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## USING GENERAL COUNSEL TO SET THE TONE FOR WORK IN LARGE CHAPTER 11 CASES

Nancy B. Rapoport\*

Culture eats strategy for lunch.<sup>1</sup>

In a recent article,<sup>2</sup> I suggested that general counsel should take a more active role in managing the costs of large Chapter 11 cases. Given the way that court-appointed professionals get paid in Chapter 11—either as a priority administrative expense<sup>3</sup> or from a carve-out of a secured creditor's collateral<sup>4</sup>—there's a deep disconnect between the professionals who are doing the work in Chapter 11 cases and those who are watching the costs of that work add up.<sup>5</sup> The bankruptcy court reviews the fees and expenses for reasonableness,<sup>6</sup> and it can appoint a fee examiner or fee committee to assist

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\* Garman Turner Gordon Professor of Law, William S. Boyd School of Law. This Article was prepared for the *Colloquium on Corporate Lawyers*, hosted by the *Fordham Law Review* and the Stein Center for Law and Ethics on October 11, 2019, at Fordham University School of Law. Special thanks go to Youngwoo Ban, Randy Gordon, Dwayne Hermes, McKay Holley, Morris Rapoport, Bill Rochelle, Joe Tiano, and Jeff Van Niel, and to all of the participants in the Colloquium, all of whom gave me extraordinarily helpful comments.

1. No one actually knows who first used this phrase, but many people attribute it to Peter Drucker, even though none of his books seem to use it. *See, e.g.*, Shep Hyken, *Drucker Said 'Culture Eats Strategy for Breakfast' and Enterprise Rent-A-Car Proves It*, FORBES (Dec. 5, 2015, 9:02 AM), <https://www.forbes.com/sites/shephyken/2015/12/05/drucker-said-culture-eats-strategy-for-breakfast-and-enterprise-rent-a-car-proves-it/> [https://perma.cc/7S9X-H9EN] (“‘Culture eats strategy for breakfast,’ is a famous quotation attributed to the late business management guru Peter Drucker.”); *cf.* Laura Weiss, *Uber's New In-House Lawyers Emphasize Importance of 'Culture,'* CQ ROLL CALL (Cong. Quarterly Inc., Washington, D.C.), Mar. 8, 2019 (discussing Uber's culture in light of several scandals).

2. Nancy B. Rapoport, *Client-Focused Management of Expectations for Legal Fees in Large Chapter 11 Cases*, 28 AM. BANKR. INST. L. REV. 39 (2020).

3. *See* 11 U.S.C. §§ 330(a)(1), 507(a)(2) (2018).

4. *See, e.g.*, *E. Coast Miner LLC v. Nixon Peabody LLP (In re Licking River Mining, LLC)*, 911 F.3d 806, 812 (6th Cir. 2018) (discussing carve-outs).

5. *See, e.g.*, Cynthia A. Baker, *Other People's Money: The Problem of Professional Fees in Bankruptcy*, 38 ARIZ. L. REV. 35, 37 (1996); Matthew Adam Bruckner, *Crowdsourcing (Bankruptcy) Fee Control*, 46 SETON HALL L. REV. 361, 381–83 (2016); Nancy B. Rapoport, *Rethinking Professional Fees in Chapter 11 Bankruptcy Cases*, 5 J. BUS. & TECH. L. 263, 263–65 (2010); Robert K. Rasmussen & Randall S. Thomas, *Timing Matters: Promoting Forum Shopping by Insolvent Corporations*, 94 NW. U. L. REV. 1357, 1369 (2000); Clifford J. White III & Walter W. Theus, Jr., *Professional Fees Under the Bankruptcy Code: Where Have We Been, and Where Are We Going?*, AM. BANKR. INST. J., Dec. 2010, at 78, 78.

6. 11 U.S.C. § 330(a)(1) provides:

in that review. Absent objections from parties in interest,<sup>7</sup> from the United States trustee, or from a fee examiner, though, the busy docket of a bankruptcy court (and the sheer size of some of these fee applications) makes meaningful, line-by-line review of fee applications a daunting prospect.<sup>8</sup> And without such review, professional fees in large Chapter 11 cases can run into the hundreds of millions of dollars in the blink of an eye.<sup>9</sup>

Here's an example. In the Pacific Gas and Electric Company (PG&E) bankruptcy, the United States trustee raised a litany of problematic entries after reviewing the first round of fee applications:

- Internal meetings and conference calls that were billed by as many as 22 attorneys from the same firm, with no explanation or justification—including several firm-wide “case update” meetings

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After notice to the parties in interest and the United States Trustee and a hearing, and subject to sections 326, 328, and 329, the court may award to . . . a professional person employed under section 327 or 1103—

(A) reasonable compensation for actual, necessary services rendered by the trustee, examiner, ombudsman, professional person, or attorney and by any paraprofessional person employed by any such person; and

(B) reimbursement for actual, necessary expenses.

11 U.S.C. § 330(a)(1) (2018). The bankruptcy court can also award less than the fees and expenses requested. *See id.* § 330(a)(2). Sections 330(a)(3) and 330(a)(4) provide a list of factors for the court to consider. *See id.* § 330(a)(3)–(4).

7. Parties in interest rarely object to professionals' fees. As my friend Joe Tiano notes, “[f]irms know what needs to be done and what has been done and can evaluate outcome vs. work input. The ‘what comes around goes around’ disinclination to turn a blind eye to objectionable fees really leaves the [United States] Trustees Office and Fee Examiners in a[n] isolated, second class position.” Email from Joseph Tiano, Founder & Chief Exec. Officer, Legal Decoder, Inc., to Nancy Rapoport, Garman Turner Gordon Professor of Law, William S. Boyd Sch. of Law (Aug. 21, 2019, 9:14 AM) (on file with author) [hereinafter Tiano Email]. Joe goes on to make a good suggestion: if firms could reach the fee examiner confidentially to report on what they considered to be waste or inefficiency, that information would be useful in formulating follow-up questions to fee reviews. *See id.*

8. *See, e.g.,* Bruckner, *supra* note 5, at 372–73 (“In a large corporate bankruptcy case, a bankruptcy court typically receives fee applications from twelve to sixteen professional firms every three months, and fee applications are usually thirty or more pages. Assuming there are twelve professional firms each filing a thirty-page application every three months for two years, Fee Controllers [defined as bankruptcy judges and assistant United States trustees] must closely scrutinize 2880 pages of ‘single-spaced, small font lines of time entries and expense details’ over the course of the case. Add only four more professional firms, and Fee Controllers will have to scrutinize 3840 pages (and hundreds of thousands of lines of time and expense entries) instead.”). Of course, using good legal analytics data, the reviews are becoming less daunting. *See* Tiano Email, *supra* note 7.

