAC that the Trust acquire ATM. Street also breached the fundamental purpose of the Trust when he permitted FdM to conduct business through Dorsey, thus creating an additional loss to the Trust in the aggregate amount of $3,336,736.

Moreover, the Court found that Street's actions derailed the sale of FdM, which was also a breach of the Trust Agreement. Street compounded this breach by, among other things, failing to salvage the souring deal with ACS, by failing to file consolidated tax returns for the Trust entities, by failing to maintain adequate books and records from which consolidated financial statements could be prepared and certified, and unreasonably withholding the requisite environmental report.

Defendant breached his duty to keep and render accounts

The Court also ruled that Street breached his duty to keep and render accounts by either improperly maintaining corporate records and by actually keeping certain information off of the Trust's books and records.

Defendant breached his duty to preserve Trust assets

The Court also found that Street failed to preserve trust assets when he permitted the Trust's fiduciary liability and director and officer liability policies to go into "runoff" status causing difficulty for the successor trustee to obtain standard coverage at a higher premium. Street was found to have willfully breached his duty to preserve trust assets when he destroyed the Trust's files contained in the Trust's computer.

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[2] The Trust Agreement expressly prohibited the Trust from conducting any trade other than the preexisting business of the Trust. It also prohibited purchasing assets or property other than that necessary to preserve, conserve, and protect trust assets in carrying out the Trust's express purpose to liquidate. The main purpose of the Trust was to "conserve[e] and liquidat[e] the Trust Estate for the benefit of the Beneficial Interest holders ... with no objective to engage in the conduct of a trade or business (although companies whose stock is owned by the Liquidating Trust may operate a business)." The Trust also precluded any investment other than interest-bearing deposits or certificates of deposit, among others.

Defendant breached his duty to keep trust assets separate

By permitting his own companies, Street Asset Management Co. and Chriss Street and Co., to use Trust assets, such as office space, telephone numbers, e-mails, and personnel, without reimbursing the Trust for their use, the Court concluded that Street breached his duty to keep trust assets separate and was personally enriched by having his companies' expenses paid for by using Trust assets.

Damages

In light of these significant breaches, the Court found that the Successor Trustee was entitled to judgment against Street in the form of (i) money damages arising from his breach of duty and breach of Trust Agreement, and (ii) a reduction in his compensation in excess of his authorized compensation including reimbursement for his personal expenses.

Counter-Claim: Indemnification

Finally, the Court rejected Street's defense that his actions were entirely based upon advice of counsel and, as such, he was entitled to indemnification from the Trust. In rejecting Street's counterclaim for indemnification, the Court ruled that Street was not entitled to indemnification as the evidence showed that Street willfully and knowingly engaged in the aforementioned acts of self-dealing. The Court also found that Street's conduct amounted to gross negligence and willful misconduct in violation of the Trust Agreement.

POST CONFIRMATION: CASE SUMMARIES

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

Issue:

Whether or not a law firm who represented the debtors prepetition should be disqualified from representing defendants in an adversary proceeding commenced by the chapter 7 trustee to set aside certain prepetition payments by the debtors

Summary:

In this case, the defendant, Sun Captial Partners, Inc. ("Sun"), through an affiliate, acquired all of the outstanding stock of Indalex Inc. and Indalex Limited (the "Indalex Entities") by way of a stock purchase agreement with Honeywell International, Inc., in February of 2006. On March 20, 2009, Indalex, Inc., along with certain of its affiliates, (the "Debtors"), filed for bankruptcy protection under Chapter 11 of the Bankruptcy Code. The Debtors subsequently sold substantially all of their assets and, on October 30, 2009, their cases were converted to cases under Chapter 7. George L. Miller was appointed the Chapter 7 trustee (the "Trustee").

On July 30, 2010, the Trustee initiated an adversary proceeding (the "Adversary Action") against eight companies, including, Sun, and fourteen individuals (the "Defendants") to recover certain prepetition transfers and for damages related to breaches of fiduciary duties occurring after Sun's buyout of the Indalex Entities and Sun's resulting control thereof. In his complaint, the Trustee alleged that the Defendants used such control to extract money from the Indalex Entities through transaction fees, management fees, and by declaring improper dividends. Moreover, the Trustee alleged that the Defendants masked what were actually equity infusions in the Debtors as secured loans.

