

Three for Three

AMR Court Follows Adelpia And Lehman Rulings

By Veronique A. Urban and
Ted A. Berkowitz

As can be expected, bankruptcy cases often involve numerous claimants holding general unsecured claims against the debtor. As a result, an official committee is usually appointed under Bankruptcy Code section 1102 to represent the interests of all of the debtor's unsecured creditors. Upon approval of the bankruptcy court, Bankruptcy Code section 1103 authorizes the committee to retain attorneys, accountants and other professionals to assist it in performing its services during the course of the bankruptcy case. The committee's professionals are paid by the estate for their services in accordance with Bankruptcy Code sections 503(b)(2) and 330.

Recently, controversy arose when the individual members of the committee sought to have their professional fees paid by the estate. The decision in *In re AMR Corporation, et al.*, Case No. 11-15463 (Bankr. S.D.N.Y. Sept. 13, 2013), highlights a growing trend that allows committee members and other creditors to bypass Bankruptcy Code section 503(b) and have their professional fees paid through a debtor's plan of reorganization.

Veronique A. Urban is an associate and **Ted A. Berkowitz**, a member of this newsletter's Board of Editors, is a partner in the Bankruptcy & Creditors' Rights practice group of Farrell Fritz, P.C. The authors may be contacted at vurban@farrellfritz.com and tberkowitz@farrellfritz.com, respectively.

A BRIEF RECAP OF SECTION 503

Bankruptcy Code section 503 provides a list of claims that are entitled to administrative expense status. Administrative expenses are those that accrue after the filing of the bankruptcy petition and were incurred for the actual and necessary costs of preserving the bankruptcy estate. Under Bankruptcy Code section 503(b)(3)(F), administrative expenses include the "actual, necessary expenses, other than compensation and reimbursement specified in [section 503(b)(4)] of the Bankruptcy Code, incurred by a member of a committee appointed under section 1102 of [the Bankruptcy Code], if such expenses are incurred in the performance of the duties of such committee." While this provision allows for the reimbursement of an individual committee member's expenses, such as travel and lodging expenses, it specifically does not provide for the payment of professional fees incurred by individual committee members.

Bankruptcy Code section 503(b)(4) permits reimbursement of "reasonable compensation for professional fees rendered by an attorney" for certain specified parties listed in section 503(b)(3), but section 503(b)(3)(F) is not one of the enumerated subsections listed in section 503(b)(4). As a result, the professional fees incurred by individual committee members cannot be reimbursed pursuant to Bankruptcy Code section 503(b)(4). Rather, these types of fees are usually paid pursuant to Bankruptcy Code section 503(b)(3)(D), but only if the creditor can show that it made a "substantial contribution" to the bankruptcy case.

THE ISSUE IN *AMR CORPORATION*

The debtors in the *AMR Corporation* cases (the "Debtors") filed a plan of reorganization that included a provision for the consensual reimbursement by the Debtors of the reasonable professional fees and out-of-pocket expenses of the individual members of the creditors' committee. The U.S. Trustee objected to the proposed payments on the basis that Bankruptcy Code section 503(b)(3)(D) provides the exclusive vehicle for creditors to receive these types of fees and that the committee members had not met the requirements under such section.

Bankruptcy Code section 503(b)(3)(D) authorizes the court to allow, as an administrative expense, "the actual, necessary expenses" incurred by a creditor who has made a "substantial contribution" in a Chapter 11 case. In order to show that the creditor has made a substantial contribution, among other things, the creditor must demonstrate that its actions were "extraordinary" and resulted in a "direct, significant and demonstrably positive benefit upon the estate." *In re Best Prods. Co., Inc.*, 173 B.R. 862, 865-66 (Bankr. S.D.N.Y. 1994).

The U.S. Trustee argued that the proposed payments violated Bankruptcy Code section 503(b)(3)(D) because the Debtors' Plan did not require the committee members to establish that they made a substantial contribution in order to receive payment from the estate. The U.S. Trustee concluded in its objection papers that "[b]ecause sections 503(b)(3)(F) and 503(b)(F) are the specific provisions that govern these payments ... the Committee members are prohibited from recovering their attorney and professional fees as administrative

expense payments for their Committee-related work under the Plan.”

The Debtors countered that the proposed payments to the Committee members were not being paid under Bankruptcy Code section 503(b)(3)(D) but, rather, pursuant to Bankruptcy Code sections 1123(b)(6) and 1129(a)(4). Section 1123 governs the required contents of a plan of reorganization and subsection (b)(6) provides that the plan may “include any other appropriate provision not inconsistent with the applicable provisions of [Chapter 11].” Section 1129(a)(4) provides that any payment may be made under a plan so long as such payment “has been approved by, or is subject to the approval of, the court as reasonable.” The Debtors’ position before the court was that the court could approve the proposed payments to the individual committee members without the need for the committee members to meet the stringent evidentiary requirements set forth in Bankruptcy Code section 503(b)(3)(D).