9. *See, e.g.,* Mark Chediak, *PG&E Spent \$127 Million in Bankruptcy Costs, Fees in Two Months*, BLOOMBERG (May 2, 2019, 8:56 AM), <https://www.bloomberg.com/news/articles/2019-05-02/pg-e-spent-127-million-on-bankruptcy-costs-fees-in-two-months> [https://perma.cc/5NP4-A8LL] (“[PG&E] expects Chapter 11 costs for this year to range from \$360 million to \$430 million, according to a slide presentation posted online Thursday. The costs for the first quarter included \$114 million in financing and \$24 million in ‘legal and other costs,’ offset by \$11 million in interest income.”); *see also* Tom Corrigan, Joel Eastwood & Jennifer S. Forsyth, *The Power Players That Dominate Chapter 11 Bankruptcy*, WALL ST. J. (May 24, 2019), <https://www.wsj.com/graphics/bankruptcy-power-players/> [https://perma.cc/WER9-BL5N] (“In the case of Lehman Brothers, the largest and most expensive chapter 11 in history, bankruptcy professionals took home more than \$2.5 billion.”).

attended (and billed) by attorneys with minimal other involvement in the case;

- Numerous instances of large numbers of attorneys billing for attending or observing the same hearing, again without any explanation or justification for the attendance of so many timekeepers;
- Implausibly high numbers of billable hours recorded by individual timekeepers in a single day, including at least one instance in which a timekeeper billed for 24 hours in one day . . . ;
- Expenses that have been charged to the estate despite the fact that they were incurred before the bankruptcy cases were filed or otherwise predate the firm's employment;
- Non-travel working meals and overtime meals that have been charged to the estate, despite that such expenses are also non-reimbursable under the Local Guidelines;
- In a number of instances, "overtime" meals and transportation expenses that have been charged to the estate on days when the charging timekeeper did little or no work on PG&E matters . . . .<sup>10</sup>

To state the obvious, funds spent on professionals can move a case forward, leading to a successful reorganization,<sup>11</sup> but the dollars spent on professionals are also dollars not provided pro rata to general unsecured creditors<sup>12</sup> or kept in the coffers of the secured creditor whose collateral may be paying for those fees and expenses. There must be some way to provide real-time (or near real-time) oversight to professionals making decisions about which tasks to do, who should perform those tasks, and how long those tasks can take.<sup>13</sup> This Essay refers to that combination as the "staffing/budget

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10. United States Trustee's Response to Motion to Approve Fee Procedures & Comments Regarding First Interim Fee Applications at 4-5, *In re PG&E Corp.*, No. 19-30888 (DM) (Bankr. N.D. Cal. Sept. 27, 2019), ECF No. 4025. As the United States trustee's response explained, "[o]n the basis of these issues alone, there are at least \$4 million in improper, excessive, or otherwise objectionable fees and expenses in the Interim Applications, representing approximately 6% of all fees and expenses that have been sought." *Id.* at 5. Some of the professionals involved would disagree with the issues that the United States trustee was raising, but it is clear why the United States trustee (and the fee examiner in the case) read the PG&E fee applications so closely: line-by-line monitoring was necessary to catch any potential billing errors and lapses in billing judgment.

11. Or a successful sale outside the ordinary course of business per 11 U.S.C. § 363.

12. See Stephen J. Lubben, *What We "Know" About Chapter 11 Cost Is Wrong*, 17 *FORDHAM J. CORP. & FIN. L.* 141, 144 (2012) ("Being in chapter 11 means that creditors' recovery on their claims becomes higher than zero. The professional fees are the cost of moving to that higher recovery. The notion that money paid to professionals belongs to creditors is true only if the creditors could realize that value without the professionals.").

13. In fact, one of the potential solutions discussed during the Colloquium involved real-time (daily) monitoring of fees, perhaps by the court, the fee examiner, and the United States trustee (and perhaps only those three, given the professionals' fear of revealing strategy through their time entries). Discussion with Miriam H. Baer, Professor of Law, Brooklyn Law Sch., at the Fordham Law Review and the Stein Center for Law and Ethics Colloquium: Colloquium on Corporate Lawyers (Oct. 11, 2019).

decision.” The general counsel (or her delegate) might be just the person to take on that job.

This Essay suggests that one way for the general counsel to help bankruptcy professionals make better staffing and budget decisions is to communicate her values more clearly to those professionals at the beginning of the engagement.<sup>14</sup> In her role as the chief legal officer, the general counsel needs to let the bankruptcy professionals in on her thought processes. How does she watch over her own attorneys’ decisions in other types of cases? What expenses does she consider reasonable? If she takes an active role in monitoring her bankruptcy professionals’ work, her values (assuming that they’re good values) will contribute to the oversight necessary to keep the fees and expenses reasonable.

#### I. CULTURE IS EVERYTHING, BUT THE TRICK LIES IN FIGURING OUT WHAT THE CULTURE REALLY IS

One can hardly pick up a newspaper these days without reading about the culture of some business enterprise.

—Greg Urban<sup>15</sup>

Culture can be good or bad. It can also be a mix, with pockets of positive culture and pockets of Hobbesian<sup>16</sup> misery. In businesses, the culture can encourage profligate behavior, where limousines and four-course catered dinners are the norm, or it can encourage miserly behavior (think bus fare and deli sandwiches).<sup>17</sup> Enron was a prime example of how a bad culture generated bad decisions. Countless books and articles have attempted to dissect all of the bad decisions that led to Enron’s downfall,<sup>18</sup> and I think that

14. There are three groups of general counsel who could take an active role in a large Chapter 11 cases: the general counsel for the debtor, the general counsel for any of the unsecured creditors appointed to the creditors’ committee (because the creditors’ committee will have its own set of professionals), and the general counsel for any major secured creditor. For a primer on how professionals get paid in Chapter 11 cases, see, for example, Rapoport, *supra* note 2, at 40–42 and Nancy B. Rapoport, *The Case for Value Billing in Chapter 11*, 7 J. BUS. & TECH. L. 117, 121–26 (2012).

