

**American Bankruptcy Institute  
Winter Leadership Conference**

**Presentation of the  
Unsecured Trade Creditors' Committee**

**Scottsdale, Arizona  
Friday, December 1, 2006  
3:45 – 5:15 p.m.**

***Recent Developments Affecting Businesses and  
Chapter 11 Cases under the Bankruptcy Abuse  
Prevention and Consumer Protection Act:***

- *Creditors' Committees*

***Presenters:***

Honorable Joan N. Feeney  
Edward T. Gavin, CTP  
Judith Greenstone Miller  
Adrienne Murphy

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## *Biographies of Presenters*

*Honorable Joan N. Feeney  
Chief Judge  
United States Bankruptcy Judge  
for the District of Massachusetts*

HON. JOAN N. FEENEY has been a United States Bankruptcy Judge for the District of Massachusetts since 1992. She is currently the Chief Judge. She is also a member of the First Circuit Bankruptcy Appellate Panel. Judge Feeney is the First Circuit representative to the Bankruptcy Judges Advisory Group and a member of the Budget and Finance Advisory Council of the Administrative Office of the United States Courts, is a Fellow of the American College of Bankruptcy, is a member of the Board of Directors of the American Bankruptcy Institute, and was a member of the Board of Governors of the National Conference of Bankruptcy Judges from 2002 to 2005. Judge Feeney is co-chair of the Joint Bankruptcy Court/Boston Bar Association Task Force on Financial Literacy and is also Co-Chair of the Local Rules Committee for the District of Massachusetts. Judge Feeney is the co-author the West publication Bankruptcy Law Manual and Chapter 9 of the treatise Chapter 11 Theory and Practice. In 2005, Judge Feeney received the Boston Bar Association's Haskell Cohn Award for Distinguished Judicial Service. Prior to her appointment, Judge Feeney was an associate and partner of Hanify & King, P.C. She was Law Clerk to Hon. James N. Gabriel, U.S. Bankruptcy Judge for the District of Massachusetts. Judge Feeney is a graduate of Connecticut College and Suffolk University Law School. Judge Feeney is a frequent panelist and lecturer on bankruptcy law topics in Massachusetts and throughout the country.

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Ted Gavin is a Certified Turnaround Professional and Managing Director of NachmanHaysBrownstein's Wilmington, DE office. He has more than 10 years experience with distressed companies, including regulated and non-regulated manufacturing, distribution and service firms, where he has served leadership roles in restructuring, engineering, manufacturing, I.T. and regulatory affairs functions. Ted has extensive experience in strategic planning, process re-engineering and hands-on management of turnarounds in for-profit, non-profit and public sector operations.

Ted is co-leader of NHB's Creditors' Services Group and specializes in bankruptcy matters, having successfully served debtors, creditors and secured lenders in numerous cases. In working with debtors, he has performed turnarounds for manufacturing companies with multi-site US, Canadian, Mexican and Middle East enterprises across a variety of industries. Ted has also

provided expert witness testimony in support of collateral valuation disputes and in support of bankruptcy adversarial proceedings brought by creditors and debtors. Ted is a member of the Turnaround Management Association, the National Association of Credit Management, the Equipment Leasing Association and is an Associate Member of the Association of Certified Fraud Examiners. Ted is a Lifetime Member of the American Bankruptcy Institute and is an active supporter of the ABI Endowment Fund. He has written articles for The Journal of Corporate Renewal, Business Credit Magazine, Credit & Collections Risk and other publications and is authoring articles for the ABI Journal which will appear in late 2006.

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Judith Greenstone Miller's practice at Jaffe Raitt Heuer & Weiss, P.C. focuses upon bankruptcy and insolvency, creditors' rights and commercial litigation. Her practice has involved representation of debtors, secured and unsecured creditors, creditors' committees and trustees in bankruptcy proceedings, primarily involving Chapter 11 reorganizations. She also represents parties in litigation in complex commercial disputes. Ms. Miller is a frequent lecturer nationally and has authored numerous articles dealing with issues relating to bankruptcy practice and Revised Article 9 of the Uniform Commercial Code.

Ms. Miller is a member of the Commercial Law League of America and its Bankruptcy and Creditors' Rights Sections. She served on the Board of Governors (Bankruptcy Section Representative, 2003-2004); Legislative Committee (Co-Chair, 1998-2002), Education Committee (Co-Chair 1997-1998); Executive Council of the Bankruptcy Section (Chair, 2002; Chair Elect, 2001; Secretary, 2000); Co-Chair National Governmental Affairs Committee (2002-2005); Vice-Chair NCBJ Committee (2001-2005). Ms. Miller has testified before the Subcommittee on Commercial and Administrative Law on the Judiciary Committee of the United States House of Representatives and the Subcommittee on Administrative Oversight and the Courts on the Judiciary Committee of the United States Senate numerous times on proposed and recently enacted bankruptcy legislation. Ms. Miller is also a member of the American Bankruptcy Institute and served on its Advisory Board for the Central States Bankruptcy Workshop from 1998 through 2003. She also serves as the Chair of the Creditors' Committee Task Force of the ABI's Unsecured Trade Creditors Committee.

Ms. Miller is a member of the American Bar Association (Business Law Section; Business Bankruptcy Committee; Chair, Litigation Subcommittee of the Business Bankruptcy Committee (2002-2005); Co-Chair, Bankruptcy Appeals Subcommittee of the Business Bankruptcy Committee (2005-2006); Chair, Task Force on Attorney Discipline of ABA Ad Hoc Committee on Bankruptcy Court Structure and Insolvency Processes); Federal Bar Association

for the Eastern District of Michigan; Detroit Metropolitan Bar Association (Chair, Debtor/Creditor Section, 1997-2002: Chairperson of the Year, 1998); and the State Bar of Michigan (Co-Chair, Debtors/Creditors Rights Committee of the Business Law Section; Member of the Business Council; and Member of the Debtor/Creditor Committee of the Real Property Law Section). She is also a member of the Bankruptcy Court Advisory Committee and the Mediation Panel for the Eastern District of Michigan, Southern Division; the Chapter 11 Rules Committee; and the Bankruptcy Judges Tribute Committee. The Michigan Consumer Bankruptcy Association honored her in December 2000 as a local practitioner that is a nationally recognized bankruptcy leader.

*Adrienne Murphy, CCE*  
*Sundberg Furniture Manufacturing Co.*  
*Los Angeles, California*

Adrienne Murphy, CCE has been in the Credit field for over 25 years. She was recently elected to the National Association of Credit Managers board of directors and serves as advisor to CMA Business Credit Services board of directors. She served as Chairman of the Board from 2004-2005 for CMA Business Credit service and has held every office since she was elected in 1996 as a director.

She has been a National Committee Member on the NACM Professional Designation Work Group for several years. She also is a member of American Bankruptcy Institute, Credit Research Foundation, Credit & Financial Development Division (CFDD), and Furniture Manufacturers Credit Association and serves on several committees.

Adrienne has been with Sandberg Furniture for 12 years and 28 years in the Furniture Industry. She currently is Director of Customer Financial Services.

In July of 1999 she earned her CCE designation and in 2002 she received her Certified Expert Witness certificate. She has given presentations at the local, regional and national level on credit management, customer service, and bankruptcy issues.