The Defendants retained the law firm of Kirkland and Ellis ("K&E") to represent them in the Adversary Action. K&E previously represented Sun and its affiliates since February of 2000. K&E additionally represented the Debtors from approximately 2006 through 2009. Due to K&E's prior representation of the Debtors, the Trustee moved for their disqualification as counsel to the Defendants in the Adversary Action (the "Motion"). K&E opposed the Motion asserting that the Debtors had waived any potential conflict, the Trustee's claims were not substantially related to K&E's work for the Debtors, the Trustee failed to show that K&E obtained any confidential information from the Debtors, the Trustee waived any conflict through his delay in seeking disqualification and disqualification would unfairly prejudice the Defendants and reward the Trustee.

The Court first considered whether or not K&E's representation of the Debtors was "substantially related" to the claims raised in the Adversary Action and found in the affirmative. In reaching such determination, the Court looked to the test set forth in the *Meridian* opinion, and opined that "matters may be substantially related on two separate bases: (1) if they involve the same transaction or (2) if there is a risk that the attorney gained confidential, relevant information from the former client." *In re Meridian Automotive Systems-Composite Operations, Inc.*, 340 B.R. 740, 747 (Bankr. D. Del. 2006). In this case, the Court found that the billing invoices produced by K&E to the Trustee demonstrated that K&E had extensive dealings with the Debtors and that such dealings were directly related to the issues raised in the Adversary Action. The Court specifically noted that K&E, upon the basis of a solvency opinion, drafted the board resolution authorizing the very dividend payment which was under attack in the Adversary Action. Since the Court found the matters to be substantially related, it was not necessary to decide whether or not K&E had obtained confidential information.

The Court turned next to K&E's assertion that the Debtors had waived any potential conflict. The Court found that a client may consent to conflicts through signing a waiver, however, the effectiveness of such waiver depends on "the extent to which the client reasonably understands the material risks that the waiver entails." *Model Rule 1.7*, comment 22. The Court further noted that general, open-ended waivers, usually, are not effective while comprehensive waivers and those agreed to by sophisticated clients, are more likely to be effective. *Id.* In this instance the Court found the waiver at issue to be "explicit and narrow" and that it was signed by the CFO of one of the Debtors who was a sophisticated business person. Thus, the Court found the Debtors' consent to be effective; however, such consent was limited to Sun and its affiliates, which included six of the eight corporate defendants and none of the individual defendants.

Lastly, the Court considered whether or not the Trustee failed to raise the issue of disqualification promptly thereby implicitly waiving his disqualification argument. K&E asserted that the motion for disqualification was filed late in the Adversary Action, noting that the Official Committee of Unsecured Creditors (the "Committee") first contemplated filing the Adversary Action prior to the conversion to Chapter 7 and that neither the Committee nor, later, the Trustee raised the issue of disqualification during pre-complaint settlement negotiations. K&E argued the prior failure to raise the disqualification issue provided the grounds for finding an implied waiver on the Trustee's part. The Court found that only the Trustee's actions following the filing of the Adversary Action were at issue, there was no undue delay on the Trustee's part in raising disqualification, and, as such, the Trustee did not waive his disqualification argument.

In conclusion, the Court denied the motion as to Sun and its affiliates and granted the motion as to the remaining defendants. While the Court's decision cleared the way for K&E to continue its representation of the six Sun defendants, the Court noted that K&E may end up in a tenuous position should the Trustee later elect to waive attorney/client privilege and call K&E as a fact witness in the Adversary Action.

POST CONFIRMATION ISSUES: CASE SUMMARY

In re FRUEHAUF TRAILER CORPORATION, *et al.*, Debtors.
Daniel Harrow, as Successor Trustee of the End of the Road Trust and American Trailer Industries, Inc., Plaintiff,
v.
Chriss Street, Defendant

2010 WL 2109600 (Bkrtcy.C.D.Cal.)

March 5, 2010

United States Bankruptcy Judge Richard M. Neiter

Judge Neiter described this as "a case where a fiduciary lost sight of his mandate to liquidate trust assets for the benefit of the trust's beneficiaries by engaging in unsuccessful business ventures, self-dealing, and violations of the liquidating trust agreement." As a result of this conduct, the trust lost significant sums of money otherwise available for its beneficiaries and delayed their payment through seven years of the trustee's tenure.