REVIEWING PRECEDENT: ADELPHIA AND LEHMAN BROTHERS

In issuing its decision, the court reviewed two recent cases that had brought similar concerns: *In re Lehman Brothers, Inc.*, 487 B.R. 181 (Bankr. S.D.N.Y. 2013), and *In re Adelphia Commc'ns Corp.*, 441 B.R. 6 (Bankr. S.D.N.Y. 2010). In *Adelphia*, ad hoc committees and individual creditors sought reimbursement of their legal fees and other professional expenses under the debtors’ Chapter 11 plan. The plan, similar to the one proposed by the Debtors, contemplated that the payment of these fees would be subject only to reasonableness and would not require the creditors to satisfy the substantial contribution test set forth under Bankruptcy Code section 503(b)(3)(D). As in the *AMR Corporation* cases, the U.S. Trustee in the *Adelphia* cases objected to the payment of such fees.

The court in *Adelphia* reviewed the text of Bankruptcy Code section 503(b) and noted that “section 503(b) does not provide that it is the *only* way by which individual creditors’ fees may be absorbed by an estate. Nor does any other provision of the Code prohibit their payment; while they may or may not be authorized, they are not forbidden.” *Adelphia*, 441 B.R. at 20-21 (emphasis in original). The court held in that case that creditors could be paid their reasonable fees as part of a Chapter 11

plan pursuant to Bankruptcy Code section 1129(a)(4) without a showing of substantial contribution under section 503(b).

The *Lehman Brothers* cases also presented a similar factual situation. In that case, the debtors’ plan of reorganization provided for the payment of the professional fees of the individual committee members and the U.S. Trustee objected to the payment such fees. In *Lehman Brothers*, the court was keenly aware that “[t]he issue presented, whether to allow the professional fees of the members of the Official Committee of Unsecured Creditors ... focuses attention on the suitability of using plan provisions as a means to authorize the payment of professional fees where it is unclear — or even doubtful — that such fees could be recovered as administrative expenses if payment provisions had not been specified in the Plan.” *Lehman Brothers*, 487 B.R. at 183-184.

After reviewing the various Bankruptcy Code provisions discussed above, the court in *Lehman Brothers* found that the proposed payments to the individual committee members were proper, provided that the payments were reasonable and not inconsistent with applicable provisions of the Bankruptcy Code. The court further reminded the parties to the action that the plan process under Chapter 11 is a creative one and that “the Bankruptcy Code allows and even encourages such creativity ...” *Lehman Brothers*, 487 B.R. at 185.

In reaching its decision the court explicitly rejected the U.S. Trustee’s overly restrictive reading of section 503(b): “Section 503(b) is not a straightjacket [sic], and the provisions of that section directly govern the allowance of administrative claims do not control the plan process.” *Lehman Brothers*, 487 B.R. at 186.

COURT’S DECISION

The court in the *AMR Corporation* bankruptcy cases followed the reasoning set forth in the *Lehman Brothers* and *Adelphia* cases and held that the payment of the professional fees as contemplated by the Debtors’ Plan was permissible pursuant to Bankruptcy Code sections 1129(a)(4) and 1123(b)(6). The matter is not necessarily settled, however. In a footnote to its decision, the court stated that it expected that the parties would file motions seeking approval for the precise amount of fees sought to be paid by the estate to the individual

committee members. The U.S. Trustee, it seems, may have a new opportunity to object to the payment of the individual professional fees if the U.S. Trustee believes that the amount of such fees is not reasonable.

The decision in *AMR Corporation*, taken together with the *Lehman* and *Adelphia* cases, is important for two reasons. The first, and the most obvious, is that the court confirmed that there are other avenues besides Bankruptcy Code section 503(b) that can be used for the payment of individual creditor fees. This is important as it provides an alternative to the tough standards set forth in Bankruptcy Code section 503(b)(3)(D) for the payment of creditor fees.

The second, and perhaps the biggest reason, is that the case provides a useful reminder that in bankruptcy cases, creativity is king and consensus is queen. Attorneys and other professionals have a tendency to recycle arguments when seeking various relief from the bankruptcy court. Whether that is the case due to laxness on the part of the professionals or their confidence that arguments that have worked in the past will succeed once again is a matter not worth debating. What is important, rather, is that attorneys and other professionals should be constantly pushing themselves to review and interpret the provisions of the Bankruptcy Code in new and radical ways.

CONCLUSION

The Bankruptcy Code and the case law interpreting it are not static — there is always a novel argument to be made and courts are ready and willing to listen to such arguments. Of course, it is equally important to build consensus regarding the novel approach to be used. Without the support of the Debtors in *AMR Corporation* (which was no doubt negotiated for in the plan process), it is doubtful that the objections of the U.S. Trustee would have been overruled. So be brave, get motivated, and excite the court with a fresh take on the Bankruptcy Code.