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***Recent Developments Affecting Businesses and  
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- *Creditors' Committees*

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<sup>1</sup> This article was previously presented as part of a larger program and in a different format at the Annual Meeting of the America Bar Association in August 2006. This portion of the article has been revised to address additional developments that have occurred since it was first published.

## Creditors' Committees

### **A. Section 1102(b)(3)**

The Bankruptcy Abuse Prevention Consumer Protection Act (“BAPCPA”) imposes, among other things, new duties and responsibilities on creditors’ committees. Section 1102(b)(3) mandates “information sharing” and “solicitation of creditors,” as follows:

- (a) A committee appointed under subsection (a) shall -
  - (A) provide access to information for creditors who –
    - (i) hold claims of the kind represented by that committee, and
    - (ii) are not appointed by the committee;
  - (B) solicit and receive comments from creditors described in paragraph (A); and
  - (C) be subject to a court order that compels any additional report or disclosure to be made to the creditors described in subparagraph (A).

### **B. Legislative History**

There is a paucity of legislative history surrounding §1102(b)(3). This “information sharing” provision was first introduced during the 106<sup>th</sup> Congress by Representative Nydia Velazquez of New York, as House Amendment 57 to the then pending bankruptcy legislation. Rep. Velazquez expressed that the intent in introducing the legislation was to protect ‘small business creditors’ that do not have access to the same information as provided to large creditors involved in a case. The absence of such information precludes such small business creditors from being able to accurately access and make business decisions affected by the outcome of the bankruptcy case. When introducing the amendment, Rep Velaquez stated:

Mr. Chairman, while H.R. 833 provides a plan for overhauling our Nation's bankruptcy law, there is one issue that, while seemingly small, will have a great impact on this Nation's small businesses. That is the way that the bankruptcy process leaves small businesses who are creditors on the outside looking in to solve this problem, I am offering an amendment that will quickly and fairly address the issue by ensuring more small business involvement and greater communications in the bankruptcy process. My amendment will make two simple changes:

First, it would allow a small business involved as a creditor in a Chapter 11 bankruptcy case to be added to the creditors committee by the court. The court could make such an appointment by comparing the amount of the claim as a proportion of the business 'gross annual revenue,' thus showing that a business is disproportionately affected.

*Second, my amendment will ensure that those small businesses not included on the creditor committee will have access to critical information regarding the credit [sic] committee's actions. This could be achieved by simply making the committee open to comments from and required to provide additional information to those small businesses not included on the committee but who will nonetheless be affected by the outcome.*

145 Cong. Rec. H2709-08 (Daily Ed. May 5, 1999) (Emphasis added).

The language contained in §1102(b)(3) does not limit the duties imposed on a creditors' committee to share information solely with small businesses. *See*, Vance, Catherine E. Development Specialists, Inc. "The Origin of Information Sharing under New §1102(b)(3)(C)" (2006). As indicated below, none of the courts that have thus far interpreted §1102(b)(3) has suggested that the statute should be limited consistent with the Congressional intent expressed at the time that the amendment was first introduced. Moreover, the plain language of the statute does not suggest such an interpretation. Furthermore, it is unlikely that courts will delve into congressional intent when the language of the statute is clear and unambiguous on its face, consistent with standard rules of statutory construction.

**C. Cases Interpreting §1102(b)(3)**

- (i) *In re Refco*, 336 B.R. 87 (Bankr. S.D.N.Y. 2006)

Creditors' Committee filed motion seeking protective order and to establish protocols for dealing with new duties under §1102(b)(3). Initially, Bankruptcy Judge Drain expressed concern that the relief being requested was in the nature of an advisory opinion because there was no actual controversy pending before him. Rather, the Committee was, in essence, requesting a comfort order and the court questioned whether it had jurisdiction to grant such relief under these circumstances.

The Committee was concerned that if it did not obtain an order setting forth the protocols to be observed, §1102(b)(3) could be interpreted to impose obligations contrary to other applicable laws (such as attorney-client privilege and securities laws) and further, cause the Committee to violate its fiduciary duties. Moreover, in light of the size of the case, the rapid pace at which the case was moving and the fact the debtor was a public company with its shares being traded, the Committee argued that it was of paramount importance for the Court to address these issues; otherwise the Committee would risk a complete curtailment on the flow of information from the debtor, thereby, precluding it from performing its statutory duties.

In ultimately deciding to accept jurisdiction and granting the relief sought by the Committee, the Court observed that §704(a)(7) provides that “a trustee shall ... furnish such information concerning the estate and the estate’s administration as is requested by a party in interest.” The court indicated that

even though this duty had been broadly interpreted, nonetheless, it did not require the release of confidential or proprietary information or information protected by the attorney-client privilege, or when disclosure of such information would interfere with a counter-veiling fiduciary duty.

In addition, in reaching its determination, the Court relied on *In re Gilcrest Co.*, 410 F.Supp. 1070 (E.D. Pa. 1976), a case decided under the Bankruptcy Act, which held that a committee was “not required to ‘forward to each creditor all the raw data it considers’ as if it were a virtual information bank for its constituents in the process of carrying out its duties.” *Refco*, 336 B.R. at 194 (quoting *Gilcrest*, 410 F.Supp. at 1078).

The Court further observed that “[I]t has frequently been held that committee members’ fiduciary duties of loyalty and care to the unsecured creditor body require such information to be held in confidence. Otherwise, communications between the committee and third parties and among committee members themselves would be improperly curtailed, or the debtor might be harmed with a resulting decline in the creditors’ recovery.” *Id.*

Thus, in order to establish a balance between the committee’s duties under §1103(b)(3), the need to protect access to sensitive information, the attorney-client privilege and compliance with the securities laws, the Court ordered the following procedures and protocols to be established:

- (a) A Committee website is to be established to provide general information about the debtor, calendar of significant events and dates, frequently asked questions, access to claims docket, committee reports and case updates.

- (b) The Committee is not required, without a court order, to provide access to confidential, proprietary or other nonpublic information about debtor or Committee, or information that would constitute a waiver of the attorney-client privilege.
  - (c) Requests for information under Federal Rule of Bankruptcy Procedure 2004 are not covered by protocol.
  - (d) Debtor is to assist the Committee in identifying confidential information.
  - (e) The Committee must respond to requests for information within 20 days of response from creditor for information. If request is denied, creditor may meet with committee, and if creditor is not able to resolve request, the requesting creditor can seek information through filing a motion with the court. If request implicates confidential information and the Committee, nevertheless, agrees to comply with the request, the Committee may send a demand to the debtor or other entity with 15 days to respond.
  - (f) The Committee may require creditor requesting information to agree to confidentiality agreement and trading restrictions.
  - (g) The Protocol provides exculpation of Committee and its members for any action taken thereunder.
  - (h) A creditor may request a confidentiality log and an *in camera* review of material claimed to be confidential by the Court.
- (ii) *Oneida* (S.D.N.Y.): the Court adopted similar provisions as in *Refco* and authorized the Committee to use debtor's noticing agent and debtor's website to provide information.
- (iii) *J.L. French Automotive Casting, Inc.*, Case No. 06-10119(MFW)

The Court adopted similar procedures to *Refco*, and in addition, required the following:

- (a) Committee counsel to provide access to information by maintaining copy of all material pleadings and providing copy upon a creditor's written request.