15. Greg Urban, *Corporate Compliance as a Problem of Cultural Motion: Extension of Remarks to the Symposium on New Directions in Corporate Compliance*, 69 RUTGERS U. L. REV. 495, 496 (2017). For more on corporate scandals, see generally NANCY B. RAPOPORT & JEFFREY D. VAN NIEL, *CORPORATE SCANDALS AND THEIR IMPLICATIONS* (3d ed. 2018).

16. THOMAS HOBBS, *LEVIATHAN* 186 (C. B. Macpherson ed., Penguin Books 1968) (1651) (describing the state of nature in the war of human against human as “nasty, brutish, and short”).

17. One might think that well-off companies have more of a tendency to splurge and companies teetering on the edge of bankruptcy would be more thrifty, but I haven’t found that strong a correlation between resources and behavior.

18. See, e.g., BETHANY MCLEAN & PETER ELKIND, *THE SMARTEST GUYS IN THE ROOM: THE AMAZING RISE AND SCANDALOUS FALL OF ENRON* (2003); MIMI SWARTZ & SHERRON WATKINS, *POWER FAILURE: THE INSIDE STORY OF THE COLLAPSE OF ENRON* (2003); Lynne L. Dallas, *Enron and Ethical Corporate Climates*, in *ENRON AND OTHER CORPORATE FIASCOS: THE CORPORATE SCANDAL READER* 151 (Nancy B. Rapoport, Jeffrey D. Van Niel & Bala G. Dharan eds., 2d ed. 2009); Marleen A. O’Connor, *The Enron Board: The Perils of Groupthink*, 71 U. CIN. L. REV. 1233 (2003); Anita Raghavan et al., *How Enron Bosses*

many of them can be boiled down to one thing: people will adjust their behavior to that which gets rewarded. When Enron was a normal natural gas company, it made mostly intelligent decisions.<sup>19</sup> When it decided that it wanted to be the “world’s leading company,” it made bad ones, starting with a reward system that valued estimated profits over real ones and that valued cronyism over talent.<sup>20</sup> Enron got exactly that behavior that it incentivized and praised, and the behavior was often venal. When the Enron executives spent lavishly, that observable behavior encouraged Enron’s rank and file to do the same: “[e]very year, young [Enron] executives received big bonuses and more stock options. And every year, the number of new Porsches and BMWs in the Enron garage multiplied.”<sup>21</sup> Enron tolerated temper tantrums,<sup>22</sup> rather than punishing them. What people see their leaders do, they will do too.

My point isn’t to rehash Enron, especially because there is a never-ending supply of post-Enron corporate scandals (and we don’t seem to learn much from any of them, unfortunately). My point is that, if the general counsel wants to encourage behavior from her outside law firms that comports with her own values, she needs to be clear on what her values are at the outset of the engagement, and she needs to monitor compliance with those values during the entire engagement. Her words will matter. If she wants to put the brakes on overspending by professionals who are representing the client in a

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*Created a Culture of Pushing Limits*, WALL ST. J. (Aug. 26, 2002, 11:58 AM), <http://www.wsj.com/articles/SB1030320285540885115> [<https://perma.cc/YRR5-URCN>].

19. We can ignore the Valhalla brouhaha, although it was a precursor to the later, larger Enron scandals. For a quick primer on Valhalla, which involved two Enron traders exposing Enron to \$90 million of risk and keeping two sets of books, see Carrie Johnson, *Prosecutors Link Enron Fall to 1987 Scandal*, WASH. POST (Nov. 5, 2005), <https://www.washingtonpost.com/archive/politics/2005/11/05/prosecutors-link-enron-fall-to-1987-scandal/1cc9a9d0-0a88-43f9-8d11-16972f2e9a87/> [<https://perma.cc/7EFS-RVL2>].

20. Robert Prentice, *Enron: A Brief Behavioral Autopsy*, 40 AM. BUS. L.J. 417, 428 (2003) (“When Enron employees valued proposed deals, which affected the numbers Enron could put on its books, which in turn determined whether or not employees met their bonus targets, which in turn determined whether millions of dollars in bonuses were paid to the very people who were deciding what the numbers should be, even assuming good faith (and at least some of the Enron officers must have been acting in good faith), the self-serving bias must have had an impact.”). For just a partial listing of my (and my husband’s) fixation on Enron’s missteps, see, for example, ENRON AND OTHER CORPORATE FIASCOS, *supra* note 18. See also NANCY B. RAPOPORT & BALA G. DHARAN, ENRON: CORPORATE FIASCOS AND THEIR IMPLICATIONS (2004); RAPOPORT & VAN NIEL, *supra* note 15; Nancy B. Rapoport, *Enron and the New Disinterestedness—the Foxes Are Guarding the Henhouse*, 13 AM. BANKR. INST. L. REV. 521 (2005); Nancy B. Rapoport, *Enron*, Titanic, and The Perfect Storm, 71 FORDHAM L. REV. 1373 (2003). It’s safe to say that we are Enron-obsessed people, even after all this time; Nancy B. Rapoport, *Lessons from Enron—and Why We Don’t Learn from Them*, COM. LENDING REV., May–June 2009, at 21; Nancy B. Rapoport, *Managing U.S. News & World Report—the Enron Way*, 48 GONZ. L. REV. 423 (2013).

