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The Importance of Being Earnest: Bankruptcy Disclosure Rules¹

*Robert Fishman, Honorable Judge John Henry Squires,
Steven Towbin, and Daniel Zazove*

MR. FISHMAN: I got drafted at the last second to moderate this panel because these gentlemen couldn't figure out how to divide their time amicably. I don't have a Blackberry up here with me; it's my watch. I don't want you to think I'm reading my email during this program; it would be very rude.

The title of today's program is "The Importance of Being Earnest: Bankruptcy Disclosure Rules," and some of the presentation is going to be an effort to identify the obligations for disclosure, the circumstances and manner in which you do it. But another part of the discussion I think is going to revolve around what does disclosure resolve and what does disclosure fail to resolve.

There are certain parties I think who sometimes believe that if you just tell everybody what the facts are, the problem which results from those facts sometimes go away. One of the things the panelists are going to talk about is, when will, while disclosure is appropriate, will it not make the problem go away.

So the first thing we want to do is address why we're all gathered here. We have a lot of duties related to disclosure rules in bankruptcy. So gentlemen, when we talk about disclosure rules and obligations, what exactly are we talking about? What do the parties need to understand about disclosure?

MR. TOWBIN: To put the disclosure rules into context, what we're talking about is when a Chapter 11 or Chapter 7 is filed and the debtor in possession, the trustee, or the creditors' committee want to retain counsel, and certain disclosure rules are required — that govern what has to be disclosed to the other party in interest and most importantly, to the court and the U.S. Trustee. Those rules are set forth in the material. Obviously we're not going to go through them in detail, but the whole idea is the court and the parties of interest in the case

1. This is an edited version of the transcript from the third panel at the DEPAUL BUSINESS AND COMMERCIAL LAW JOURNAL SYMPOSIUM, Into the Sunset: Bankruptcy as Scriptwriter of the Dénouement of Financial Distress, held on April 16, 2009.

have to understand what the “connections” are between the counsel that’s being chosen to represent the estate, either the trustee or the debtor in possession or the creditors’ committee and the other parties in the case.

So it’s number one, a disclosure of actual conflicts if there are any, potential conflicts, and then things that perhaps the judge should be aware of while the case is progressing.

MR. ZAZOVE: Why do we have those rules, and why are they in the Bankruptcy Code at all?

MR. TOWBIN: You could really rely, if you wanted, on state rules of conflicts of interest to a certain degree. But I think Congress has taken the position in bankruptcy cases in particular because it’s not generally a plaintiff and a defendant, but multiple parties, and Congress wants to make sure that a full and complete disclosure is made.

MR. ZAZOVE: Do they have any fiduciary obligations to act in that capacity?

MR. TOWBIN: There’s some debate about whether or not you have fiduciary duties to creditors or to people other than your direct client. So yes, I think most people take the position a Chapter 11 debtor’s lawyer does have a fiduciary obligation at least to the estate.

MR. ZAZOVE: The trustee certainly does. So if you start with a trustee and you take the word trust—

MR. TOWBIN: But who does your fiduciary duty really run to? Does it run to the creditors? Does it run to the estate?

MR. ZAZOVE: But the estate is something where all the assets are contained and parties of interest are participants in the estate. So if a trustee is appointed for an estate or for a debtor, that trustee has fiduciary obligations. Isn’t that really the origin of all these rules and provisions?

MR. TOWBIN: That’s part of it, sure.

MR. ZAZOVE: So now instead of a trustee, a debtor stays in possession. Does the debtor in possession occupy the same fiduciary position?

MR. TOWBIN: I think there’s a split of opinion about that. I think there’s clearly this concept that there’s a fiduciary duty that runs from a trustee to creditors of an estate, but I’m not sure that the same fiduciary duty necessarily runs to creditors if you’re representing a debtor in possession. It clearly runs to your client.

MR. ZAZOVE: What about a committee counsel?

MR. TOWBIN: A committee counsel has fiduciary duties to the committee as opposed to general unsecured creditors. The committee

counsel does not represent general unsecured creditors per se individually. They represent them as a class. They really represent the committee. The communications between the committee and the committee counsel would be privileged as opposed to communications between creditors.

MR. ZAZOVE: But a committee occupies the fiduciary position in the bankruptcy case.

MR. TOWBIN: To the unsecured creditor of that class.

MR. ZAZOVE: Or if it's an equity committee to the equity committee.

MR. TOWBIN: That's right.

MR. ZAZOVE: So really the origin of all of these to say that there's a person in a position of a fiduciary and we have to measure that person's independence, loyalty, and ability to act on behalf of his client or his constituency.

MR. TOWBIN: That's correct. No argument.

MR. ZAZOVE: If we trace the origin of bankruptcy back far enough that there were only really trustee, Chapter 10s, and things like those cases, and/or Chapter 7s or trustees, so really it comes about; the origin of it really is the independence of a trustee who is not beholden to one group or another and the professionals and the trustee retained had to be as independent as the trustee.

MR. TOWBIN: But the — no. The trustee could be elected and could be disinterested. Could be elected by the creditors and often-times—

MR. ZAZOVE: Are you saying that you could elect a non-disinterested trustee?

MR. TOWBIN: You absolutely could and as a matter of fact, people do it all time, and used to do it more often. So that's you know, so interesting obviously a debtor in possession is not disinterested in any way. So they're—

MR. FISHMAN: They have fiduciary duties even if you're not disinterested.

MR. TOWBIN: They have fiduciary duties, but the individual who is the officer of the corporation or the general partner of the partnership, their fiduciary duty runs to the entity; it does not run to the creditors.

MR. FISHMAN: Let's focus this discussion a little bit because the debate about what kind of fiduciary duty a debtor in possession's counsel has or does not have to an estate is an interesting topic, but we're not going to resolve it this afternoon.

In the context of why we are making these disclosures, there's rules that require disclosures, but give us the context in which the disclosures are being presented, who is looking at them, and what are they being asked to do when they see them. Dan?

MR. ZAZOVE: They're obviously in connection with retentions of professionals or parties who have a responsibility to carry out these duties in a bankruptcy case. In order to determine the relative dependence or independence of anyone who might be retained we hold up their compensation. You know, I often wonder whether or not you're going to have a completely interested and non-independent person as long as they never sought to be compensated from the estate. Doesn't sound like a good idea, but putting that aside, we're saying, "Look, you want to get paid." We hold the purse and if you want to work for one of these fiduciary parties or in the estate, then we're going to measure your relative dependence or independence. We do that with you disclosing and having everybody else have a shot at determining whether or not you're dependent or independent.

MR. FISHMAN: So we've done this disclosure under Rule 2014.² Who exactly do we need to satisfy with this disclosure? Judge, would you like to address that question?