- (b) Committee counsel required to be available to respond to telephonic inquires regarding the status of case. In lieu of responding to telephonic inquiries, the Committee was authorized to direct creditors to make inquiries via email. In addition, as a condition to providing information and access, the Committee may require the requesting creditor to provide credentials to assure that it is an unsecured creditor entitled to access and the information.
  - (c) Debtor's noticing agent required to be available to respond to creditors' questions regarding information related to claims resolution process, notice of claims bar date, notice of objections to claims, and copies of all proofs of claim and proofs of interest.
  - (d) Committee members restricted with respect to use of confidential information -- must keep confidential, not use it for competitive or business purpose or work not related to cases, not disclose to anyone other than employees, advisors and agents (subject to their treating such information as confidential and execution of a confidentiality agreement acceptable to debtor and, if requested, a protective order) -- unless disclosure is required by subpoena or court process or debtor consents to such disclosure in writing.
  - (e) The Court appeared to approve the protocol as satisfying the requirements of Section 1102(b)(3)(A) and (B) based on the size of the chapter 11 case and the Debtors' proposal to pay substantially all trade creditors in full pursuant to the plan, coupled with the confidentiality procedures.
  - (f) The Court held that the information and confidentiality procedures discharged the Committee's obligations to (a) provide access to information to creditors, and (b) to solicit and receive comments from creditors under Section 1102(b).
  - (g) The Committee was permitted, but not directed, to utilize a website for the purpose of providing access to documents, pleadings and other information and materials to creditors.
- (iv) *In re Calpine Corp., et al.*, Case No. 05-60200 (Bankr. S.D.N.Y. 2006).

Judge Lifland provisionally granted the Committee's motion providing that the Committee was not required to disseminate any nonpublic information to anyone other than the Committee members.

Thereafter, Judge Lifland entered a stipulation and order setting forth guidelines consistent with the *Refco* order.

- (v) *In re FLYi, Inc., et al.*, Case No. 05-20011 (Bankr. D. Del 2005).

Judge Walrath held that the Committee was not required to disclose “confidential information” or “privileged information” under §1103(b)(3). In addition, the Court held that the Committee was sole party to control the privilege.

- (vi) *In re Dana Corp., et al.*, Case No. 06-10354 (Bankr. S.D.N.Y. 2006).

Judge Lifland entered an order similar to Judge Walrath in *FLYi, Inc.* Unlike *Refco* and *FLYi, Inc.*, the Court did not (i) establish a deadline for the Committee to respond to inquires for information or (ii) require the Committee to establish a website to provide access to creditors for information.

- (vii) *In re Amcast Automotive of Indiana, Inc. and Amcast Industrial Corporation*, Case No. 05-33322-FJO-11 (Bankr. S.D. Ind. 2006).

Judge Otte granted the Committee’s motion and provided as follows:

- (a) The Committee, through counsel, will share any non-confidential or public information.
- (b) The Committee was ordered to maintain a copy of all pleadings and provide copies to any individual or entity making a written request.
- (c) Committee counsel is to be available to parties requesting details regarding status of case via telephone calls from creditors.
- (d) The Committee is not required to share any confidential, privileged or nonpublic information defined very broadly, to include: “(a) information regarding debtor’s assets, liabilities, business operations, projections, analysis, compilations, studies

and other documents prepared by debtors or their advisors or other agents, furnished, disclosed or made known to the Committee; (b) any notes, summaries, compilations, memoranda or similar written material disclosing or discussing confidential information, (c) any other confidential information conveyed to committee orally that debtors or their advisors advise committees should be treated as confidential.”

(e) The Committee controls, in its sole discretion, what is “Privileged Information” or “Confidential Information.”

(f) If a request for information is made and the Committee fails or refuses to produce, creditor may seek an order from the court making specific reference to the information sought.

(viii) *In re Glycogenesys, Inc., et al.*, Case No. 06-10314-JNF (Bankr. D.Mass. 2006).

In this case, the debtors filed a motion seeking to establish a protocol by which information would be authorized or permitted to be provided to creditors by the Committee under Section 1102(b)(3)(A). The Committee responded to the motion and, while conceding that such relief was needed, nevertheless, was concerned with the form of the order that the debtors had submitted for establishing the protocol. Ultimately, Judge Feeney entered an order clarifying the scope of the Committee’s obligations, similar to those orders entered by the Court in *Pliant Corp.* The order was subsequently amended and, in large part, tracts the requirements contained in new proposed Local Bankruptcy Rule 2003-1 for the Bankruptcy Court for the District of Massachusetts.<sup>2</sup>

New Local Bankruptcy Rule 2003-1 for the District of Massachusetts establishes a process and procedure by which creditors’ committees can satisfy

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<sup>2</sup> The new Local Bankruptcy Rules for the District of Massachusetts have been noticed for comment and are expected to be final and operative soon. While other bankruptcy court are reviewing and revising their local rules in light of the adoption of BAPCPA, at this juncture, no other bankruptcy courts have yet issued rules establishing committee protocols.

their new statutory requirements under Section 1102(b)(3)(A) without having to file a motion seeking the establishment of a protocol. The rule requires:

(a) General Requirement: committees are required to respond to written, telephonic and/or electronic inquiries from unsecured creditors and to provide access to documents, pleadings and other materials that the committee believes “in its reasonable business judgment” are “relevant” and “informative.” Such information must be provided not later than 20 days after appointment of committee counsel. The committee is required to advise all general unsecured creditors of the preferred means to make inquiry. This time period is subject to enlargement by the court.

(b) Limitation on General Requirement: the committee is not required to disclose “confidential information.” “Confidential information” is defined as: “any nonpublic information subject to a confidentiality agreement with the debtor or another entity or other nonpublic information the committee “believes in its reasonable judgment” should be confidential for the committee to perform its duties and (i) was furnished to the committee by the debtor or (ii) was developed by professionals employed by the committee and disclosure of which would impair performance of their duties.

The rule then defines what is not confidential as: if the information (i) becomes generally available to the public; (ii) becomes available to the committee on a nonconfidential basis so as not to violate a contractual, legal or fiduciary obligation to the debtor; or (iii) was in possession of the committee prior to its disclosure by the debtor or committee professionals and is not subject to any other duty to maintain confidentiality.

(c) Limitation on Privileged Information: The committee is not required to disclose or provide access to “privileged information.” “Privileged Information” is defined as: “any information subject to the attorney-client privilege or other state, federal or other privileged whether controlled solely by the committee or jointly with the debtor or other party.” The committee is permitted, but not required, to share privileged information so long as it is not confidential and the privilege at issue is held solely by the committee.

(d) Creditor Remedies: If a creditor is denied access to information and is not satisfied, the creditor may file a motion with the court seeking to compel productions of the documents or

information. The filing of such a motion is deemed to constitute a “discovery dispute” subject to MLBR 7037-1, as applicable.