21. FRANK PARTNOY, INFECTIOUS GREED: HOW DECEIT AND RISK CORRUPTED THE FINANCIAL MARKETS 306 (2003).

22. See Greg Hassell, *The Fall of Enron/the Culture/Pressure Cooker Finally Exploded*, HOUS. CHRON., Dec. 9, 2001, at A1 (“I remember one [Enron] trader going crazy because his bonus was only \$500,000. He was cursing and screaming and throwing things at his desk,’ one former Enron employee recalls. ‘He thought because he was so brilliant, they should be paying him a lot more.’”).

large Chapter 11 bankruptcy, in addition to creating a basic understanding of the representation's parameters,<sup>23</sup> she should spend some time talking about what she considers reasonable, what she considers questionable, and what she considers out-of-bounds. By giving specific examples of how she handles certain situations inside her own company, she can convey that culture to her outside law firms. Tone at the top is important in creating and sustaining any organization's culture, because

messages from executive leadership, organizational structure, selection systems, orientation and training programs, rules and policies, formal reward and performance appraisal systems, and decision-making processes all contribute to ethical culture creation and maintenance. . . . Informally, the culture's norms of daily behavior, heroes, rituals, stories, and language keep the ethical culture alive and indicate to both insiders and outsiders whether the formal systems are actually implemented or are merely a façade.<sup>24</sup>

It's often not the case that the client pushes back in terms of fees and expenses in bankruptcy,<sup>25</sup> but I think that the general counsel is in a good position to try. After all, every general counsel chooses her outside law firms, and every general counsel is in a position to recommend law firms to colleagues (or to warn colleagues away). That's a natural leverage point for anyone with hiring power, and the partners with whom she deals likely already think of her as a peer. In addition, some of the fundamental tasks in any Chapter 11 case are those with which most lawyers are familiar: basic litigation, such as preference actions or fraudulent transfer lawsuits; document production; and the ongoing "ordinary course" work that would occur whether or not a company is in Chapter 11. Moreover, every general counsel is familiar with the concept of deciding staffing/budget questions: how many people, and at which level of experience, should perform certain tasks. Whether or not the general counsel stays with the organization after the bankruptcy is over, she can still take her evaluation of each professional's performance with her and use it to make future hiring decisions and to help other general counsel make their hiring decisions. It is in her best interest to develop opinions of how well her organization was served by each professional in the bankruptcy case.<sup>26</sup>

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23. See, e.g., Rapoport, *supra* note 2, at 72–84.

24. Linda Klebe Treviño, *Out of Touch: The CEO's Role in Corporate Misbehavior*, 70 BROOK. L. REV. 1195, 1202 (2015).

25. See *supra* note 5 and accompanying text (discussing the disconnect in Chapter 11 between who's doing the work and who's paying for the work).

26. As Bruce Green pointed out in his notes to me on an earlier draft, the general counsel will be influenced by the board of directors, as well as her fellow C-suite executives. See Email from Bruce Green, Louis Stein Chair of Law, Fordham Univ. Sch. of Law, to Nancy Rapoport, Garman Turner Gordon Professor of Law, William S. Boyd Sch. of Law (Aug. 20, 2019, 11:38 AM) (on file with author). She is not calling the bankruptcy shots on her own. It would be wonderful if the board of directors and the other executives paid attention to the burn rate of professional fees in large Chapter 11 cases, but it's just not my experience that they do so—at least not in terms of anything that gets filed in the case.

So why don't most general counsel push back on bankruptcy fees, given that they aren't shy about pushing back on fees in other areas of the law?<sup>27</sup> Simply put, bankruptcy may not be in a general counsel's experiential wheelhouse.<sup>28</sup> Bankruptcy is typically a bet-the-company event, not an ordinary course event.<sup>29</sup> Even though, by now, there are enough data points about fees in large Chapter 11 cases to be able to benchmark certain recurring events, benchmarking may not be at the top of the general counsel's priority list. Even the most diligent general counsel may need to partner with a bankruptcy fee expert to understand the burn rate of the professional fees in the case. That said, having a general counsel monitor the burn rate is likely the best way to keep bankruptcy costs down.

## II. IF THE GENERAL COUNSEL CAN ENUNCIATE HER VALUES, IT WILL BE EASIER FOR HER OUTSIDE LAW FIRMS TO CONFORM TO THOSE VALUES

Not only will people inside the general counsel's organization—her own cadre of lawyers—take their cues from her behavior but so will the outside law firms that she hires. If she brings her lunch from home or orders a sandwich rather than a plate of expensive sushi, her colleagues will probably think twice about ordering in their own expensive lunches. If she sends emails at 4 a.m.,<sup>30</sup> her colleagues will become (or pretend to become) early risers.

Here's a good example of how a general counsel's values affected her outside law firms: when Shell's general counsel, Cathy Lamboley, started drilling down into which of her outside law firms had a diverse mix of talent (and which ones actually used that talent), she used metrics to winnow out those firms for whom diversity was merely window dressing.<sup>31</sup> Humans are value-maximizing creatures, and they will tend to gravitate toward behavior that gets rewarded. If a company's general counsel were to use data

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27. See, e.g., Sara Randazzo, *Corporate Clients Push Back After Law Firms Hike Starting Salaries*, WALL ST. J. (June 15, 2016), <https://www.wsj.com/articles/companies-push-back-at-law-firms-starting-salary-hikes-1466029554> [<https://perma.cc/48YU-RGLT>]. There may be all sorts of specialty areas in the law that are outside a general counsel's wheelhouse, and so my suggestions might well apply to other types of practice areas. But, much like the old saying, "if you have a hammer, everything looks like a nail," I can only speak from my own wheelhouse.

28. See Rapoport, *supra* note 2, at 43, 61.

29. On the other hand, there are some companies that have made that bet more than once, necessitating a repeat filing. See, e.g., Daniel Gill, *Retailers Repeat Bankruptcies Show Plans Falling Short*, BLOOMBERG L. (Feb. 14, 2019, 2:35 PM), <https://news.bloomberglaw.com/bankruptcy-law/retailers-repeat-bankruptcies-show-plans-falling-short> [<https://perma.cc/W9W5-F6US>]; Katie Intner, *Charming Charlie Plans to Close 260 Stores After Filing for Bankruptcy Again*, PEOPLE (July 12, 2019, 12:44 PM), <https://people.com/style/charming-charlie-files-for-bankruptcy> [<https://perma.cc/M9VV-W3TV>].

30. Not a good idea, and I try not to do that anymore. There's a reason that most email programs allow someone to schedule the transmission of an email at a more reasonable time.