JUDGE SQUIRES: I'm the one that has to sign the order approving the retention and pass on any objections thereto. In addition, to the points that Dan and Steve made, part of the process is to make it transparent which is very important for legitimizing the entire bankruptcy process.

Previously, under the Act, when referees were appointed by the district judge as political appointees, things were done behind closed doors and the disclosure requirements were not what they are now. There was a perception in this area and other areas that bankruptcy rings, which the disclosure rules are in part intended to dissipate and make the whole proceeding spread of record with certain things that have to be publicly disclosed. And that's an important policy consideration underlying this disclosure requirement. After all, the estate is being administered as a trust estate and if you want to get paid, generally out of the estate as a professional person, you have to be retained under Section 327,³ you have to make the disclosures required under Rule 2014⁴ and what is it 5002,⁵ have a hearing on a notice to the appropriate parties and that's the condition precedent as far as getting

2. Fed. R. Bankr. P. 2014.

3. 11 U.S.C. § 327 (2008).

4. Fed. R. Bankr. P. 2014.

5. Fed. R. Bankr. P. 5002.

paid, especially in the Seventh Circuit after one case that I was intimately familiar with, the *Grabill*⁶ decision.

MR. ZAZOVE: You're raising a good point that everybody gets a shot at objecting to the independence of any of the professionals.

MR. TOWBIN: Who gets notice of these applications? It certainly isn't every creditor in the case.

MR. ZAZOVE: I guess that's right.

MR. TOWBIN: So it's anybody who is really anybody?

MR. ZAZOVE: Just the important people. First of all, you have to rely to a certain extent that parties in interest are filing appearances and requesting them. You're certainly serving them upon your largest creditors, the United States Trustee. In fact, under the new rules you can present your application, but you can't get an order authorizing the retention.

MR. TOWBIN: That's an important thing. The rules have basically been changed to require at least a twenty-day period after an order for relief of a petition to be employed to be entertained by the court unless it's going to cause irreparable harm. I've yet to see a judge think that not entering an order employing a professional is going to have irreparable harm kinds of consequences.

But that rule was changed because obviously on the first day of most Chapter 11 cases, the judge has a stack of motions and all the parties in interest have motions their interested in. Congress in its infinite wisdom decided that they're going to change the rules a little bit and make sure some of the things such as retention of professionals is going to be delayed past the first day.

Now, I have seen cases where interim orders authorizing a retention have been entered. I don't think that's what the rules really intended and I think those interim orders were entered for the purpose of protecting the right to be paid if subsequently it turns out there are professionals not disinterested and cannot be employed.

MR. FISHMAN: Do we think that works? If you're not disinterested or are ultimately determined to be not disinterested, do you think having an interim order entered somehow preserves your right to be paid, or is it something of a hollow gesture to get that interim order?

MR. TOWBIN: I can't speak for other circuits, but certainly in the Seventh Circuit the rule is very clear. Judge Squires indicated in the *Grabill*⁷ case and others if you are not disinterested, it's not going to

6. *Matter of Grabill Corp.*, 983 F.2d 773 (Ill.1993).

7. *Id.*

help you to have an order that appointed you on less than full notice or less than full consideration in the Seventh Circuit. As a matter of fact, it might work against you given opinions that we've seen lately from the Seventh Circuit.

So I would say that kind of order is not necessarily going to help you. Now, there's a certain amount of leeway and discretion I think that courts have in determining who is disinterested, who is not disinterested, and we can get to those cases. As a matter of fact, I don't know if you've taken a look at the materials, but at the end of the materials there's a recent set of case papers that were filed by a firm in Madison, Wisconsin. An objection that was filed by the U.S. Trustee and that was a very interesting process as to how that got worked out and hopefully we'll have some time to talk about that. But it's not as clear-cut on these rules about conflicts and who is disinterested and who is not. So I think that there is some leeway. I haven't seen interim orders in our court in Chicago.

MR. FISHMAN: Judge, has anyone asked you to enter an order like that yet?

JUDGE SQUIRES: No, and I wouldn't do it. The important thing is to get your application on file and then you can notice it up for hearing twenty days out or whatever if you're worried about getting paid. The main thing is just getting the application on file and follow the rules.

MR. FISHMAN: I was involved in a recent case in the Northern District of Florida where they did enter an interim order the first time we appeared in court. It wasn't to retain me so I was not that concerned with its effectiveness or exactly why we were doing it. But counsel for the debtor in possession in that case believed it very important to get that interim order entered because he believed it was of value to him with respect to compensation he might earn during that interim period.

I don't know the difference in the status of the law in the Eleventh Circuit as opposed to the Seventh Circuit, but in the Seventh Circuit I don't think that interim order would be of much value if you ultimately are not found to be disinterested.

MR. ZAZOVE: I'd just pose a question to Judge Squires here. Suppose somebody did file an application day one and it turned out they had a disqualifying conflict. Could you not enter an order authorizing their retention as special counsel for that interim period so they could at least be compensated for the work they did?

JUDGE SQUIRES: That's a possibility. You know, all these things are incredibly fact intensive and I wish practitioners would remember

when these cases hit the court's docket, generally me and my colleagues don't have the foggiest idea who the debtor is. We may know some of the lawyers and other professionals who would be in the case. We don't know anything about it. Especially in Chapter 11, where one of the first day motions is frequently a motion for extension of time to file schedules and statement of financial affairs and all the other paperwork. We don't have a clue as to what the estate consists of, what the problems are. And we realize that you as practitioners may be in a steep learning curve trying to find out what's going on, but we are at the end of the information pipeline, at least at the trial court level. So bear with us. And you know, we'll try to do the right thing, but you have to understand your audience. And on matters in the bankruptcy court generally the judge assigned the case is your main audience, so bear in mind that we don't have the same perspective and background information that you ever will. There's no way I am ever likely going to know the intricacies of the case in front of me and that's because I only see the tip of the litigation iceberg that surfaces in bankruptcy court. I'm not privy to any of the out of court negotiations and contacts et cetera, et cetera, unless and until it comes up during the course of discovery or trial on a contested matter or adversary proceeding. I don't really want to know all of that stuff. I'm just trying to sort through the matter of your case which is one of, on my docket, of about 4,000 other active pending cases.

So you have to keep that in mind and especially in 11s, don't expect the court to be as promptly deciding all this stuff as perhaps you would like. It would be preferred if you'd get everything on file you have to and then stage it out for what's really important early on, that maybe critical other than in the Seventh Circuit, critical to your motions. But just bear in mind we've got dockets to manage and we are, as I said, at the end of the information pipeline. So you know, take your time and try and do it right the first time.