(e) What the New Local Rule Does Not Provide: The new local rule does not (i) set forth or mandate any specific time period by which the information or documents must be provided; (ii) how to process requests for information; (iii) the extent to which the committee may need to deal with the debtor on requests for information and determining what is confidential and/or privileged; (iv) timing for responding to requests or denials for information; (v) does not contain any exculpation provisions; (vi) does not provide for the involvement and/or participation of claims agents; (vi) does not specify what documents and/or pleadings must be maintained by the committee; (vii) does not require the preparation or maintenance of a privilege log; and (viii) does not provide for or mandate trading restrictions or execution of confidentiality agreements as conditions precedent to receiving information.

(ix) In some smaller cases, instead of filing a motion seeking an order establishing a protocol, committees have merely transmitted a letter to creditors advising them about status of case, the nature of Chapter 11, key bar dates, the process and procedures for obtaining information when a request is denied by Committee and notice that “confidential and privileged” information will not be released or disclosed.

**D. Committee Composition Under Section 1102(a)(4)**

In 1986, the Bankruptcy Code was amended to delete former Section 1102(c) which gave the court, on request of a party in interest and after notice and a hearing, the right to change the membership or size of a committee if the court found that the membership was not representative of the different kinds of claims or interests to be represented thereon. A conflict arose among the courts regarding the impact of this change. The majority of the courts held that this statutory deletion still allowed the courts to review the U.S. Trustee’s appointment for abuse of discretion or on a de novo basis. A

minority of the courts held that the repeal of this subsection deprived courts of the right to review the U.S. Trustee's committee appointment. The change to Section 1102(a)(4) appears to have resolved this split.

Section 1104(a)(4) provides, in relevant part, as follows:

On request of a party in interest and after notice and a hearing, the court may order the United States trustee to change the membership of a committee appointed under this subsection, if the court determines that the change is necessary to ensure adequate representation of creditors or equity holders. The court may order the United States trustee to increase the number of members of a committee to include a creditor that is a small business concern (as described in section 3(a)(1) of the Small Business Act); if the court determines that the creditor holds claims (of the kind represented by the committee) the aggregate amount of which, in comparison to the annual gross revenue of that creditor, is disproportionately large.

There is very little legislative history regarding this new provision. Moreover, the new Code provision does not provide any standard that the court is required to apply in making decisions about the constitution, or reconstitution, of a committee. Possibly, courts will look to pre-BAPCPA law to determine how to apply this section. *See* Hon. Jeffrey A. Deller, Laura Davis Jones, Edward T. Gavin, Adam G. Landis, and Mary E. Seymour, "*Report From the Front: Creditor Committees After BAPCPA*," American Bankruptcy Institute, Mid-Atlantic Bankruptcy Workshop, July 2006. The section also appears to grant the courts greater discretion to appoint a small business concern as a member of a committee when that creditor generally would not otherwise qualify to serve on a committee under Section 1102(a)(1).

Since this section of the Bankruptcy Code was amended, the issue of how a committee was constituted, or should be reconstituted, has arisen in the case of

*In re Werner Holding Co. (DE), Inc., et al.*, Case No. 06-10578 (KJC) (Bankr. D.Del. 2006). In this case, after the Committee, consisting of 3 trade creditors, a holder of the notes and an indenture trustee for the notes, was appointed by the U.S. Trustee, Murray Capital and Claren Road, 2 hedge funds holding unsecured notes issued by the debtor and members of an ad hoc pre-petition committee, filed a motion seeking to be appointed to the Committee after the U.S. Trustee had failed and refused to appoint them to the Committee. Both hedge funds had prepared and submitted questionnaires to the U.S. Trustee seeking to be appointed to the Committee. In filing the motion, the hedge funds relied on new Section 1102(a)(4) for the relief sought – reconstitution of the Committee by adding them as additional members to the Committee.

A review of the Debtors' schedules reflected that they had approximately \$143.0 million in principal and interest due and owing on the notes (\$5.7 million of which was held by Murray Capital and \$1.0 million of which was held by Claren Road. The Debtors' trade debt approximated \$18.0 million on the petition date and, based on certain first day orders entered by the Court, the hedge funds contended that approximately \$8.0 million of the trade debt was expected to be paid over the first month of the case. The hedge funds argued that after payment of this trade debt, the overwhelming proportion of unsecured debt would be held by the noteholders (approximately 93.5%), and thus, "a committee comprised of one Noteholder, three trade creditors and BNY [the Indenture Trustee] does not adequately represent the interests of Noteholders." They also contended that, absent reconstitution of the Committee, an ad hoc committee of noteholders

would need to be formed because the Committee was controlled by a small group of trade creditors and “[t]he Debtors cannot reliably negotiate a plan of reorganization with the Committee with the assurance that the Committee can “deliver” the support of the Noteholders for positions taken by the Committee,” thereby necessitating the formation of an ad hoc committee of noteholders to ensure that their interests were pursued, articulated and protected. Ultimately, if the motion were granted, it would change who would control the Committee – the trade vendors or the noteholders, and potentially open up the entire selection process for Committee appointment. The U.S. Trustee objected to the motion.

While the Court did not ultimately make a ruling on the motion, an extensive hearing with legal arguments was held on the motion. The transcript of the initial hearing does not necessarily set forth how the Court may have ruled on the motion; nevertheless, it provides insight from the Court regarding the issues raised in the motion. At the hearing, the Court stated:

. . . I agree with you that the amendments answered the question of who ultimately was the decision maker on whether the Committee adequately represent - - was adequately represented.

What it didn’t answer was at least two things:

One is what’s the standard to be applied by the Court in determining adequate representation, whether it’s abuse of discretion or de novo review. Frankly, I’m inclined to apply a de novo standard.

But depending on what the record is, it may not matter what the standard is in this case.

And secondly, whether the Court can specifically name who ought to be - - who ought to be added to the Committee.

My thought was that the United States Trustee is right. That what the Court is limited to doing is determining whether the standard under the Statute’s met. And if not, simply directing that the United States Trustee make adjustments.

In responding to the movant's arguments, the Court also indicated "[t]here's nothing inherent in the memberships which prevents [the members of the Committee] from [adequately representing the interests of the unsecured creditors]. Your argument is, well, the disproportionality of it in this case does prevent that. But the cases say, you know, proportionality, as I read and distill them may be a factor, but it's not the be all and end all." *Id.* at pg. 16, lines 16-22. Rather, to determine and assess whether reconstitution was appropriate, the Court would need to review and assess various other factors, such as the ability of the Committee to function and the ability of parties not on the Committee to be represented outside the formal committee process, utilized by courts in pre-BAPCPA cases. *Id.* at pg. 80, lines 20-23.

The Court expressed concern about the disparity of representation (based on the amount of debt) and the basis of the U.S. Trustee's decision in appointing the Committee, particularly in deviating from the requirement under Section 1102(a)(1) to appoint a seven-member committee holding the largest unsecured claims. In response to this query, the U.S. Trustee initially attempted to invoke "the Government deliberative process privilege" to negate having to respond to the Court's question. The Court dismissed this response because, according to Judge Carey, "I don't see anywhere in the Statue where it relieves the U.S. Trustee upon challenge from having to explain the departure." *Id.* at pg. 43, lines 14-16. Thereafter, the U.S. Trustee tried to explain in a very limited fashion, the bases of its selection and appointment process. As a result of the failure of the U.S. Trustee to fully explain and disclose information key to its decision process – information that was exclusively within the province of the U.S. Trustee – the Court indicated that the initial burden to come forward that is generally on the movant

may in this instance shift to the U.S. Trustee to come forward and adequately explain its decision process.