31. Terry Carter, *Coming Out of Her Shell*, A.B.A. J. (Dec. 3, 2004, 7:35 AM), [http://www.abajournal.com/magazine/article/coming\\_out\\_of\\_her\\_shell](http://www.abajournal.com/magazine/article/coming_out_of_her_shell) [<https://perma.cc/KY9C-YXLM>].



analytics<sup>32</sup> to determine how her law firms staff their cases,<sup>33</sup> how careful they are about curtailing unnecessary expenses,<sup>34</sup> and how well tailored their work product is to the company's legal needs,<sup>35</sup> she could do the same type of winnowing out of firms whose values don't match her own and could reward (by retaining and by referring) those firms whose values did match hers. She could also shape behavior in those law firms by telling the engagement partners how, for example, she handles meals and travel at her own company. We know that social pressure has significant effects on people's behavior—when someone sees how the rest of the group behaves, that person is more likely to conform to that behavior<sup>36</sup>—so the general

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32. See, e.g., Nancy B. Rapoport & Joseph R. Tiano, Jr., *Legal Analytics, Social Science, and Legal Fees: Reimagining "Legal Spend" Decisions in an Evolving Industry*, 35 GA. ST. U. L. REV. 1269, 1291 (2019).

33. *Id.* at 1273–77.

34. *Id.*

35. See, e.g., Dwayne J. Hermes, Erica R. LaVarnway & Nancy B. Rapoport, *A Solutions-Oriented Approach: Changing How Insurance Litigation Is Handled by Defense Law Firms*, 2017 J. PROF. LAW. 129.

36. See, e.g., Randy D. Gordon & Nancy B. Rapoport, *Virtuous Billing*, 15 NEV. L.J. 698, 725–26 (2015) (“The effect of social pressure (how other billers behave in the same firm) can counteract any official training program over time. Not only is it important that the people at the top of the pecking order set the right tone, but it is equally important that a biller's peers behave appropriately. Solomon Asch's work teaches us that having as few as one or two people in a group diverge can cause others to go astray, even when they ‘know better.’” (footnotes omitted)); see also Larry Richard, *Ethics Corner: What Can Social Science Tell Us About Ethics?*, A.B.A. (Mar. 20, 2016), [https://www.americanbar.org/groups/business\\_law/publications/blt/2016/03/ethics\\_corner/](https://www.americanbar.org/groups/business_law/publications/blt/2016/03/ethics_corner/) [<https://perma.cc/UP3W-2NZ8>] (“One of the well-established principles of social psychology is that most people respond to ‘social proof’ (also known as the bandwagon effect or peer pressure)—that is, they look around them to see what others are doing in a particular situation, and are often unconsciously guided by the flow of the crowd. The more people that are behaving in a particular way, the more likely it is that any given individual will go along and behave in the same way. People are even more likely to rely on social proof when (a) the situation contains some ambiguity about what the right way to behave is; and (b) when the individual perceives the crowd as similar to him/herself in some way.”). In essence, we can use social pressure to mold more ethical behavior. Social consensus is defined by Thomas M. Jones as “the degree of social agreement that a proposed act is evil (or good).” Thomas M. Jones, *Ethical Decision Making by Individuals in Organizations: An Issue-Contingent Model*, 16 ACAD. MGMT. REV. 366, 375 (1991). Kenneth D. Butterfield states that it is “the individual's perception of social consensus within the individual's relevant social sphere that is most important to determining whether an individual will recognize a moral issue.” Kenneth D. Butterfield et al., *Moral Awareness in Business Organization: Influences of Issue-Related and Social Context Factors*, 53 HUM. REL. 981, 990 (2000). His empirical study confirms that

moral awareness is more likely to be triggered when an individual perceives a social consensus within the organization/profession that the activity in question is ethically problematic. Thus, although previous normative and descriptive writings have tended to suggest that the ethical decision-making is an individual or personal process, this research suggests that, in organizational contexts, it is very much a social process. If a decision-maker perceives that others in the social environment will see an issue as ethically problematic, she or he will be more likely to consider the ethical issues involved.

*Id.* at 1001; see also Lynne L. Dallas, *A Preliminary Inquiry into the Responsibility of Corporations and Their Officers and Directors for Corporate Climate: The Psychology of Enron's Demise*, 35 RUTGERS L.J. 1, 10–11 (2003) (discussing Butterfield's study). Of course, not everyone will succumb to conformity pressure. That is the fun of social science research.

counsel should be able to use social pressure to her advantage in terms of conforming outside law firm behavior to her values.<sup>37</sup>

General counsel have some natural allies in terms of enforcing the values of efficiency in large Chapter 11 cases. Fee examiners and the Office of the United States Trustee both provide assistance to bankruptcy courts in terms of reviewing the fee applications in Chapter 11 cases. A few courts have even adopted guidelines that spell out what is and isn't presumptively reasonable in terms of fees and expenses. Some examples include the prohibition of block-billing time entries<sup>38</sup> and the requirement that firms must justify the use of multiple professionals<sup>39</sup> and the necessity for intrafirm conferences.<sup>40</sup> These guidelines also forbid reimbursement of overhead or secretarial work,<sup>41</sup> set tight restrictions on working meals,<sup>42</sup> and ban reimbursement for alcohol, in-room entertainment, and the like.<sup>43</sup> Not all courts have adopted such guidelines or adopted the United States Trustee

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37. The biggest issue will be the tendency of lawyers representing fiduciaries not to leave any stone unturned. *See, e.g.*, Rapoport, *supra* note 2, at 55; Rapoport & Tiano, *supra* note 32, at 1275–77; *see also supra* note 5 and accompanying text (explaining the budget/payment disconnect in Chapter 11 cases).

38. *See, e.g.*, BANKR. N.D. TEX. R. app. F; *Guidelines for Compensation and Expense Reimbursement of Professional and Trustees*, U.S. BANKR. CT. N. DISTRICT CAL. (Feb. 19, 2014), <http://www.canb.uscourts.gov/procedure/guidelines-compensation-and-expense-reimbursement-professional-and-trustees> [<https://perma.cc/Y6ZT-VFCY>].