This matter arose as an adversary complaint filed by a successor trustee against the former trustee of liquidating trust established pursuant to a chapter 11 debtors' confirmed plan, asserting that liquidating trustee breached his fiduciary duties to the trust and violated the terms of the trust agreement. The liquidating trustee filed a counterclaim for indemnification.

Following a bench trial, the Bankruptcy Court held that the liquidating trustee: (1) breached his duty of loyalty and good faith; (2) breached the trust agreement by using trust assets to acquire a bankrupt trailer manufacturer; (3) breached his duty to keep and render accounts; (4) breached his duty to preserve trust assets and pursue claims of the trust; and (5) breached his duty to keep trust assets separate. Additionally, the Bankruptcy Court held that the successor trustee was entitled to money damages as well as a reduction in liquidating trustee's compensation; and that the liquidating trustee was not entitled to indemnification.

BACKGROUND:

On October 7, 1996, Fruehauf Trailer Corporation, Maryland Shipbuilding & Drydock Company, F.G.R. Inc., Jacksonville Shipyards, Inc., Fruehauf International Limited, Fruehauf Corporation, The Mercer Co., Deutsche-Fruehauf Holding Corporation, MJ Holdings, Inc., and E.L. Devices, Inc. (collectively, the "Debtors," and on behalf of their respective creditors and interest holders, collectively, the "Trust Beneficiaries"), filed petitions for relief under chapter 11 of title 11 of the United States Code, §§ 101, *et seq.* (the "Bankruptcy Code"). The Debtors' Amended Joint Plan of Reorganization ("Plan") was confirmed on September 17, 1998. The Plan contemplated the creation of a Delaware common law liquidating trust to liquidate the Debtors' assets

for the benefit of the Trust Beneficiaries. On October 27, 1998, Street and the Debtors entered into a Liquidating Trust Agreement ("Trust Agreement") which created The End of the Road Trust ("Trust").

Trust assets were placed in six special purpose entities: (i) JSI Property Corp.; (ii) Hogan's Creek Realty, Inc.; (iii) Picketsville Realty, Inc.; (iv) Mayport Realty Inc.; (v) JSI Lexington Realty Inc.; and (vi) FrudeMex, Inc. ("*FrudeMex* "). FrudeMex was a Delaware corporation formed for the sole purpose of holding the stock of Fruehauf de Mexico, S.A. de C.V. ("FdM "), a Mexican operating company, and the most valuable asset of the Trust. As trustee, Street became the sole director and President of FrudeMex. At the time the Trust was created, the Trust had an aggregate value of $21 million. In addition, the Pension Transfer Corporation (the "PTC") was created and included in the Trust estate to facilitate the ongoing sponsorship and administration of the Fruehauf Trailer Corporation Employees' defined benefit pension plan ("Pension Plan").

Beginning December 31, 1998, FrudeMex underwent several corporate form and name changes until November 8, 1999, when FrudeMex (then, FDM, Inc.) ultimately changed its name to American Trailer Industries, Inc. ("ATII"). During this time, Street was the sole director of ATII from November 19, 1999 through August 1, 2005.

Defendant acted as trustee for the Trust from October 27, 1998, to August 1, 2005 when Plaintiff took over as successor trustee. As liquidating trustee, Street's duties, responsibilities, limitations and rights as trustee were as set forth in the Trust Agreement. The Plan provided Street with indemnification for "claims arising out of the good faith performance of duties under the Bankruptcy Code or this Plan."

Limitations of the Trust

The express purpose of the Trust was set forth in Paragraph 2.3 of the Trust Agreement as follows:

> "This Liquidating Trust is organized for the sole purpose of conserving and liquidating the Trust Estate for the benefit of the Beneficial Interest holders as herein set out, with no objective to engage in the conduct of a trade or business (although companies whose stock is owned by the Liquidating Trust may operate a business). Pursuant to this express purpose, the Trustee is hereby authorized and directed to take all reasonable and necessary actions to conserve and protect the Trust Estate and to sell, lease or otherwise dispose of the Trust Estate, and to distribute the net proceeds of such disposition ... in as prompt, efficient and orderly fashion as possible...."