During the hearing, the Court asked the parties to take a break to attempt to resolve the issues and for the U.S. Trustee to consider voluntarily reconstituting the Committee. After the break, the U.S. Trustee advised the Court of its unwillingness to take such action. Ultimately, the matter was adjourned for an evidentiary hearing because, on the record presented, the Court was unable to make a ruling. Prior to evidentiary hearing, the U.S. Trustee relented to resolve the issues contained in the motion and appointed both of the hedge funds and the Pension Benefit Guaranty Corporation as additional members to the Committee.

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**Report From the Front: Creditor Committees After BAPCPA**

**Hon. Jeffery A. Deller**  
**United States Bankruptcy Court – Pittsburgh, PA**

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## I. General Case Issues

A. **MIPs– Changes Have Increased Committee’s Power.** Congress amended Bankruptcy Code Section 503 to “significantly restrict” a debtor’s “ability to pay bonuses, severance payments, and other payments to insiders of the debtor after the case is filed.” H.R. Rep. No. 109-31 (109<sup>th</sup> Cong., 1<sup>st</sup> Sess. 2005) at 19. Since the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (“BAPCPA”), debtors have been creative in developing employee plans that are not related to “stay” bonuses but rather are tied to specific performance goals or sales. It is the Creditors’ Committee’s job in many instances to flush out these new programs and determine whether, no matter what they are called by the debtors, they meet the standards of Bankruptcy Code Section 503. An analysis of recent cases follows.

1. *In re Nobex Corporation – Case No. 05-20050 (MFW).* In *Nobex*, the Debtor sought authority to pay sale-related incentive pay pursuant to Bankruptcy Code Sections 105, 363(b) and 503(c)(3) to Charles Dimmler, the Debtor’s Chairman and Chief Executive Officer, and Russell M. Savre, the Debtor’s Vice President of Finance and Administration. The Debtor proposed to pay certain percentages if the sale price exceeded various points. In support of the motion, the Debtor argued that the payments were a valid exercise of its business judgment pursuant to Section 363(b). The Debtor further argued that to the extent Bankruptcy Code Section 503(c)(3) applied, the Court should approve the payments as the additional incentive pay is necessary and designed to ensure the complete implementation of the sale process, not to induce the insider employees to remain with the Debtors (such that Sections 503(c)(1) and (c)(2) did not apply).

The United States Trustee (“UST”) and the Creditors’ Committee objected. The Creditors’ Committee argued that the payment was a retention bonus and the Debtor had failed to meet the standards of Bankruptcy Code Section 503(c). Specifically, the Creditors’ Committee argued that Debtor had failed to state what specific duties the employees would perform in connection with the sale, whether they have other job offers, or whether they received retention compensation in the past year. Likewise, the UST argued that the Debtor was attempting to avoid the restrictions and evidentiary burdens of the new code provisions.

After a contested hearing, the Court approved the motion. Judge Walrath stated that she did not believe this was a retention program and Section 503(c)(1) did not apply. The Court further stated that she placed great weight on the fact that (a) the Creditors’ Committee, whose constituency was the ultimate beneficiary of a successful sale, was now on board with the motion and the payments and (b) the payments were not merely connected to a stalking-horse sale that had already been contemplated by

the stalking horse bid, rather the insiders would not get paid unless the sale price increased. Finally, the Court found the payments were reasonable and helped to maximize the value of the Debtor's assets.

2. *In re Pliant Corporation – Case No. 06-10001 (MFW)*. In this motion, the Debtors sought approval to make certain performance-based incentive compensation payments under the Debtors' prepetition Management Incentive Compensation Plan (the "MIP") pursuant to Bankruptcy Code Sections 105, 363(b)(1), 1107(a) and 1108 and the necessity of payment doctrine. The compensation under the MIP was based on certain performance goals as determined by the Debtors' compensation committee. The Debtors argued that Bankruptcy Code Sections 503(c)(1) and (c)(2) did not apply because the payments were neither retention nor severance payments. The proposed MIP payments covered 88 non-insider employees and 12 insider employees in the aggregate amount of \$3.2 million.

An ad hoc committee of secured noteholders (the "Ad Hoc Committee") objected to the motion solely with respect to payments to the insiders, disputing that Bankruptcy Code Sections 503(c)(1) and (c)(2) did not apply. The Ad Hoc Committee argued that the Debtors' attempt to use prepetition events to make postpetition payments to insiders, without a requirement that the insiders remain with the Debtors or continue to perform, directly contradicts this new provision and applicable case law. The Ad Hoc Committee further argued that any amounts in excess of \$10,000 (the statutory cap under Bankruptcy Code Section 507(a)(4)) should not be approved because the Debtors had failed to establish a compelling justification.

The UST also filed an objection and argued that the necessity of payment doctrine did not apply because the Debtors failed to show that absent payment of the prepetition MIP obligations, there was no real or immediate threat of harm to the Debtors' operations. The UST further argued that since the proposed reorganization plan paid the MIP obligations in full and the employees were incentivized to continue to perform in order to receive their 2006 MIP payments, there was no justification to make the prepetition payments prior to confirmation.

The Court heard testimony and oral argument on the motion. It seems that at the hearing, the Ad Hoc Committee abandoned the argument that Sections 503(c)(1) and (c)(2) applied and argued that the payments to insiders should be analyzed under a heightened standard and denied. The Court granted the motion in part. The Court found that the payments were not retention or severance payments and did not violate any of the new provisions of the Bankruptcy Code. The Court approved the payments to the non-insiders even though they exceeded the statutory cap. Judge

Walrath stated that pursuant to Delaware corporate law she was bound to review payments to insiders with a higher level of scrutiny and higher level of consideration of rights of the other parties. The Court expressed concern that the payments to the insiders were more than the median compensation of their peers and was disturbed by the amount of discretion the compensation committee had. The Court permitted the payment to the insiders as long as the cumulative, total compensation package equaled the median, or 50th percentile of their peers, and reserved the issue of payment of the other 50% until confirmation of the plan.

3. *In re Riverstone Networks, Inc. – Case No. 06-10110 (CSS)*. In this motion, the Debtors sought authority to continue certain prepetition employee and management programs. Specifically, the Debtors sought authority to pay (1) certain non-management employees: (a) time-based bonuses for certain employees who remained at the company for a certain period of time in the aggregate amount of \$3 million; (b) performance-based bonuses for certain employees in the aggregate amount of \$1.3 million; and (c) a discretionary bonus pool of up to \$750,000; and (2) certain management employees an aggregate amount of \$1.5 million, after approval by the Debtors' compensation committee. Finally, the Debtors sought approval of their personal time off ("PTO") policy. The Debtors argued that the continuation of these policies and the making of these payments were a valid exercise of the Debtors' business judgment pursuant to Bankruptcy Code Sections 105 and 363(b) and the necessity of payment doctrine. The Debtors also stated that the payments under the PTO policy were permitted under Bankruptcy Code Section 503(c)(2) because, for PTO payments to insiders, the PTO policy is available to all of the Debtors' full-time employees and the amount would not be greater than the statutory ceiling.