39. BANKR. N.D. TEX. R. app. F (“Multiple Professionals. Professionals should be prepared to explain the need for more than one professional or paraprofessional from the same firm at the same court hearing, deposition, or meeting. Failure to justify this time may result in compensation for only the person with the lowest billing rate. The Court acknowledges, however, that in complex Chapter 11 cases the need for multiple professionals’ involvement will be more common and that in hearings involving multiple or complex issues a law firm may justifiably be required to utilize multiple attorneys as the circumstances of the case require.”); *see also Guidelines for Compensation and Expense Reimbursement of Professional and Trustees, supra* note 38 (“Conferences—Professionals should be prepared to explain time spent in conferences with other professionals or paraprofessionals in the same firm. Failure to justify this time may result in disallowance of all fees related to such conferences.”); *cf. Guidelines for Compensation and Expense Reimbursement of Professional and Trustees, supra* note 38 (“Multiple Professionals—Professionals should be prepared to explain the need for more than one professional or para-professional from the same firm at the same court hearing, deposition or meeting. Failure to justify this time may result in compensation for only the person with the lowest billing rate.”).

40. BANKR. N.D. TEX. R. app. F, pt. II.E; *Guidelines for Compensation and Expense Reimbursement of Professional and Trustees, supra* note 38.

41. BANKR. N.D. TEX. R. app. F, pts. II.D–L.

42. *Id.* app. F, pt. II.T (“Meals (Working). Working meals at restaurants or private clubs are not reimbursable. Reasonable reimbursement may be sought for working meals only where food is catered to the professional’s office in the course of a meeting with clients, such as a Creditors’ Committee, for the purpose of allowing the meeting to continue through a normal meal period.”); *see also Guidelines for Compensation and Expense Reimbursement of Professional and Trustees, supra* note 38 (outlining similar restrictions on working meals and on meals while traveling).

43. BANKR. N.D. TEX. R. app. F, pts. II.S–T (outlining restrictions on working meals and on meals while traveling); *see also Guidelines for Compensation and Expense Reimbursement of Professional and Trustees, supra* note 38 (same). I’d be remiss if I didn’t point out that the genesis of some of these guidelines probably comes from prior abuse by a few professionals.

Program's guidelines for large Chapter 11 cases,<sup>44</sup> but I'm willing to bet that most courts reviewing fee applications apply some standard principles to the reasonableness review that they must do pursuant to 11 U.S.C. § 330. I'm also willing to bet that most general counsel have some standard guidelines about the fees and expenses that they're reviewing from their outside law firms.<sup>45</sup> Having a values-based discussion before the representation begins, and reinforcing it when necessary during the representation, can help outside law firms understand the parameters of what the general counsel considers reasonable.<sup>46</sup>

Fees can get out of whack quickly when the general counsel hasn't had that discussion,<sup>47</sup> especially given the countervailing pressures on law firms to bill significant numbers of hours in order to make their own budgets balance.<sup>48</sup> Fees also can get out of whack when the outside law firm is touting its particular bankruptcy expertise to a general counsel who hasn't lived through a Chapter 11 case before and who will trust the law firm's advice about staffing and budgets. And because there are very few firms that get tapped repeatedly for the largest Chapter 11 cases,<sup>49</sup> one could draw the conclusion that the outside law firms are using their expertise to pull out all the stops in their representation, given that they are representing fiduciaries,<sup>50</sup> which leads to a concomitant increase in the costs of that representation.<sup>51</sup>

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44. Appendix B Guidelines for Reviewing Applications for Compensation and Reimbursement of Expenses Filed Under United States Code by Attorneys in Larger Chapter 11 Cases, 78 Fed. Reg. 36,248 (June 17, 2013).

45. Moreover, I'll bet that most general counsel are sensitive to the pigs/hogs distinction, much as the court was in *In re Energy Partners, Ltd.*, 409 B.R. 211 (Bankr. S.D. Tex. 2009). "At some point, this Court must draw the line between what is reasonable and what is not. To quote the Fifth Circuit: '[W]hen a pig becomes a hog it is slaughtered.'" *Id.* at 237 (quoting *Swift v. Bank of San Antonio (In re Swift)*, 3 F.3d 929, 930 (5th Cir. 1993)).

46. One idea, suggested by Joe Tiano, is that a bankruptcy court could require, in the affidavits accompanying employment applications, that the professionals have actually had the values-based discussions with their clients. See Tiano Email, *supra* note 7.

47. For a discussion of a recent objection to the first round of fee applications in a large bankruptcy case, see *supra* note 10 and accompanying text.

48. Discussion with David Yosifon, Professor of Law, Santa Clara Univ. Sch. of Law, at the Fordham Law Review and the Stein Center for Law and Ethics Colloquium: Colloquium on Corporate Lawyers (Oct. 11, 2019) (pointing out that law firms' pressure to generate a large number of billable hours likely also factors into the choices that professionals make in staffing large, bet-the-company matters, which then leads to higher fees).

49. See, e.g., Corrigan, Eastwood & Forsyth, *supra* note 9 ("The *Journal's* analysis found that in nearly two-thirds of the largest Chapter 11 cases of the past decade by assets, at least one of the top 10 power firms played a pivotal role representing either the debtor or the official creditors' committee."); see also Discussion with Sung Hui Kim, Professor of Law, Univ. of Cal. L.A. Sch. of Law, at the Fordham Law Review and the Stein Center for Law and Ethics Colloquium: Colloquium on Corporate Lawyers (Oct. 11, 2019) (highlighting the small number of power-player firms in large Chapter 11 cases).

50. See, e.g., Rapoport & Tiano, *supra* note 32, at 1275 (discussing the incentives for leaving no stone unturned); see also Nancy B. Rapoport, *The Client Who Did Too Much*, 47 AKRON L. REV. 121, 126 (2014) ("There are many ways in which a client's actions can increase her own lawyer's fees. She can—as some Chapter 11 clients with estate-paid professionals might want to do—urge her professionals to leave no stone unturned.").

