

Publication

New Fee Guidelines for Large Chapter 11s Proposed by the Office of U.S. Trustee: A Case in Favor of the Revisions

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In the aftermath of the Great Recession as Americans downsize, rightsize and laud sensibility, it is only fitting that the growing sentiments of the public turn toward bankruptcy attorneys. After all, in some cases, bankruptcy attorneys have been the last to indulge in much of the pre-Recession era's remaining vestiges of excess. Some bankruptcy attorneys have begun to charge in excess of \$1,000 per hour for services, and these top-dollar rates have pushed administrative fees in chapter 11 cases to new heights.

For example, in the Lehman Brothers bankruptcy case, professional fees topped approximately \$1.6 billion. Professionals in the bankruptcy case of American Airlines' parent company charged approximately \$300 million in fees, and approximately \$110 million in fees were awarded to professionals in the General Motors bankruptcy case. It is hard to imagine the brainpower one must have to expend in order to charge \$16.67 per *minute* (i.e., \$1,000 per hour). By the new chapter 11 fee guidelines, the Office of the U.S. Trustee endeavors to find out. The new chapter 11 fee guidelines will require counsel to meet higher standards of disclosure and transparency aimed to demonstrate that professionals create and substantially adhere to budgets, refrain from unjustified rate increases and charge market rates — not premium ones.

New guidelines for payment of attorneys' fees and expenses in large chapter 11 cases were promulgated by the Office of the U.S. Trustee on June 11, 2013, and supersede fee guidelines that date back to 1996. Other sections of the 1996 guidelines will see updates in the coming months. Under the first phase of reform, the guidelines will apply to fees and expenses requested by attorneys in chapter 11 cases with \$50 million or more in assets and \$50 million or more in liabilities.

The guidelines aim to increase disclosure and transparency in billing practices and encourage market rates. Specifically, the guidelines call for (1) budgets and staffing plans; (2) disclosure if there is a rate increase during the representation and the reason for the increase; (3) use of market billing rates; (4) the submission of billing records in a searchable format; (5) the appointment of independent fee committees and fee examiners in some cases; and (6) the development of model forms and templates for fee applications.

Among other requirements, the guidelines mandate the use of budgets and staffing plans, and these templates are found at Exhibit D to the guidelines. A template for a chart to compare budgeted items against actual fees and expenses incurred is found at Exhibit E to the guidelines. If an area of the budget is exceeded, the applicant seeking fee approval may explain the reasons for the cost overrun. Critics of the guidelines lament the budget and staffing plan requirement and complain that it is too difficult to draft a budget given unknowns in a case. They also complain that disclosure of the budget may give rise to undesired disclosures of case strategy and privileged information.

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The critiques of the budget and staffing plan requirement are rebuttable. As corporations and professionals strive to do more with less, budgets and disclosure of the identity of the professionals who will be staffed on the legal matter, along with their rates, have become par for the course in matters outside of bankruptcy. The Office of the U.S. Trustee modeled the guidelines' sample budget and staffing plans after those suggested for in-house counsel by the Association of Corporate Counsel. Further, the proposed budget and staffing plans, which are prospective in nature, compliment § 330 of the Bankruptcy Code, which sets the criteria for professional compensation.

Retrospective in nature, § 330 allows an award of “reasonable compensation for actual, necessary services” based on a set of factors, which include “whether the services were necessary to the administration of, or beneficial at the time at which the service was rendered toward the completion of, a case under this title;” “whether the services were performed within a reasonable amount of time commensurate with the complexity, importance, and nature of the problem, issue or task addressed;” and “whether the compensation is reasonable based on the customary compensation charged by comparably skilled practitioners in cases other than cases under this title.”

The guidelines' requirement of a budget looks forward in an effort to set out the path to fulfill the factors under § 330. A budget and staffing plan will necessarily be based on assumptions and include caveats should unknowns or variables change the assumptions upon which the budget and staffing plan was based. Further, if the budget is exceeded, when the time for approval of a fee application arrives, the professional should take the opportunity to explain to the court, creditors, shareholders and other parties in interest why it occurred. The explanation for the cost overrun may, in fact, highlight a logjam or point of contention in the case that must be addressed in order for the case to move forward.

Drafting a budget and staffing plan is not a perfect science. However, the guidelines do not require a professional to match his or her budgeted forecast to actual fees incurred to the penny. To do so would be akin to landing a plane on a dime — an unreasonable expectation. The budget and staffing plan requirement does, however, aim to set realistic expectations of the legal costs and expenses that the case may generate at the beginning of the case. Setting realistic client expectations is never a bad thing, and should be encouraged.

The budget and staffing plan must be approved by the client as soon as practicable after the case commences. However, in order to address concerns over disclosure of privileged and confidential information, the budget and staffing plan will be filed retrospectively with the fee application. Redactions that are proportional to the overall fees sought are permissible.

The guidelines also seek to encourage market rates in the bankruptcy system and to discourage inflated billing by bankruptcy professionals by requiring a comparison between the fees sought to be approved in a fee application with fees charged by other professionals in the firm. The guidelines instruct that in order to make the “comparable services analysis,” attorneys must disclose a blended hourly rate billed *or* collected by professionals in its offices, excluding bankruptcy professionals. To that end, the applicants have a choice. Applicants can either disclose the average hourly rate of *all* the timekeepers in their domestic offices (again, excluding the bankruptcy professionals in those offices), or can chose to disclose the average hourly rate of the timekeepers (excluding bankruptcy professionals) in the domestic offices where attorneys billed at least 10 percent of their hours to the bankruptcy case during the application period. The guidelines include a sample worksheet at Exhibit A to assist the applicant in generating the analysis.

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The time has arrived to question whether debtor's counsel should be permitted to charge a fee, which, by the *minute*, is more than double the prevailing minimum *hourly* wage. Some take umbrage with the comparable-services analysis. They say that clients are entitled to their choice of counsel and further investigation into the client's choice of counsel is intrusive and unprecedented. The response to these critics is that the client often does not have the highest stake in the matter. Creditors, shareholders and employees of the debtor are often the parties who stand to lose the most when a bankruptcy estate becomes cannibalized by exorbitant professional fees and these constituents do not choose debtor's counsel and have limited information upon which to gauge the value of the services provided.

Although it is not perfect, the guidelines are a helpful step toward increasing transparency and disclosure and encouraging market rates in large chapter 11 cases. The guidelines compliment § 330 because they do not supersede local rules, standing court orders, statute or other controlling authority. In the end, it is the bankruptcy court's decision whether to award compensation and reimbursement of fees and expenses, and the amount. The guidelines aid in determining eligibility for a fee award by increasing the amount of evidence at the court's disposal to determine whether the requirements of § 330 are met.

The guidelines will apply to attorneys' fees and expenses in cases filed on or after Nov. 1, 2013, that meet the large case threshold. The guidelines will not apply to professionals who are not attorneys that seek compensation from the debtor's estate. The Office of the U.S. Trustee does expect to issue updated guidelines applicable to nonattorney professionals in cases below the large chapter 11 threshold and under other Code chapters in the months to come.