An equity holder ("Grimes") objected to the motion, arguing that all of the payments were prepetition claims and not authorized under the Bankruptcy Code. Grimes stated that the Debtors had failed to make a showing that the payments were necessary to the continued operation of the Debtors, particularly since the Debtors were close to finalizing the sale of substantially all of their assets and some of the employees were to be hired by the purchaser.

The Equity Committee also filed an objection arguing that it needed more information to analyze the proposals and that the Debtors had failed to establish that the payments were appropriate under Bankruptcy Code Section 503(c). The Creditors' Committee also had informal objections relating to the timing of payments, not the amounts.

At the evidentiary hearing on the motion, the parties agreed that the non-management payments could be paid. The Court heard evidence on the

management portion of the payments and continued the motion because the Debtors had failed to make an evidentiary record that the bonuses were earned or, if not earned, an appropriate exercise of the Debtors' business judgment. After a further evidentiary record, the parties agreed to the entry of an order authorizing the payments to management but preserving all parties' rights to object to the actual payment once authorized by the Debtors' compensation committee.

4. *In re LG.Philips Displays USA, Inc. – Case No. 06-10245 (BLS)*. In this motion, the Debtor sought authority to approve its severance and key employee retention plan for its three employees. Generally, the Debtor sought authority to pay one year's salary as severance, plus unused accrued vacation. In addition, the Debtor sought authority to pay its president and director of sales, Mr. Canavan, a retention bonus. Mr. Canavan had received and accepted another job offer but agreed to stay for two more weeks and consult during non-business hours thereafter. The Debtor argued that these were necessary costs of preserving the estate pursuant to Bankruptcy Code Section 503(b)(1) and were an exercise of the Debtor's business judgment pursuant to Bankruptcy Code Section 363(b). Finally, the Debtor argued that the retention payment to Mr. Canavan met the requirements of Bankruptcy Code Section 503(c)(1) because he had a bona fide job offer, his new salary was higher than the current salary and he would leave absent the retention payment. The Debtor further stated Mr. Canavan's employment was necessary to the Debtor's continued business.

The UST objected to the motion because the Debtor had failed to meet the standards under Bankruptcy Code Section 503(c) and failed to disclose the prepetition compensation to the employees, the proposed severance or retention amounts or whether each of the employees was an insider.

At an evidentiary hearing, the Court expressed some concern that Mr. Canavan would not remain employed with the Debtor. The Debtor and the other parties, after a recess, agreed to retain Mr. Canavan as a consultant to resolve the retention issues. After testimony and argument, the Court ruled that, other than Mr. Canavan, the employees were not insiders of the Debtor and Bankruptcy Code Section 503(c)(2) did not apply. The Court approved the remainder of the motion holding that the services were necessary to preserve the value of the estate. The Court also gave great weight to the fact that the secured lender and the Creditors' Committee supported the motion.

5. *In re Global Home Products – Case No. 06-10340 (KG)*. The Debtors filed a motion for approval of a management sale incentive plan. Specifically, upon the closing of the sale of certain of the Debtors' assets, the Debtors proposed to pay a one-time incentive payment ranging from

25% to 70% of the employees' annual salary, with the aggregate amount not to exceed \$520,600. The Debtors stated that the payments are a valid exercise of their business judgment. The Debtors further stated that they are not retention or severance payments subject to Bankruptcy Code Sections 503(c)(1) or (2) because they are not intended to induce anyone to remain with the Debtors but rather are to incentivize the employees to reach a performance goal – the successful sale of certain assets.

The Creditors' Committee objected to the motion arguing that it was a "thinly veiled attempt to avoid the recent amendments." The Creditors' Committee argued that the payments were compensating the employees, including three insiders, for something that had already happened and therefore, could not be treated as an "incentive."

A hearing on the motion was held on May 23, 2006, wherein the Debtors reported that they had agreed to reduce the aggregate amount of incentive payments to \$361,100 and such payments were conditioned on the closing of the sale.

6. *In re Nellson Nutraceutical, Inc. – Case No. 06-10072 (CSS)*. In this case, the Debtors filed a motion for authority to make payments under a management incentive plan. Specifically, the Debtors sought to make payments upon reaching certain performance goals in an aggregate amount of \$1.395 million. The Debtors argued that these payments were a valid exercise of their business judgment.

The Creditors' Committee filed an objection to the motion stating that (a) the management incentive plan was a poorly-disguised KERP that violates Bankruptcy Code Section 503(c)(1); (b) the payments were excessive and contained bonuses even if the Debtors failed to achieve their budgeted EBITDA by as much as 50%; (c) certain payments were tied to events unrelated to the Debtors' financial performance, such as termination of the employee or plan confirmation; and (d) the payments were in addition to any pre-petition KERP obligations of the Debtors.

A hearing on the motion has not been held.

#### **B. Committee Composition; Bankruptcy Code Section 1102(a)(4)**

- The 1986 amendments deleted former subsection 1102(c), which read: "On request of a party in interest and after notice and a hearing, the court may change the membership or the size of a committee appointed under subsection (a) of this section if the membership of such committee is not representative of the different kinds of claims or interests to be represented."

- A minority of courts held that the repeal of this subsection meant that courts had no authority to review the UST's appointment of a committee. *See e.g., In re New Life Fellowship*, 202 B.R. 994, 996 (Bankr. W.D. Okla. 1996) (UST has exclusive authority to appoint committees and the bankruptcy court is without power to abolish the committee).
- Most courts held that the bankruptcy court could review the UST's decision on committee appointment on either a *de novo* or abuse of discretion standard. *See e.g., In re Doehler-Jarvis, Inc.* 1997 U.S. Dist. LEXIS 24128 (D. Del. October 7, 1997) (since the repeal of Bankruptcy Code Section 1101(c), the Court does not have the authority to appoint any member to a committee but can review the UST's decision to determine if the UST acted appropriately); *In re Columbia Gas Sys.*, 133 B.R. 174, 176 (Bankr. D. Del. 1991) (bankruptcy court may review UST's refusal to appoint certain creditor to creditors' committee under abuse of discretion standard); *In re TransWorld Airlines, Inc.*, 1992 Bankr. LEXIS 1344, \*5 (Bankr. D. Del. March 20, 1992) (bankruptcy court may not expand creditors' committee unless it is demonstrated that UST abused its discretion); *In re Public Service Co. of New Hampshire*, 89 B.R. 1014, 1021 (Bankr. D.N.H. 1988) (bankruptcy court reviewed UST's decision to not appoint separate bondholder committee or to add more committee members *de novo*).
- Scant legislative history exists but the purpose of the addition of Section 1102(a)(4) under BAPCPA appears to be to resolve the split in the Circuits on court review of committee appointment.
- *In re Delphi Corp. – Case No. 05-44481 (RDD)* (pre-BAPCPA case). GM filed a motion under Bankruptcy Code Sections 105 and 1102(a)(2) seeking an order directing the UST to appoint them to the creditors' committee. GM argued that it was the only major creditor constituent not appointed to the committee (the UAW and PBGC were also not appointed but after request was made on the UST, become *ex officio* members). GM argued it was the debtors' largest and most important customer and UST's failure to appoint it to the committee was "arbitrary and capricious." The creditors' committee objected arguing that giving GM a "seat at the table" would limit the committee's ability to receive material information from the debtors. GM ultimately withdrew the motion based on the parties' position that GM was an adversary in this case and a seat on the committee would be counterproductive.
- Issues: What is the standard to be applied under Section 1102(a)(4)? Does this create issues with large customers, competitors, etc., trying to get a seat on the committee – or are these issues already resolved based on pre-BAPCPA law?