Paragraph 5.4.4 further restricted the trustee's powers under the Trust as follows:

> "[t]he Trustee ... shall not at any time enter into or engage in any trade or business, including, without limitation, the purchase of any asset or property (other than such assets or property as

are necessary to preserve, conserve, and protect the Trust Estate and to carry out the purposes of Section Two, Section Seven, and this Section Five) on behalf of the Trust Estate or the Beneficial Interest holders."

There was no implied duty outside of that which was expressly stated in the Trust Agreement. Moreover, Street was required to seek the Trust Advisory Committee's ("TAC") prior approval for certain trust activities such as:

(a) borrowing money in excess of $500,000 or granting liens on any part of the Trust Estate in excess of $500,000;
(b) selling assets of the Trust Estate with a value in excess of $500,000;
(c) modifying the Plan;
(d) initiating and prosecuting litigation, including but not limited to claim objections with expected fees and costs in excess of $250,000;
(e) disposing of or settling any claim of litigation with a potential value to the Liquidating Trust in excess of $500,000; and
(f) foregoing or deferring the annual distribution to Class A Beneficial Interest holders,

Violations of the Trust Agreement

In derogation of the express terms and conditions of the Trust, Street caused the Trust to acquire the assets of a bankrupt trailer manufacturer, American Trailer Manufacturing, Inc. ("ATM") through the formation of ATM Acquisition Corp., n/k/a American Trailer, Inc. between October and November 1999. ATM never became profitable for the Trust.

Testimony revealed ATM was purchased in order for FdM, the Trust's operating company, to have a presence in the United States market by using ATM's trademark. Hence, the two companies engaged in business where ATII would cover ATM's payroll and accounts payable and FdM would sell to and purchase goods from ATM. Neither the TAC nor the Delaware Bankruptcy Court authorized FdM or ATII to engage in such business transactions with ATM. ATM eventually dissolved in 2003. There was no evidence that ATM's trademark was sold. **This unauthorized business relation resulted in a loss to FdM totaling $1,112,350.00!**

Contrary to the express limitations of the Trust, Street also caused FdM and ATII to engage in unauthorized business dealings with an entity called Dorsey Trailer Corporation ("Dorsey"), a bankrupt trailer manufacturer in Alabama that Street caused the Pension Plan to purchase in 2001. The Pension Plan acquired Dorsey as a vehicle to enhance the sales and purchasing power of ATII as Street was increasing the operations of the Trust's assets rather than liquidating them.

Dorsey's acquisition was based on Defendant's desire to establish a business presence in the United States by having a factory and a trademark to use in the United States. Street intended to create a synergistic relationship between Dorsey and FdM from which Dorsey would eventually emerge a profitable public company with Street as its CEO and a substantial shareholder.

Similar to its dealings with ATM, ATII transferred funds to Dorsey to cover Dorsey's expenses (in the aggregate of $913,690.25) as Dorsey had inadequate cash flow to pay for all of its operating costs. Likewise, FdM sold finished goods to Dorsey and purchased materials from Dorsey's suppliers (which FdM paid by transferring funds through Dorsey). Street also caused the Trust to advance additional funds to Dorsey totaling $29,242. ATII also paid for certain travel expenses totaling $126,131 which Street and various ATII employees incurred in providing management services to Dorsey. Neither the TAC nor the Delaware Bankruptcy Court approved the foregoing transactions.

Dorsey never became profitable. In September 2004, Dorsey again filed a chapter 11 petition in Alabama. FdM filed a claim in Dorsey's bankruptcy case in the sum of $2,681,363 and ATII filed a claim in the sum of $500,000. No payments were made on account of these claims. **The aggregate of the Trust's losses related to Dorsey amounted to $3,336,736.**

In its decision, the Court found that the Street's purported justification for engaging in business with these entities was to create a business presence in the United States for Fruehauf de Mexico, which was contradictory to the express purpose of the Trust to liquidate Trust assets for its beneficiaries. Not only did these actions violate the express purpose of the trust but, in reality, significantly depleted Trust funds to which Trust Beneficiaries would have been entitled.

Improper Accounting

The extent of Defendant's improper accounting and Defendant's failure to keep adequate books and records during his term as trustee was revealed during trial testimony. Street tried to assign blame for the inaccurate accounting on his bookkeeper, Ms. Dolan. However, while Ms. Dolan was responsible for managing the Trust's books and records, the Court noted that Street, himself, oversaw all of the management activities of the Trust including, without limitation, the information that was placed in the Trust's books and that Street also was provided regularly with financial reports of the Trust. As such, the Court found that Street had full knowledge of any inadequacies in such statements.