MR. FISHMAN: So here we are ready to get retained. We're going to file a motion whether you're representing a committee, a trustee, or a debtor in possession, you are a professional and along the way someone can take a shot at defining what is included in the concept of professional.

But we file this application and it implicates Rule 2014,⁸ which I'll, one of you who happens to have the rule in front of you can read it so the audience can hear the words, and the word to focus on in Rule

8. Fed. R. Bankr. P. 2014.

2014⁹ is the word connection. So the next part of the discussion that I'd like us really to focus on is what exactly is a connection?

JUDGE SQUIRES: As luck would have it, this is another one of those interesting words that's not a defined term. It's Section 101.¹⁰

MR. FISHMAN: Can I take connection for 200?

JUDGE SQUIRES: Is that your billing rate?

MR. FISHMAN: Now.

JUDGE SQUIRES: My response to the question is you tell me. I don't know anything about connections, but most of the 2014¹¹ applications I see are pretty much vanilla. They're garden variety and we see them mostly in 7s, but we occasionally see them in the 11s. Where it just says Mr. or Miss X is the applicant here for whatever the position is as a professional person and we are, I'm statutorily disinterested and I'm not representing an interest adverse to the estate. So appoint me. That's basically what it says.

MR. ZAZOVE: I think we could talk about some things that we would generally all agree are connections. First of all, if you ever represented the debtor before, that would be a connection. The debtor's officers or directors, its subsidiaries and affiliates, certainly its secured creditors, lenders, and its twenty largest unsecured creditors because you're likely going to have some further interaction with them. Another connection is if there are critical contracts. I think an interesting case was The Tribune representation where the investment banker, who shall remain nameless, was seeking to be retained and failed to disclose they represented The Tribune's largest competitor, the Sun-Times. I don't know whether it was successful or not, but an objection was lodged on the grounds it created an irreconcilable conflict for the investment banker.

MR. FISHMAN: Let me interrupt for a minute to further focus us in this discussion. In the many contexts of discussions that come up about the disclosures that are made in conjunction with retention, people will confuse the two terms connections and conflicts. Often the terms will be used interchangeably, but they are not the same things, don't mean the same things, and don't have the same consequences.

So when we're talking about one or the other, let's try to be specific. In my opinion at least, a connection is merely the identification of a relationship with something or someone that is embodied within Rule

9. Fed. R. Bankr. P. 2014.

10. 11 U.S.C. § 101 (2008).

11. Fed. R. Bankr. P. 2014.

2014.¹² While a conflict is governed by the rules of professional conduct. A connection may or may not be a conflict, while I suppose it's possible a conflict might not be a connection, they probably all are. So as we're talking about connections and conflicts, let's use the words with some exactness.

MR. TOWBIN: Here's an example that came up in a case, as far as a connection. The counsel for the creditors' committee in a relatively small case was going to be required to take on the secured creditor. It turns out the secured creditor in that case had a lien on all the debtor's assets and was the major financing provider to that lawyer's law firm. Should that have been disclosed or not? Was that a connection the secured creditor, because they held the purse strings to the law firm's finances, could use to put pressure on the lawyer to basically take a pass at challenging his lien? It was an issue that came up. It was ultimately disclosed.

I happened to represent a party in interest there and didn't file something with the court. I basically took the lawyer aside and I said, "Hey, don't you think that maybe this is an important connection that you ought to be disclosing to people?" Sure enough, ultimately upon the threat I would file if they didn't, they did file it and it turned out that the judge in that particular case didn't think it was a disqualifying conflict of interest.

MR. FISHMAN: Do you think that's a conflict of interest at all?

MR. TOWBIN: To me it bordered on a conflict of interest. It was a potential conflict and there are issues about whether or not you could be disqualified because of a potential conflict or if it has to be an actual conflict. I think courts have moved away from disqualifying people or not approving their retention because of potential conflicts and now require an actual conflict.

But I think that's something at the very least that has to be disclosed. If I was an unsecured creditor I would want to know the lawyer representing my interests didn't hold its livelihood or ability to pay its employees hostage to a secured creditor who they were going to attack. Is it a conflict? I don't know.

MR. ZAZOVE: Certainly it's a connection.

MR. FISHMAN: And that's the distinction I'm trying to draw. There's no doubt it's a connection and maybe one of you guys can read the pertinent language for 2014¹³ for anyone who is not expressly familiar with it.

12. Fed. R. Bankr. P. 2014.

13. Fed. R. Bankr. P. 2014.

MR. TOWBIN: Unfortunately, the sentence is rather lengthy. It says this is an application to be employed only for professionals retained under 1103,¹⁴ 1114,¹⁵ or 327,¹⁶ and the standards for committee counsel, 3278,¹⁷ and counsel for debtors or trustees really are different; and we'll talk about that in a minute. But 2014 says, "The application shall state the specific facts showing the necessity for the employment, the name of the person to be employed, the reasons for the selection" — somewhat interesting — "the professional services to be rendered, any proposed arrangement for compensation and to the best of the applicant's knowledge all of the person's connections with the debtor, creditors and other parties in interest" — other parties in interest is a pretty broad term — "their respective attorneys and accountants, the United States Trustee or any person employed in the office of the United States Trustee."¹⁸

So you've got some terms there between connections and parties in interest. By the way, do you know everybody who works in the U.S. Trustee's office and who their relatives are, because I sure don't? But that's how broad this is supposed to be. I guess the best rule of thumb is if you think it ought to be disclosed, if there's a question at all, disclose it.

MR. FISHMAN: Probably one of the takeaways from this is if you have to ask yourself whether it should be disclosed, it should be disclosed because if it's not obvious to you that it doesn't fit within the gamut of the word connection under rule 2014,¹⁹ then it arguably does and you're only jeopardizing yourself if you're not including it.

Now, in big cases and in big firms it's interesting to see what they do with this stuff sometimes. One of the things that I started to do, most recently today when an email went around our office that General Growth happened to file its bankruptcy today, which you may or may not know, in the Southern District of New York. Somebody called us to represent a client in that case and sent an email around and I disclosed in response to the email, which is part of how we do our connection and conflict search, that I'm a shareholder of General Growth Corporation. Too bad for me. I'm not sure that's a good thing to do to be a shareholder of a debtor.

14. 11 U.S.C. § 1103 (2008).

15. 11 U.S.C. § 1114 (2008).

16. 11 U.S.C. § 327 (2008).

17. Fed. R. Bankr. P. 3278.

18. Fed. R. Bankr. P. 2014.

19. Fed. R. Bankr. P. 2014.

In any event, it's a connection. We represent a client and I am a shareholder of the adverse party. I'm a shareholder of 100 shares or something so who cares, but that starts to highlight the kinds of things that may constitute connections that I think don't ever even remotely rise to the level of a conflict of interest. But depending on how you read that rule and what depth you think it requires you to go, you may have to disclose connections.