## II. Section 1102(b)(3) Obligations

### A. **Background and In General**

Bankruptcy Code Section 1102(b)(3), as added pursuant to BAPCPA, provides that a creditors' committee appointed under Section 1102(a): "shall (A) provide access to information for creditors who (i) hold claims of the kind represented by the committee; and (ii) are not appointed to the committee; (B) solicit and receive comments from the creditors described in subparagraph (A); and (C) be subject to a court order that compels any additional report or disclosure to be made to the creditors described in subparagraph (A)." 11 U.S.C. § 1102(b)(3).<sup>1</sup> Prior to the BAPCPA amendment, there was no such or similar provision in the Bankruptcy Code requiring the sharing of information with creditors or solicitation of comments from creditors by statutory committees. Importantly, an overly broad information-sharing obligation on the part of committees could potentially chill a debtor from sharing confidential and other sensitive, non-public information with the committee (in the fear that such information would have to then be turned over by the committee to creditors, notwithstanding any confidentiality agreements between the debtor and committee), thus hindering and harming the committee's advisory and investigative roles and functions in the case. Further, an overly broad construction of Section 1102(b)(3) would almost certainly increase compliance expenses of committees and their counsel and other professionals, which would likely be borne by the debtors' estates.

Unfortunately, Section 1102(b)(3) is patently ambiguous on its face regarding committee obligations as to the nature, scope and extent of the information to be provided to creditors, and how access to said information is to be provided. And, there is no enlightening legislative history on this particular provision.<sup>2</sup> Thus, upon the motion of either debtors or official committees (made often in a "first day" motion in the case of the debtor or made promptly after committee formation in the case of the latter), courts in numerous cases, including the following, have

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<sup>1</sup> This particular amended provision applies only to cases filed after October 17, 2005. While the language in this statute does not expressly exclude equity committees (the statute simply provides that a "committee appointed under subsection (a) shall ...."), the operative provisions refer specifically and only to "creditors," and thus, by implication, Section 1102(b)(3) must apply only to creditors' committees.

<sup>2</sup> See H.R. Rep. No. 109-31, 109<sup>th</sup> Cong., 1<sup>st</sup> Sess. 87 (2005) ("Section 405(b) requires the committee to give creditors having claims of the kind represented by the committee access to information. In addition, the committee must solicit and receive comments for these creditors and, pursuant to court order, make additional reports and disclosures available to them."). While there is also available some early, related legislative history, such legislative history does not shed meaningful light on the scope of committees' information sharing obligations (other than possibly that the proponents' intent behind the earliest incarnation of this provision was to have it, at that point, applicable only as to small-business creditors). See 145 Cong. Rec. H2709-08 (daily ed. May 5, 1999) (statement of Rep. N. Velazquez; "my amendment will ensure that those small businesses not included on the creditor committee will have access to critical information regarding the credit [sic] committee's actions. This could be achieved by simply making the committee open to comments from and required to provide additional information to those small businesses not included on the committee but who will nonetheless be affected by the outcome.") (quoted and discussed in Catherine E. Vance, Development Specialists, Inc., "The Origin of Information Sharing Under New § 1102(b)(3)").

adopted procedures and protocols to flesh out this amendment and make it workable for committees, as well as debtors: *In re FLYi Inc.*, Case No. 05-20011 (MFW) (Bankr. D.Del.) (upon debtors' motion; order entered after committee formation); *In re Global Home Products, LLC*, Case No. 06-10340 (KG) (Bankr. D.Del.) (upon debtors' motion; order entered after committee formation); *In re Nellson Nutraceutical, Inc.*, Case No. 06-10072 (PJW) (Bankr. D.Del.) (upon debtors' motion; order entered after committee formation); *In re Nobex Corp.*, Case No. 05-20050 (MFW) (Bankr. D.Del.) (upon debtor's motion; order entered after committee formation); *In re Pliant Corp.*, 06-10001 (MFW) (Bankr. D.Del.); *In re Riverstone Networks Inc.*, 06-10110 (CSS) (Bankr. D.Del.); *In re World Health Alternatives, Inc.*, Case No. 06-10166 (Bankr. D.Del.) (PJW); *In re Calpine Corp.*, Case No. 05-60200 (BRL) (Bankr. S.D.N.Y.); *In re Refco Inc.*, Case No. 05-60006 (RDD) (Bankr. S.D.N.Y.); *In re G+G Retail, Inc.*, Case No. 06-10152 (RDD) (Bankr. S.D.N.Y.); *In re Oneida Ltd.*, Case No. 06-10489 (ALG) (Bankr. S.D.N.Y.); *In re Amcast Industrial Corp.*, Case No. 05-33322 (FJO) (Bankr. S.D.Ind.). (Copies of the applicable orders entered in the *FLYi*, *Global Home*, *Pliant* and *Riverstone* cases (“[\_\_\_\_\_] Order”) are attached hereto as Exhibits A through D, as examples.)

#### B. **The *Refco* Decision**

In *In re Refco Inc.*, 336 B.R. 187 (Bankr. S.D.N.Y. 2006), the first reported opinion addressing the § 1102(b)(3) obligations, Judge Robert Drain of the Southern District of New York set forth certain conditions for committees to meet their new disclosure and solicitation obligations, which in large measure have been adopted by courts outside the Second Circuit as well. Because the committee in that case was undertaking an enormous investigation into litigation related matters (involving the exchange of confidential information with the debtors and other parties), and with the complication of the debtor being subject to securities laws, the committee moved shortly after its appointment for approval of a suitable protocol under Section 1102(b)(3). The committee, debtor and U.S. Trustee negotiated an interim order which subsequently, with some modifications, became the final order of the court. In light of the quickly moving proceedings and the lack of guidance from Congress, the *Refco* court issued its decision to provide the necessary guidance.

As set forth in its opinion, the *Refco* court balanced, among other things, (i) the need for confidential information to be protected and in connection therewith, the concern over potentially chilling negotiations and interaction between the committee and the debtor and other parties in interest in case such information would have to be disclosed to the creditor body, (ii) the need for the committee to preserve its attorney-client and other privileges, and (iii) the overlay of securities law requirements and concerns. Based on its consideration of such factors, the court approved a protocol which allowed disclosure of specified information (discussed below) to creditors while restricting the disclosure of information that would violate securities laws, prohibit or hinder discussions with the debtor

and/or breach applicable privileges; provided that the committee would have to take into account the requesting creditor's willingness to agree to confidentiality and other constraints when considering that creditor's request for any confidential or privileged information. To carry out its obligations under Section 1102(b)(3), the court specifically directed the committee to (a) set up a fairly elaborate website on which pertinent case and other information could be accessed by creditors and through which creditors could ask questions and submit comments for review and response by the committee, (b) provide case updates via email to creditors who registered for such updates, (c) provide and maintain a telephone number and special email address for creditors to submit questions and comments, and (d) respond to creditors' requests for disclosure of information promptly (within 20 days). The court's order provided exculpation for the committee, the debtors, and other related parties from liability for actions taken in connection with the disclosure of information to creditors. Finally, under the court's order, the court would promptly decide any disputes where an agreement on information sharing could not be reached by the parties, and creditors could move for disclosure of confidential information (including requests for a log or index of confidential information and for *in camera* review). (A copy of the *Refco* court's order is attached hereto as Exhibit E.)