The Court also took special note of Defendant's creation of a separate set of books. This lack of proper documentation further evidenced Street's improper record-keeping as the Trust's fiduciary.

The absence of proper books and records also prevented ATII's and FdM's accountants from opining on the consolidated financial statements that would have enabled ATII to save over $1.5 million in taxes. In addition the improper records also became a major obstacle to selling FdM.

Street's Compensation as Trustee and Self-Dealing

The Court adopted the decision of Judge Peter J. Walsh, as contained in his Memorandum of Decision dated September 17, 2008, which found that the Disclosure Statement, Plan and Trust Agreement were the sole governing documents for Defendant's compensation.[1] As such, Judge Walsh invalidated the provisions of the purported employment agreement with the Trust and the purported employment agreement with FrudeMex to the extent that they contradicted the Trust's express language.

As disclosed in the Disclosure Statement, Street was entitled to receive an annual salary of $200,000 for serving as trustee and $50,000 for serving as Chairman and CEO of FdM. He was also entitled to receive "all reasonable out-of-pocket expenses incurred in the performance of his duties." As the Chairman and CEO of FdM, he was provided with "all fringe benefits and perquisites that [were] provided to senior executives of FdM, ... all employee benefit plans, programs and arrangements...." In violation of the terms of his compensation, Street paid himself an additional $242,544 during his term from 1998-2005.

Similarly, FdM reimbursed Street for his personal expenses and charitable contributions in violation of the authorized terms of his compensation. The record demonstrated that Defendant's company credit card was used for both work and personal expenses. **Because of these reimbursements, the Trust lost an additional $203,754.**

In addition to paying for his personal expenses, testimony revealed that Street also permitted his own companies, Street Asset Management Co. and Chriss Street and Co., to use Trust assets, such as office space, telephone numbers, e-mails, and personnel, without reimbursing the Trust for their use.

Other Acts of Mismanagement

In addition to the aforementioned, Street also caused the Trust's fiduciary liability and director and officer liability policies to be changed into "runoff" status which made it difficult for the successor trustee to obtain standard (non-runoff) coverage without paying a substantially higher premium.

Second, Street also neglected certain adversary proceedings that were pending at the onset of the Trust. As a result of this neglect, these proceedings became stale and made it difficult for the successor trustee to revive and litigate the Trust's remaining claims.

Third, Street also destroyed certain files contained in an Apple computer the Trust owned by reformatting the hard drive causing all information therein to be erased.

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[1] Subsequent to this decision, Judge Walsh transferred the matter to California.

Lastly, evidence also demonstrated that Street attempted to derail the sale of FdM on two occasions. American Capital Services ("ACS") initially expressed interest in purchasing FdM in 2004. Subsequent to expressing an interest, ACS encountered difficulty in dealing with Street and *vice versa*. Street also unreasonably withheld an essential environmental report which ultimately led to ACS withdrawing its expression of interest. In 2005, ACS renewed its interest in purchasing FdM. However, tax problems emerged that caused the sale to fall apart—problems which were ultimately the result of Street failing to effectuate the timely filing of consolidated tax returns.

HELD:

Trust Law not Corporate Law Applies

The Court found that the laws of the State of Delaware and common law on trusts governed the Trust Agreement and the disposition of the proceeding. Under trust law, the Court found that the burden to justify the upholding of a transaction by an interested trustee rests on the fiduciary and not the beneficiary. *Id.* (citing *Stegemeier v. Magness,* 728 A.2d 557, 563 (1999)).

In so finding, the Court rejected Street's argument that the "business judgment rule" applied to the liquidating trust and noted that when reviewing allegations of self-dealing, the standards of trust law and corporation law are different. *Id.* (citing *Stegemeier,* 728 A.2d at 562). Unlike corporate law, self-dealing on the part of a trustee is virtually prohibited under trust law. *Id.* at 563. Accordingly, the Court held Street to a higher standard of complete loyalty than that imposed upon a director or officer of a corporation and rejected the lesser standard of the "business judgment rule."