MR. TOWBIN: By the way, in cases where there's publicly held debtors and counsel for the debtor in possession and members of the firm own stock, I have seen orders where the stock has been required to be sold even though it's a minimal amount of stock. Nevertheless, you know the court in those cases feels there's an apparent conflict. I mean, to me requiring that and letting some other stuff go is hard to reconcile, but nevertheless, courts have different views of different types of connections and what's required to cure them.

Another interesting issue is if you are not disinterested, can you cure it? We have seen more and more cases where conflict counsel is being retained by Chapter 11 debtors and Chapter 11 committees. What you're saying when you file a motion to retain conflict counsel is I'm not disinterested. I don't qualify under 327²⁰ and here's how I'm going to solve that problem. The statute doesn't say you have to be disinterested, but if you're not, you can get a fix. It says you have to be disinterested.

But when you have a case like *Enron*²¹ or *United*²² or you have a case of that scope — and wait till you see General Motors if it files and the conflicts there — what do you do as a practical matter. What can a judge really do in a situation where a debtor has invested hundreds of thousands or millions of dollars in professional fees in a firm, they need that firm to represent them and they're presented with a potential conflict.

JUDGE SQUIRES: It happened to me in the *Clark Retail*²³ case. My solution to that problem because I knew exactly what Steve's point was, I ordered a Chinese Wall to be erected. There was an objection by the UST and I think maybe one other creditor about complicated connections that could pose a potential conflict. But case law out there that allowed this to be done and I thought that was the appropriate way to exercise what equitable discretion I had. I required

20. 11 U.S.C. § 327 (2008).

21. *In re Enron Corp.*, 279 B.R. 695 (Bankr S.D.N.Y.2002).

22. *In re United Airlines*, 438 F.3d 720 (7th Cir. 2006).

23. *Clark Retail Group, Inc. v. Clark Retail Enter., Inc.* (*In re Clark Retail Enter., Inc.*), 308 B.R. 869 (Bankr.N.D.Ill.2004).

in that case that the individuals who were in the firms for the debtor in possession who had done work for whatever this entity was, be screened off from all communication, all correspondence, all emails, et cetera, et cetera. I even required one of the firm members, the eminent and now, I guess retired, scholar, George Treastor, to act as the firm ombudsman and file periodic records with the court on whether the Chinese Wall had been maintained in order to avoid the appearance of impropriety.

Everybody seemed happy with that, or relatively happy and no appeal was filed. The case was, as those cases go I guess, relatively successful. But it would have been a huge mess on the front end of a major mega case to have that firm out of L.A. disqualified for considering how much money had been invested in getting the case to court and ready to hopefully get on track.

MR. FISHMAN: Let's focus on — we talked about the kind of disclosures that might need to be made in regard to connections. Dan, let's turn to you. You can use Perkins Coie as a starting example. Go wherever your thoughts take you. Judge, I would particularly like to have you share with us what you've seen from other firms — you don't have to name firms, but other examples of methodologies. How do you go about figuring out what connections a firm has to who, what method do you use, what communications do you make and where do you draw the line is worth mentioning.

MR. ZAZOVE: Bob's raising some very good questions and it certainly has to vary on a case-by-case basis. In the first instance, I guess you really want to know whether or not your potential client is publicly held or privately held. If it's publicly held, hell will be rained on your partners because you'll have to ask every one of them whether or not they're stockholders. We also send this around to every single employee of the firm and require them to disclose if they have any share holdings in the prospective client and of course, it has to be done on a very confidential basis as well because you don't want any information that the potential client may file to leak.

Beyond that, we maintain an incredibly large database of all of our present and former clients; even those who are no longer our clients and have not been. But even then how far back do you go? We go back and look at something from the last five years and see if we haven't represented somebody during that time. We generally disclose it, but it will be at the option of the person who is preparing the affidavit.

MR. TOWBIN: I have a question. Does your firm have a policy about sending out termination of engagements when you're done with

an engagement? How do you know when an engagement is over? Do they stop paying the bill?

MR. ZAZOVE: That's one way certainly. But you're right, Steve. Sometimes you do send a letter out terminating the engagement while sometimes you just close the file because you realize the matter in which you were working on has been concluded with no formal termination. You might terminate the matter, but then the question is have you terminated the client relationship which is another issue entirely. You have to look at both of those things.

MR. TOWBIN: I have seen clients say, "Well, you didn't represent me in the last year, but we are a client of the firm." I've also seen financial institutions do this to lawyers and disqualify them on that basis because they don't want to see them represent the debtor in the case.

MR. ZAZOVE: One of the things that we do is we're pretty careful about our engagement letters, which is not always possible to do, but certainly for one-shot type relationships or engagements, we're pretty careful. Say we're being engaged in this specific matter and this doesn't extend to any other matter unless both of us agree that we shall represent you in these other matters. It doesn't extend to your affiliates or your parents or subsidiaries or your officers and directors you know, without some specific agreement in writing that it shall.

So you know, I cannot tell you, Steve, that there aren't situations where someone wants to file a case, you run a conflicts check and it comes back revealing somebody's got a matter that hasn't been active for five years or more. You call that lawyer and say, "Why is this case still open?" "Why is this client still open?" Sometimes it's because the lawyer who was involved doesn't want to close the relationship and is trying to hang onto something even though there may not be a relationship there anymore.

MR. TOWBIN: Is it your practice to file a copy of your retention letter with your application?

MR. ZAZOVE: It depends on the circumstances. There are two circumstances where I do file: one, is if there is any kind of a waived conflict of some kind where you may have represented a party who may be adverse, not in connection with this case but with something else. But that's because the represented party thinks the court has to judge the type of waiver that you're getting and so you do file a copy of the retention letter with the application.

MR. TOWBIN: So in other words, if you get a retention that says you can go ahead perhaps from a financial institution that says you can go ahead and represent this debtor and negotiate the debtor in

possession financing arrangement. You will never take an adverse action against the bank or sue the bank in any way because that's something that's disclosed or should it be disclosed?

MR. ZAZOVE: It definitely has to be. I don't think there's any question. We get prospective waivers from most of our clients and what our standard engagement letter says is, "Look, I cannot tell you what will happen in the future. It may be that during the time that we're representing you, we might represent someone who has an adversity to you but not in connection with anything we're representing you on." The clients agree to us asking them to agree up front that as long as there is not an actual conflict, we can continue to represent the adverse party in matters unrelated to you and will ask the same of that party as well.