51. See *supra* note 10 and accompanying text.

### III. A VALUES-BASED DISCUSSION BETWEEN THE GENERAL COUNSEL AND HER OUTSIDE LAW FIRMS CAN HELP LAW FIRMS AVOID MAKING BAD CHOICES

A big Chapter 11 case is intense, with long days and many moving parts. In the heat of deciding what to do, who should do particular work, and how long that work should take, the partners in charge of the engagement are probably not regularly checking the budgets that they send the client to confirm whether they're in compliance with the various budget subcategories.<sup>52</sup> I recognize the reality of large Chapter 11 cases, but I also believe that some of the inefficiencies that can ensue come from the speed of the decisions made in those cases.<sup>53</sup> Without some sort of touchstone—and the budget isn't a good touchstone, being honored more in the breach<sup>54</sup>—law firm decision makers can find themselves making short-term decisions that have bad long-term implications. After all, a bankruptcy court can't authorize the payment of unreasonable fees and expenses. Once any unreasonable time has been spent (or the fancy steak dinner has been billed), that is money that the law firm won't recover. Bad decisions are costly.

Moreover, bad decisions can cascade. For example, at the start of the engagement, having an all-hands-on-deck meeting is a useful, efficient way to decide who will take on which tasks. But as the case progresses, those all-hands meetings may not be particularly efficient. People will show up because they showed up last week, and the week before last, but without necessarily needing to be at each such meeting. Making a deliberate choice about whom to invite, though, takes time, and a time-pressured partner may have other things on her mind. Taking the time to decide who should be at a weekly half-hour meeting may result in significant cost savings, because those billable hours in ten- or twenty-person meetings will add up. Tailoring the meetings to only those who truly need to spend real-time face time together would reduce the inefficiencies and thus the fees. But the partner running those meetings might believe that her time is better spent focusing on other issues than on editing the attendee list.<sup>55</sup> On the other hand, if the

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52. It would be a lot better if they did. *See, e.g.*, Rapoport, *supra* note 2, at 81–83; *see also* Robert A. Prentice, *Behavioral Ethics: Can It Help Lawyers (and Others) Be Their Best Selves?*, 29 NOTRE DAME J.L. ETHICS & PUB. POL'Y 35, 74 (2015) (“People may wish to do the right thing, but when under time pressure they are more likely to act unethically.”); Jennifer K. Robbennolt, *Behavioral Ethics Meets Legal Ethics*, 11 ANN. REV. L. & SOC. SCI. 75, 79 (2015) (“It is not simply time pressures that can have negative consequences for ethics. Fatigue and cognitive load can also have similar detrimental effects.”).

53. Again, there are emergencies in all areas of the law—clients can face temporary restraining orders, year-end closings, and the like—and bankruptcy law doesn't have a monopoly on urgency. *But see* Randazzo, *supra* note 27. I can only speak from my own experience, and my experience lies in reviewing fees in large Chapter 11 cases.

54. *Cf.* WILLIAM SHAKESPEARE, *HAMLET* act 1, sc. 4 (“Ay, marry, is't:/ But to my mind, though I am native here/ And to the manner born, it is a custom/ More honour'd in the breach than the observance.”).

55. *See, e.g.*, Prentice, *supra* note 52, at 69 (“One of the major reasons why people make poor ethical choices and thereafter engage in unethical actions is their ability to rationalize.”); Robbennolt, *supra* note 52, at 77 (“[U]nethical decisions can result from too little thinking—when deliberation is needed but not engaged to override unethical intuitions. But unethical

general counsel decides to say, at the beginning of the engagement, that it matters to *her* how many people show up at these weekly meetings, though, then the partner might be willing to focus on that issue.<sup>56</sup>

But *will* the partner focus? Again, the disconnect between who does the work and who pays for it creates disincentives for values-based discussions. The problem is that the general counsel is also focusing on *her* internal priorities. If she's the general counsel for the debtor, she's working with outside counsel to try to keep the debtor afloat. If she's the general counsel for the secured creditor whose collateral is being used to pay professionals, perhaps she's watching the burn rate for the fees and expenses but, once that carve-out has been spent,<sup>57</sup> she has no more skin in the game, and the bankruptcy professionals must still do a competent<sup>58</sup> and diligent<sup>59</sup> job, even if they're no longer getting paid for their efforts. If she's the general counsel for one of the unsecured creditors on the creditors' committee, then she's just one voice out of several and might not focus on the costs of the representation. There are all sorts of reasons why no one has the values-based discussion.<sup>60</sup>

And yet, the general counsel has the tools to have that values-based discussion and to set the ground rules for the representation, possibly even including an alternative form of billing.<sup>61</sup> Omari Scott Simmons's paper for this Colloquium provides an important discussion of just what a chief legal officer can do to control the amounts spent on outside counsel:

In the legal services context, [chief legal officers] can disrupt service provider overreach and opportunism in several ways. As sophisticated purchasers within the corporation, they can help to mitigate information

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decisions can also result from too much thinking—when deliberation is employed to justify an intuitively attractive but unethical course of action.”).

56. In a way, the issue becomes whether to control the expenditure of time at the front end (the values-based, “integrity” approach, see, for example, Donald C. Langevoort, *Monitoring: The Behavioral Economics of Corporate Compliance with Law*, 2002 COLUM. BUS. L. REV. 71, 104 (“[I]ntegrity based systems . . . seek to persuade rather than command employees to act in a manner consistent with the firm’s best interests . . . .”)) or to reduce efficiencies post hoc (the monitoring approach, see, for example, Veronica Root, *The Monitor-“Client” Relationship*, 100 VA. L. REV. 523, 526 (2014) (“[A] monitor appears *after* the compliance failure has occurred to investigate the scope of an already identified compliance failure.”)). Discussion with Miriam H. Baer, *supra* note 13.

57. The carve-out, having already been budgeted, is a sunk cost.

58. See MODEL RULES OF PROF’L CONDUCT r. 1.1 (AM. BAR ASS’N 2018) (defining “competence”).

59. See *id.* r. 1.3 (defining “diligence”).

60. One additional reason, at least for unsecured creditors, could be that those creditors are far more concerned with their percentage recovery than they are with the burn rate of professional fees. Discussion with Omari Scott Simmons, Howard L. Oleck Professor of Bus. Law, Wake Forest Univ. Sch. of Law, at the Fordham Law Review and the Stein Center for Law and Ethics Colloquium: Colloquium on Corporate Lawyers (Oct. 11, 2019).