The Court then found that Street failed to meet the higher standard when he (i) allowed the depletion of Trust assets by facilitating the transactions among FdM, the Trust, ATII, ATM and Dorsey for which the Trust, ATII and FdM were never reimbursed; (ii) purchased companies with the ultimate intent of creating a public trailer conglomerate for which he could serve as the CEO and a major shareholder; (iii) permitted the payment of his personal expenses without justification; (iv) risked losing the Fruehauf license by not paying royalties; (v) hindered the sale of FdM; (vi) engaged in improper accounting of books and records; and (vii) created obstacles that made it difficult to replace him as trustee in an effort to keep his position.

Defendant breached his duty of loyalty and good faith

The Court then found that Street breached his duty of loyalty when he permitted the Pension Plan to acquire Dorsey knowing that the Trust would have to provide funds and management to Dorsey. The Court observed that the Dorsey acquisition was part of a scheme involving the Trust, ATII and FdM to do business with Dorsey in order to establish a new trailer company—a company in which Street would become the CEO. The transactions among those entities were not a

fair equivalent exchange, but instead, caused the Trust to lose money.

Street also breached his duty of loyalty when he permitted intercompany transfers between the ATM and FdM, for which no equivalent exchange occurred, causing FdM to lose $1,112,350, and when he allowed Trust assets to be diverted to pay for his personal expenses and to pay his salary in excess of that authorized.

Defendant breached the Trust Agreement

The Count held that Street breached the Trust Agreement[2] when he affirmatively recommended to the TAC that the Trust acquire ATM. Street also breached the fundamental purpose of the Trust when he permitted FdM to conduct business through Dorsey, thus creating an additional loss to the Trust in the aggregate amount of $3,336,736.

Moreover, the Court found that Street's actions derailed the sale of FdM, which was also a breach of the Trust Agreement. Street compounded this breach by, among other things, failing to salvage the souring deal with ACS, by failing to file consolidated tax returns for the Trust entities, by failing to maintain adequate books and records from which consolidated financial statements could be prepared and certified, and unreasonably withholding the requisite environmental report.

Defendant breached his duty to keep and render accounts

The Court also ruled that Street breached his duty to keep and render accounts by either improperly maintaining corporate records and by actually keeping certain information off of the Trust's books and records.

Defendant breached his duty to preserve Trust assets

The Court also found that Street failed to preserve trust assets when he permitted the Trust's fiduciary liability and director and officer liability policies to go into "runoff" status causing difficulty for the successor trustee to obtain standard coverage at a higher premium. Street was found to have willfully breached his duty to preserve trust assets when he destroyed the Trust's files contained in the Trust's computer.

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[2] The Trust Agreement expressly prohibited the Trust from conducting any trade other than the preexisting business of the Trust. It also prohibited purchasing assets or property other than that necessary to preserve, conserve, and protect trust assets in carrying out the Trust's express purpose to liquidate. The main purpose of the Trust was to "conserve[e] and liquidat[e] the Trust Estate for the benefit of the Beneficial Interest holders ... with no objective to engage in the conduct of a trade or business (although companies whose stock is owned by the Liquidating Trust may operate a business)." The Trust also precluded any investment other than interest-bearing deposits or certificates of deposit, among others.

Defendant breached his duty to keep trust assets separate

By permitting his own companies, Street Asset Management Co. and Chriss Street and Co., to use Trust assets, such as office space, telephone numbers, e-mails, and personnel, without reimbursing the Trust for their use, the Court concluded that Street breached his duty to keep trust assets separate and was personally enriched by having his companies' expenses paid for by using Trust assets.

Damages

In light of these significant breaches, the Court found that the Successor Trustee was entitled to judgment against Street in the form of (i) money damages arising from his breach of duty and breach of Trust Agreement, and (ii) a reduction in his compensation in excess of his authorized compensation including reimbursement for his personal expenses.

Counter-Claim: Indemnification

Finally, the Court rejected Street's defense that his actions were entirely based upon advice of counsel and, as such, he was entitled to indemnification from the Trust. In rejecting Street's counterclaim for indemnification, the Court ruled that Street was not entitled to indemnification as the evidence showed that Street willfully and knowingly engaged in the aforementioned acts of self-dealing. The Court also found that Street's conduct amounted to gross negligence and willful misconduct in violation of the Trust Agreement.