If it turns out that there is such an adversity, I will generally disclose it in the engagement letter and file and attach a copy of the letter to my application.

The circumstance that you're talking about is a bit more tricky. That's where representing an institutional lender, maybe not in connection with this case but someone in one of your other offices, and you may have to get a specific conflict waiver from that institution. In that case, you not only have to file a copy of your engagement letter, but you better file a copy of your conflict waiver with it as well.

AUDIENCE: I just want to go back to the point you made earlier about opening discrete matters. I've seen a lot of large law firms pro forma open a general matter for almost every client and then open specific matters. It would seem that if you do any billing under a general matter, then you really have to research what work you were doing specifically and that could be quite a broad variety of work.

MR. ZAZOVE: Sure. What we tend to do is open one matter for that client. It starts with matter one, and then if somebody calls and says, during the time you're representing them, I have a question that I wanted to ask you and you want to bill the client for that time, you might get it in a general category even though you have fifteen or twenty, we represent, we do a lot of work for Weyerhaeuser Realty. We have forty-seven matters open for them, but I'll tell you half the time they call me and say, "I just have a general question and I want you to bill me for it." Okay.

MR. FISHMAN: Let me add something to that because I think I have certainly seen in the last couple of years in conjunction with our applications to renew malpractice insurance that malpractice insurers are getting a lot savvier on account of all of the conflict problems that they are finding landing in their lap. For instance, our malpractice

insurer has given us discounts for our agreement to use an engagement letter for every matter for every client. Our malpractice insurer also gave us a discount for agreeing to use termination letters to terminate engagements. We also, like Dan, have I think a very sophisticated engagement letter that delineates who we're representing, who we're not representing, and what the matter is, what the matter isn't, and it talks about what we can do with files after a certain period of time.

There's a lot of loose ends and I think actually the malpractice carriers are assisting law firms in developing systems that are helpful to meet the requirements. In our particular case we've actually gotten discounts on our insurance because we've agreed to adhere to a more difficult set of rules than we used to follow say four or five years ago.

MR. ZAZOVE: I was going to ask Judge Squires what his view is of how many creditors you have to search. Certainly I think there's a consensus amongst most people that you really have to search the 20 largest creditors. But some law firms literally search every single creditor in a case and that could be very burdensome.

JUDGE SQUIRES: Unfortunately, Rule 2014(a)²⁴ doesn't limit it to 20; it just says creditors. So, it's problematic and I hasten to remind you the last sentence of Rule 2014(a)²⁵ requires it to be a verified statement. Steve & Barry is a citation to *United States v. Gellene*²⁶ with which I hope you all become familiar with. The case has been described as the perfect storm for inadvertent perhaps, but materially omitted 2014(a)²⁷ disclosures that went as far as you can go. It didn't result in just loss of fees, but also in criminal prosecution up in Milwaukee.

MR. FISHMAN: Jail time.

JUDGE SQUIRES: The whole nine yards. So it's serious. There's a book out that I would highly recommend everybody read, which has a real catchy title that caught my interest. It's called *Eat What You Kill*.²⁸ The author's surname escapes me, but it's now out in paperback. It was published in 2004 at the University of Michigan and it is a very detailed story of the Bucyrus-Erie bankruptcy up in Milwaukee that gave rise to Mr. Gellene's criminal prosecution after he'd done a very credible job of representing the debtor and debtor in possession.

24. Fed. R. Bankr. P. 2014(a).

25. Fed. R. Bankr. P. 2014(a).

26. *United States v. Gellene*, 182 F.3d 578 (7th Cir.1999).

27. Fed. R. Bankr. P. 2014(a).

28. MILTON C. REGAN, JR. *EAT WHAT YOU KILL*, (U. Mich. Press 2004).

After I read the book, I called my friend and now retired colleague, Russ Eisenberg, who was the bankruptcy judge who heard the Bucyrus-Erie bankruptcy, recommended the book to him and asked him to read it and tell me what he thought. He called me back about six weeks later and said the book was substantially very accurate about what went occurred.

So, it's a fascinating case study of how something can really go wrong if you're not careful in your 2014²⁹ disclosures and update them as soon as you learn of some new information that was out there that isn't in it. It's also got a very nice historical background on how the profession ended up with the prevailing fee structure in most bankruptcy cases and big time litigation which is a rather interesting historical context. It's something every young lawyer ought to read to realize how serious this can be. The consequences can be utterly devastating if you don't do the right thing at the right time and are found to have willfully and fraudulently concealed something that should have should have been disclosed.

MR. TOWBIN: Judge Squires raised an important issue of, given the preference of claim trading that we have today, and people coming in and out of cases, it seems the rules don't require updated disclosures to be filed, but as a practical matter we all do it. Is there a particular time that you do a search? Let's say you file a case on January 1st. Is it every quarter? Is it every six weeks? Is it never? Is it once a year?

MR. ZAZOVE: You're raising a really good question and I think people look at it from two aspects. One aspect is if another lawyer joins your law firm, especially our law firm, they go through a very, very rigorous conflict disclosure process. If we find there is any potential conflict, not only is the screen set up at the time, but our 2014³⁰ statement on file is immediately amended

But that's not really addressing the situation when you live in the claims trading world. Not only do we live in a claims trading world, but it's so sophisticated now that creditors holding large claims will often split up the distribution rights, hold the claim in their name and the actual parties in interest, maybe four or five other people, and assign those rights out. So, when one distribution is made that creditor might keep a piece for itself and then divide up the rest; really kind of like a hedging strategy. We do some work for hedge funds and that's exactly some of the strategies that they engage in.

29. Fed. R. Bankr. P. 2014.

30. Fed. R. Bankr. P. 2014.

So, when we talk about the utility or the advisability of searching every creditor, every creditor today may not be every creditor tomorrow. Sometimes I don't know if, Steve, you read the *Daily Bankruptcy Review* which shows the claims traded. That's sometimes how I learn if I've got a conflict or not.

MR. TOWBIN: Is it a practice? Do you have something in your computer that says time to do another conflict search every thirty or sixty days?

MR. ZAZOVE: Certainly with respect to anybody joining the firm, but not with respect to the claims. We haven't done that because the trading is so volatile. It's so difficult. If we know of a situation, of course we'll disclose it, but I don't know if there's a practice on a periodic basis to do it.

MR. TOWBIN: Might be something to think about.

MR. ZAZOVE: It is. I just don't know how you monitor it and provide some sort of a consistent result.

MR. FISHMAN: Judge Squires, do you see regular periodic 2014³¹ updated statements or do you mostly see ones that arise on account of some identifiable act which causes, perhaps something large happens and they're aware that they have to add a disclosure? Do you feel like you get regular, routine updated ones from counsel?