61. *Id.* 11 U.S.C. § 328 certainly contemplates the possibility of alternative billing structures. See 11 U.S.C. § 328(a) (2018) (“The trustee, or a committee appointed under section 1102 of this title, with the court’s approval, may employ or authorize the employment of a professional person under section 327 or 1103 of this title, as the case may be, on any reasonable terms and conditions of employment, including on a retainer, on an hourly basis, on a fixed or percentage fee basis, or on a contingent fee basis.”).

gaps associated with experience and credence services. Their embedded legal acumen enables them to help diagnose problems and, equipped with data-driven tools, they can collect and analyze reliable information about the proposed service, thereby creating more value for their companies. For example, a data analysis of contracts might reveal costly errors and gaps for which the service provider bears responsibility. Similarly, data analytics might reveal that a law firm's recommended litigation strategy has not generated desirable results commensurate with the costs. [Chief legal officers'] guidance is not simply *ex post*; they can provide valuable predictive guidance to assist *ex ante* decision-making.<sup>62</sup>

General counsel can provide useful input and, certainly, someone must. If the estate-paid professionals aren't regularly monitoring their own staffing and task decisions on the front end, then the aggregate amount of recommended reductions on the back end can reach into the hundreds of thousands (or even millions) of dollars. Moreover, if one considers that every action in a bankruptcy case spurs significant reactions by other parties in interest,<sup>63</sup> then finding ways to eliminate wasted effort inures not just to one professional's bottom line but to multiple professionals' bottom lines, as well as to the ultimate recovery by unsecured creditors.<sup>64</sup> There are no easy fixes for the "who does the work/who pays for it" conundrum in Chapter 11 cases, but having an involved general counsel is a good place to start.

#### IV. HAVING THE GENERAL COUNSEL COMMUNICATE HER VALUES IS NOT THE ONLY NECESSARY CHANGE

During the Colloquium, we brainstormed ideas that might help with initiating and implementing the necessary changes. Eli Wald suggested that having the general counsel—and not just the professional<sup>65</sup>—sign off on the fee applications, indicating that she has reviewed them and approved them (under penalty of perjury), might focus her attention on just what is getting

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62. Omari Scott Simmons, *Chief Legal Officer 5.0*, 88 FORDHAM L. REV. 1741, 1746 (2020) (footnotes omitted); *see also* Rapoport, *supra* note 2, at 72–91.

63. *See, e.g.*, Stephen J. Lubben, *The Chapter 11 Attorneys*, 86 AM. BANKR. L.J. 447, 471 (2012) ("The regression models in this paper show that the key factor in counsel costs is the size of the web of parties engaged in a Chapter 11 case. The debtor's lead bankruptcy counsel stands in the middle of this web, and the more parties they have to interact with the greater the amount the debtor will have to pay to attorneys."); Rapoport, *supra* note 2, at 54.

64. Or, indeed, the likelihood of an effective reorganization at all. It's possible to spend so much on the fees and expenses of professionals that a Chapter 11 case becomes administratively insolvent.

65. The United States Trustee Program's guidelines ask fee applicants to answer this question: "If the fees sought in this fee application as compared to the fees budgeted for the time period covered by this fee application are higher by 10% or more, did you discuss the reasons for the variation with the client?" Appendix B Guidelines for Reviewing Applications for Compensation and Reimbursement of Expenses Filed Under United States Code by Attorneys in Larger Chapter 11 Cases, 78 Fed. Reg. 36,248, 36,252 (June 17, 2013). Thus, there's some authority for asking the general counsel to affirm that, at least with respect to any budget-blowing fees, she has reviewed them.

billed to the estate.<sup>66</sup> She would first need to have access to a system that sorts the fees other than by a line-by-line, time-entry review, but there are plenty of fee examiners out there who could help her with that task. Miriam Baer suggested that a form of real-time review, possibly by only those who wouldn't use the information in the time sheets to counteract any signaled strategy moves,<sup>67</sup> could catch bad decisions much earlier in the process. Although a bankruptcy judge wouldn't have the bandwidth to review the fees and expenses each day (nor might the United States trustee), certainly a fee examiner could use the real-time review, coupled with trend analysis during the case, to catch potentially bad staffing or budget decisions before a fee application was filed.<sup>68</sup> And Nancy Moore suggested that we focus our attention on the general counsel with the most incentive to push back on questionable fees.<sup>69</sup> That could be the general counsel for the secured creditor whose collateral is paying for the fees, or it could be the general counsel for one of the unsecured creditors. With the right tools for data analysis in place, the right creditor might be incentivized to become more active in reviewing fees. One thing's for sure, though: the more we return to a values-based discussion, the more likely we are to affect overall behavior.

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66. Discussion with Eli Wald, Charles W. Delaney Jr. Professor of Law, Univ. of Denver Sturm Coll. of Law, at the Fordham Law Review and the Stein Center for Law and Ethics Colloquium: Colloquium on Corporate Lawyers (Oct. 11, 2019).

67. In other words, the bankruptcy judge, the United States trustee, and the fee examiner. Discussion with Miriam H. Baer, *supra* note 13.

68. Donald Langevoort also suggested that judges could more actively enunciate their values about billing up front. Discussion with Donald C. Langevoort, Thomas Aquinas Reynolds Professor of Law, Georgetown Univ. Law Ctr., at the Fordham Law Review and the Stein Center for Law and Ethics Colloquium: Colloquium on Corporate Lawyers (Oct. 11, 2019). And some have, either in their jurisdiction's local rules or in their own, case-specific rules. *See, e.g.*, Letter from A. Benjamin Goldgar, Judge, U.S. Bankr. Court N. Dist. of Ill., to Nancy Rapoport, Garman Turner Gordon Professor of Law, William S. Boyd Sch. of Law (June 23, 2015) (on file with author) ("I thought it might assist you in your work to let you know that in my long-held view, in-town travel expenses a person incurs because he has stayed at [sic] late at the office or come in early are never reimbursable.").

69. Discussion with Nancy J. Moore, Professor of Law, Bos. Univ. Sch. of Law, at the Fordham Law Review and the Stein Center for Law and Ethics Colloquium: Colloquium on Corporate Lawyers (Oct. 11, 2019).