JUDGE SQUIRES: In some cases I do. In most cases I don't. It's usually in the bigger, more complicated cases where we've got experienced, sophisticated counsel who take this stuff seriously, that we'll see the 2014³² amended statements or supplemental statements or whatever. So I know there are people out there that take this seriously.

The operative word on disclosure is also voluntary disclosure. If something pops up that you learn about, it's much better that the disclosure come from you, the party that has to make the disclosure, rather than in somebody's motion to vacate the order of retention or motion to vacate the order on fees because we've just learned that this professional person has this perceived conflict and they knew about it and never made a timely disclosure. That was part of Mr. Gellene's problem.

MR. FISHMAN: This task of keeping your disclosures updated is a very complicated task. I know we represent a lot of debtors and I have personally stumbled on this rule a few years back when we filed a case for a debtor that was related in an ownership sense, but not in a

31. Fed. R. Bankr. P. 2014.

32. Fed. R. Bankr. P. 2014.

bankruptcy rule sense, to another entity. We filed the case while the second case was in front of a different judge. We made all the disclosures in the second case about the first case, but we forgot to go back and file an amended disclosure in the first case about the second case. Then somebody who was trying to create some strategic advantage in the first case became aware of the failure to file the amended disclosure and filed a motion with bad intentions in the first case; alleging that we were engaged in inappropriate conduct. While fortunately, we made an amended disclosure and the court was satisfied, it reminded me just how extensive and complicated this notion of the evolution of relationships in an existing case can become.

MR. ZAZOVE: We haven't even discussed the real difficult situation and that is for committee counsel. In my opinion, that is the most difficult circumstance to stay ahead of because there's so much — you know, maybe not quite as much now, but the economy had so much money in it and so many claims were being traded on such a regular basis. It was very, very, very difficult to keep up with just the volume of daily claims traded and make disclosures.

In fact, I think prudent committee counsel now indicates in their application they will make periodic searches, but will only do so either if something comes to their attention or once an order usually to indicate has been filed. But, it's acute for many counsel and I don't know what they can do other than try to stay on top of it and know as much as they can. In fact, it's so difficult that sometimes in cases, wasn't it the *Schwinn*³³ case where the entire committee turned over?

MR. TOWBIN: Oh, yeah. Well, that's not the first case. Talking about committee members it's interesting because there's no rules that say what disclosures committee members have to make. I don't know if any of you saw this article in the Wall Street Journal last week, by a professor at the University of Texas, I think named Wu. But, it was very interesting in that it explained really what the danger is of conflicts, of committee members sitting on committees who have credit insurance or are parties to the credit default swaps where they're hoping the debtor goes down as opposed to sitting there saying we want to help this reorganization along. You never know if the person sitting next to you, even though they're theoretically a trade creditor, do they hold insurance or do they hold a credit default swap where they can get paid off in full if that debtor terminates its case or converts to a Chapter 7.

33. *Schwinn Cycling and Fitness, Inc. v. Benonis (In re Schwinn Bicycle Co.)*, 210 B.R. 747 (Bankr.N.D.Ill.1997).

There's been issues raised more and more about disclosures that committee members have to make and I don't think the U.S. Trustee yet in going through the appointment process in Chapter 11 cases has really decided what to do or if they're going to do anything at all about it.

But we just filed a case the beginning of April. We had the committee formation meeting a couple days ago and there were some very serious conflicts and I think the U.S. Trustee's office, at least in this jurisdiction, relies heavily on debtor's counsel to bring to their attention what the debtor's counsel perceives might be a conflict, or a reason why a committee member should not be seated, or a potential committee member that should not be seated.

But that is kind of dangerous too because they should be getting their information from somebody other than the debtor's counsel. I think there's only going to be a matter of time before people that sit on committees are going to have to start making full disclosures which may dissuade people from being committee members. However, I think in the spirit of transparency, committee members and frankly, debtor's counsel, should have that information available.

MR. FISHMAN: Well, we're going to run out of time if we don't keep moving down the outline. Steve made passing reference earlier in the presentation to conflicts counsel and curing conflicts versus if you're not disinterested, and how exactly do you get around that. In our preparatory meeting we talked a little bit about the use of section 327(e)³⁴ counsel.

So will somebody lay out how this issue arises and then, Judge, I want to be sure to get your take on which of these kinds of problems are problems that could be cured and which of these kinds of problems are simply reasons why we have to get another counsel to represent the particular party. I'd rather have you guys lay it out and then have the judge comment.

MR. ZAZOVE: It is rather common in larger cases where generally one large law firm is representing a debtor that will create for that law firm multiple conflicts. They'll represent a number of creditors and not necessarily in unrelated matters and the debtor does not want to lose the benefit of having their principal counsel; either bankruptcy counsel or their general corporate counsel.

MR. FISHMAN: Don't you really mean the counsel doesn't want to lose the benefit of the representation? Isn't that really what drives this more than the client?

34. 11 U.S.C. § 327(e) (2008).

MR. ZAZOVE: Then the handcuffs. So the question is, how are these businesses reconcilable in a bankruptcy case? There are two potential ways that large law firms have dealt with this. One is the application and retention of what they call conflicts counsel. It's very common in New York, as one particular lawyer has made a terrific living being conflicts counsel in major cases and does an excellent job. His name is Al Togut, and he's not in a large firm, but I would say most of the large bankruptcy cases in New York, Togut, Segal & Segal gets retained as conflicts counsel.

Now, they're also conflicts counsel for the case, it's not just for the debtor. Sometimes they'll handle conflicts for committee counsel if there's an equity committee or even counsel for the secured creditors may have a conflict at various times. So they are called upon to represent one side or another in multiple situations.

It is now common in cases that are large enough, we were just talking about this in the context of General Motors, for each of the constituents to have conflicts counsel. The debtor will have conflicts counsel, the committee will have conflicts counsel because of certain confidential things that may go on in the committee where one party on the committee wants to trade in securities of the debtor, and then each of the major groups will have a conflicts counsel.

The other alternative, which some people like and I find to be attractive, is representation of special counsel under 327(e).³⁵ One of the best cases I ever saw this done was a case before Judge Squires called *National Steel*.³⁶ Skadden, Arps had been representing that company for a long time. They also represented its parent and almost everybody. Skadden, Arps had irreconcilable conflicts and perhaps could not have represented the debtor, even with conflicts counsel.

So what they did was farm out everyone but the debtor and then they retained DLA Piper as general bankruptcy counsel and Skadden, Arps was retained as special counsel under 327(e)³⁷ to the debtor. What did you think of it?

JUDGE SQUIRES: It worked. The other point if you look at Section 101(14)(c)³⁸ is the other prong on retention. Which is, not representing an interest adverse to the interest of the estate, any class of creditors or equity security holders by reason of any direct or indirect relationship to, in connection with, or interest in the debtor or for any other reason. Well, that can cover anything under the sun. We've

35. 11 U.S.C. § 327(e) (2008).

36. *In re National Steel Corp.*, 351 B.R. 906 (N.D.Ill.2006).

37. 11 U.S.C. § 327(e) (2008).

38. 11 U.S.C. § 101(14)(c) (2008).

only been talking about the disinterested part, but don't forget this other one.

If you take the statute literally, it doesn't work at all because the estate is, as Dan pointed out, nothing but a receptacle for the time span of the case to hold property of the estate with which to pay claims including professional fees and professional persons retained. A lot of the case law talks about how they can't be representing an interest that has got some sort of economic adversity. Well, every professional wants to get paid out of the estate. So if you're the estate, you're sitting there as a pot of money potentially and Dan is special counsel or whatever, he wants to get paid out of the estate. It doesn't get much more adverse from the estate's perspective than somebody that wants to take a part of it out to be paid for his or her fees.

So if you literally apply plain meaning of that section, it doesn't work for anybody. Fortunately, the case law has been a lot more generous than that and it's again a very ad hoc, fact-based analysis dealing with the facts and relationships of the particular case at bar in front of you.

MR. TOWBIN: This raises a disclosure issue because when you do an application and you have been retained by the debtor pre-petition, it's important and absolutely necessary to tell the court and the parties how much you've been paid and when you got paid. If you take a look at the *Pillowtex*³⁹ decision in the Third Circuit, you've got a situation where an accounting firm was disqualified and lost a great deal of money because they were preference recipients. Believe me, it's very rare that accounting firms or other professional firms put forth in their affidavits they are potential preference recipients. It's just something that people normally don't point out.

But if you don't point it out, you're going to be held hostage to people in the case because they're going to say, when your fees come up, this is what's going to happen. So you want to rethink your position on this issue or that issue. It's a dangerous thing for the estate or a committee to have a professional that is held hostage to somebody who is going to object to the professional's fees based upon a failure to disclose. So it's not just a problem for the professional. It's a problem for the whole case and the bankruptcy system. That's why these disclosures are just absolutely so important so people aren't put in that position of being threatened with the loss of their fees because of failure to properly disclose.

39. In re *Pillowtex, Inc.*, 349 F.3d 711 (3rd Cir. 2003).

MR. ZAZOVE: If you take away one thing from this lecture and speech, it is you should never be the one who decides whether or not you have a conflict. Your obligation as a professional is to make the disclosures and let someone else make that determination. The better your disclosures, the safer you are in the long run. In my experience, I've never seen any circumstance where the proper disclosures were made that someone, even if they came in later and objected, that a court would cognize that objection. You're either going to do it at the beginning of the case or you're not. You cannot lie in the weeds and attempt to exert undue influence later.

You can represent that you have no conflict, but it's not your decision to make. Your obligation as a professional is to make every possible disclosure that you can and let someone else check. Doing that at the beginning of the case is far better than the consequences of omitting something and having to deal with it later.

MR. FISHMAN: Let's talk about that exact scenario because I think that's a very good point that you made. A particular law firm seeking to be retained under section 327(a), to be general bankruptcy counsel to a particular bankruptcy estate, files its retention motion and its 2014 affidavit. In that affidavit it discloses as a connection a relationship with a creditor that constitutes an actual conflict of interest in the case. There's a companion motion filed by the debtor seeking to retain a second law firm to represent the estate with respect to the matter implicated by that actual conflict of interest.

In practice, it appears in many courts the first lawyer will be allowed to be retained under 327(a),⁴⁰ and the second lawyer will be retained as conflicts counsel to handle the matter which constitutes the conflict. My question is, under the rule how does retaining somebody as conflicts counsel cure the fact that you are not disinterested and that you represent an interest adverse to the estate? How do you make that go away, thereby allowing yourself to be retained under 327(a)⁴¹ simply by retaining conflicts counsel?

MR. ZAZOVE: You're the guy that said that your obligation is to disclose and let the court decide whether or not an actual conflict exists or not.

MR. FISHMAN: Maybe I'm asking the court.

JUDGE SQUIRES: I disclaim all advisory opinions sought.

MR. FISHMAN: Look, I've heard you do this before. Pretend like you're a judge.

40. 11 U.S.C. § 327(a) (2008).

41. 11 U.S.C. § 327(a) (2008).

MR. TOWBIN: Why don't we ask the real judge?

JUDGE SQUIRES: It's all fact specific. I can't prejudge any of this stuff until I know what all the facts and circumstances are. But if a professional person is not both statutorily disinterested and not representing an interest adverse to the estate, they're not supposed to be retained.

MR. FISHMAN: How does conflict counsel ever cure that problem? The only reason you would ask for conflicts counsel is if the existence of a set of facts creates a problem which you believe gets in the way of you being retained in the absence of conflict counsel.

MR. ZAZOVE: Bob, I'm not sure. Let me give you a little better answer. There are different types of conflicts. I might represent a debtor and ultimately find that someone buys a claim in the case, who winds up being a client of mine at a subsequent point in time. I can tell you from firsthand experience this has happened and it's the client's purchase of that claim that can create a conflict during that time frame. In that circumstance, whether or not special counsel can handle any controversy with that creditor will resolve that situation.

MR. FISHMAN: You would be then talking about something that would be a potential for a conflict because unless and until a controversy arises between the debtor and that new holder of the claim, there is no actual conflict that exists.

MR. ZAZOVE: Let me create a couple hypotheticals for the other members of the panel. Steve brought up a good situation where a particular law firm might represent a bank or another lending institution. The matter would be completely unrelated. They have a banking relationship. They have no conflict waiver because it's very hard to get prospective waivers. You have to go and request an individual waiver from that client.

Let's assume that that client constitutes five percent or more of the revenues for that law firm; which does happen on occasion as well. Do you have, in that case a reconcilable conflict, a disqualifying conflict?

MR. TOWBIN: It depends on the judge. There's a judge in the Northern District that said that five percent of your business is going to disqualify you.

MR. FISHMAN: Aren't we mixing words again? We've got all these words that often get interchangeably used, but they're not the same words. We have connection, conflict, disinterested, and holds an adverse interest. Those things are not interchangeable.

MR. TOWBIN: Holds or represents an adverse interest.

MR. FISHMAN: That's correct. I wrote it down. So the question is, the statute says you must be disinterested and whether you avoid under applicable state ethics rules a conflict may satisfy that rule, but what does it do to address the disinterestedness test which isn't completely the equivalent of a conflict?

MR. ZAZOVE: Hypothetically, let's assume that you've represented that lending institution in an unrelated matter once. Does that mean that you are interested or disinterested? Should that disqualify you from representing a debtor who has an adversity with that lending institution?

MR. FISHMAN: I get to ask the question. You have to answer.

MR. ZAZOVE: I was hoping if I asked that one you would answer.

JUDGE SQUIRES: Isn't that basically 327(c)? That provides that in a case under Chapter 7, 12, or 11, a person is not disqualified from employment under this section solely because of such person's employment by or representation of a creditor, unless there is an objection by another creditor for the United States Trustee. In which case, the court shall disapprove such employment if there is an actual conflict of interest.

Again actual conflict of interest is not a defined term so a lot of this stuff just goes under my judicial radar because it may be out there as long as it's disclosed. If nobody is going to object, being another creditor or the UST, I'm not going to make issue of it *sua sponte*. I don't know what the hell is going on until parties tell me.

MR. TOWBIN: That 327(c)⁴² has also been used where the same attorney wants to represent multiple debtors that file jointly administered cases. Often today you'll see Chapter 11 being filed by a corporate group of entities where you've got ten or fifteen different entities and there's inter-company guarantees or inter-company claims. Obviously it's not going to be financially feasible to hire twelve different lawyers for the twelve different companies. You're not going to have twelve different committees, although interestingly, the bankruptcy code says there shall be a committee in each case. But nobody really takes that very seriously.

MR. FISHMAN: That's case with a small C.

MR. TOWBIN: But the point is that 327,⁴³ I think, has been appropriately used for getting around the fact where you've got multiple debtors represented by the same lawyer, even though there might be inter-company claims, that's not going to disqualify you. For the most

42. 11 U.S.C. § 327(c) (2008).

43. 11 U.S.C. § 327 (2008).

part, those inter-company claims are not disputed and generally in a plan they're going to be resolved in one form or another anyway.

I think courts sensibly use 327(c)⁴⁴ in those situations and I don't think I've seen in the 35 years I've practiced, a law firm get objected to representing multiple debtors because of inter-company claims who are not disinterested.

AUDIENCE: You posed the question about conflicts counsel and so now I'm a little confused. My understanding of conflicts counsel was that an attorney could come in and independently research to determine if, in fact, there was an actual conflict and report to the court; not a curative.

MR. FISHMAN: I think the term is ordinarily used not — I mean that's sort of like the court's expert concept. I think that in general practice conflicts counsel is, for instance, if I represent a debtor and one of the debtor's principal unsecured creditors is a large client of my firm who I don't represent with respect to anything related to the debtor. That creditor who is a client of my firm, who I could not commence a lawsuit against. Now let's suppose that that client received a preference in that bankruptcy case. The notion of conflicts counsel would be I would retain Dan to bring the preference action against my client in the bankruptcy case on behalf of the bankruptcy estate and I would have no involvement at all in the dispute between the estate and my client on that preference matter. That's the context in which conflicts counsel is being used.

JUDGE SQUIRES: That's really 327(e)⁴⁵ so don't call it that, just call it counsel for a specified purpose.

AUDIENCE: If there had been a special conflict at the inception of the engagement and someone objected, you couldn't get past 327(c)⁴⁶ because someone would have objected.

MR. FISHMAN: I think that's probably right. If my debtor client and my other client were actually engaged in a real dispute at that time and worse yet, if I had some involvement with that dispute before I began representing the debtor, I don't believe disclosure, conflicts counsel, 327(c) or (e)⁴⁷ will get me past the fact that I can't represent that debtor as 327(a) counsel.

MR. ZAZOVE: But you will generally see the retention of conflicts counsel occur at the same time that the case is filed with the first day motions even though that might have to wait the 20 days as well.

44. 11 U.S.C. § 327(c) (2008).

45. 11 U.S.C. § 327(e) (2008).

46. 11 U.S.C. § 327(c) (2008).

47. 11 U.S.C. § 327(c), (e) (2008).

But it is generally thought that conflicts counsel is selected very early on and identified because that conflicts counsel has to do his or her own conflicts check as well.

MR. FISHMAN: You need conflicts counsel for conflicts counsel.

MR. TOWBIN: By the way, there's a limitation on 327(e),⁴⁸ which a lot of courts ignore, of conflicts counsel or 327(e)⁴⁹ special counsel must have represented the debtor pre-petition. How many times have you seen a motion by counsel for the debtor, by the debtor in possession, we're going to hire committee counsel to do some conflict work in the case. Well, they didn't represent the debtor pre-petition and under 327(e).⁵⁰ There's a split of authority. It's in the materials. We can see the split of authority, but some courts take that very seriously. As 327(e)⁵¹ was intended, if you had somebody, a non-bankruptcy lawyer, handling matters for you pre-petition who you want to continue to retain post-petition and you don't want to make him waive his claim so he's not a creditor.

MR. ZAZOVE: What's the difference between 327(e)⁵² and what is called ordinary course professionals?

MR. TOWBIN: 327(e)⁵³ requires disclosure and that you can't have an adverse interest in the estate. But 327(b),⁵⁴ ordinary course counsel, is where you have in-house counsel at the time the case is filed or in-house attorneys, accountants or other kind of professionals. You do not need to go to court to get them retained. The debtor in possession, without regards to the disclosure requirements, can continue to retain and more importantly compensate those people in the ordinary course of business.

JUDGE SQUIRES: But they have to be employees as stated in 327(b).⁵⁵

MR. ZAZOVE: In the *National Steel*⁵⁶ case I believe there was an order, or motion presented to authorize the debtor to retain outside professionals as ordinary course as long as they were not involved. I know we see it all the time.

48. 11 U.S.C. § 327(e) (2008).

49. *Id.*

50. *Id.*

51. *Id.*

52. *Id.*

53. *Id.*

54. 11 U.S.C. § 327(b) (2008).

55. *Id.*

56. *In re National Steel Corp.*, 351 B.R. 906.

JUDGE SQUIRES: Right. The way to deal with that is if they've got this title problem, as in *Clark Retail*,⁵⁷ where you have real estate in multiple states all over the country, and the client wants to use local counsel to close a real estate deal. I think the order provided you didn't have to go through the separate application process. However, before they can do any work they've got to make a 2014⁵⁸ disclosure of record and then let the chips fall where they may.

MR. FISHMAN: On that note, we have to bring to conclusion our presentation because we have overstayed our welcome. So thank you everybody very much.

57. *In re Clark Retail Enter., Inc.*, 308 B.R. 869.

58. Fed. R. Bankr. P. 2014.