### C. Other Courts' Responses to Amended § 1102(b)(3)

Working in large measure off of the *Refco* Order and similar orders entered in other cases, various courts (primarily in the Second and Third Circuits) have adopted some or all of the following or similar procedures and provisions with respect to committees' obligations under Section 1102(b)(3):

(i) Absent further court order or consent of the debtor, the committee does not have to and cannot share with creditors any confidential or privileged information or other non-public sensitive information (such as vendor relationship information, intellectual property, or other proprietary information that could give the debtor's competitors an unfair advantage) obtained from the debtor or otherwise during the course of the case.<sup>3</sup>

(ii) In some cases, however, the committee would have reasonable discretion to decide what disclosure would be appropriate and disseminate the applicable information to creditors, provided that, for example, as may be

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<sup>3</sup> See, e.g., *Refco* Order, ¶ 4 (committee not required to disseminate to any entity (i) any "confidential, proprietary, or other non-public information concerning the Debtors or the Committee," and (ii) "any other information if the effect of such disclosure would constitute a general waiver of the attorney-client, work-product, or other applicable privilege possessed by the Committee"); *FLYi* Order, ¶¶ 4 and 6, p. 3 (similar); *Global Home* Order, p. 3 (similar); *Pliant* Order, pp. 2-3 (similar); *Riverstone* Order, ¶ 4, pp. 3-4 (similar). As discussed above with respect to the *Refco* decision, and as argued by committees and debtors in their motions for § 1102(b)(3) protocols, such a provision is generally justified on the grounds that the public dissemination of non-public information could prohibit meaningful discussions between the committee and debtor, jeopardize the value of the debtor's assets and business, potentially violate federal and state securities, privacy and/or other laws, and/or breach or waive attorney-client and/or other privileges.

necessary in some cases, the creditors execute confidentiality agreements or the debtor (or other affected entity) has no objection to the proposed disclosure.<sup>4</sup>

(iii) The committee must often establish a special email address or telephone number to allow creditors to send questions and comments, and the committee and its counsel must “in their reasonable discretion” review and/or respond to questions and comments.<sup>5</sup>

(iv) Frequently, committees have proposed and courts have authorized the setup of websites or other public databases which can be (a) accessed by creditors to obtain and review pleadings, debtors’ operating reports, and other public information which the committees reasonably believe should be provided to the creditor body, and (b) used to solicit from creditors comments, questions and information requests.<sup>6</sup>

(v) Creditors’ rights to seek specific, additional disclosure are not categorically impacted, and upon creditors’ motions, depending on the circumstances, the court may require additional disclosure.<sup>7</sup>

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<sup>4</sup> See, e.g., *Refco* Order, ¶¶ 3 (“the Committee may privately provide such responses [to creditor questions, comments and requests] in the exercise of its reasonable discretion, including in light of the nature of the information request and the creditor’s agreements to appropriate confidentiality and trading constraints”), 7 (committee may deny request if the request implicates confidential or privileged information that need not be disclosed by the order or if it is unduly burdensome; requesting creditor, after good faith effort to confer with committee representative, may file motion to compel disclosure for cause), 8, 9 (prior notice to and opportunity to object by debtors and other entities); *Global Home* Order, p. 3 (committee cannot release confidential information unless debtors consent, “which consent shall not be unreasonably withheld”); *Riverstone* Order, ¶ 7, p. 5 (committee must respond to creditors’ written requests for information within 20 days; committee may deny request if it implicates information that need not be disclosed pursuant to the order or if it is “unduly burdensome”; after good faith effort to meet and confer, creditor may file and serve motion seeking disclosure), ¶ 8, p. 6 (in connection with response to creditors’ requests for confidential information, committee must consider, *inter alia*, whether creditor is willing to agree to confidentiality and other restrictions), ¶ 9, pp. 7-8 (prior notice to and opportunity to object by debtors and other entities before release of confidential information). Compare with *FLYi* Order, ¶ 4, p. 3 (blanket provision stating that committee is not authorized to provide confidential information to creditors).

<sup>5</sup> See, e.g., *Global Home* Order, pp. 2-3 (committee “may” establish special email address and in its “reasonable discretion” review and/or respond to email correspondence); *Pliant* Order, p. 2 (special email address required but committee and counsel may “in their reasonable discretion” review and/or respond to email correspondence); *Riverstone* Order, ¶ 3, p. 2 (committee “may, in its reasonable discretion” establish and maintain special email address). Compare with *FLYi* Order, ¶ 5, p. 3 (while no special email address or telephone number required to be established, committee “shall respond to written and telephonic inquiries and comments received from creditors”).

<sup>6</sup> See, e.g., *Refco* Order, ¶ 3(a) (also requiring the committee to provide on website, monthly committee reports summarizing recent proceedings and events and calendar of material events, and to distribute case updates via email for creditors who have registered on the website); *FLYi* Order, ¶ 5, p. 3 (website permitted, not directed, by court, which should include information and materials that committee “believes, in its reasonable business judgment, are relevant and informative for creditors that it represents”); *Global Home* Order, p. 2 (website “may” be established by committee); *Pliant* Order, p. 2 (website required which is to include, together with certain required information, any other information that committee and counsel “in their sole discretion” deem appropriate subject to the limitations set forth in the order); *Riverstone* Order, ¶ 3(b), p. 3 (website to be established in committee’s reasonable discretion). As noted by the *Refco* court, “proactive provision of specified types of information on a website ... may not be justified in a smaller case.” *Refco*, 336 B.R. at 198 n. 11.

<sup>7</sup> See, e.g., *Global Home* Order, p. 4 (“the foregoing [exculpation provision] shall not preclude or abridge the right of any creditor to move before the Court for an order requiring the production of other or further information”); *Pliant*

(vi) Often, exculpation is provided for the committee, its members and counsel and agents from liability stemming from actions or omissions with respect to the court-approved procedures and protocols and related matters (with certain exceptions for gross negligence, other breaches of fiduciary duty, and the like).<sup>8</sup>

In general, most courts addressing this matter have wisely come down on the side of caution, allowing committees to effectively limit the scope of the ambiguous information-sharing obligation under Section 1102(b)(3); otherwise, the role and function of committees, the value of debtors' businesses and assets, and the prospects of a successful outcome in Chapter 11 cases could be harmed. In many Chapter 11 cases, it would likely make sense for the creditors' committee to consider at the outset and, if warranted under the circumstances, seek court approval of an information-sharing and solicitation protocol along the lines discussed above, in order to delineate the parameters of the committee's obligations under Section 1102(b)(3), as well as to better manage administrative expenses and logistical issues.

#### D. **Related Issues**

With the foregoing being said about courts delineating the scope and import of Section 1102(b)(3), there are a litany of related issues that may have to be addressed or considered in due course, as necessary, by the courts, as well as committees, debtors and other parties in interest, including the following:

(i) Creditors' Conflicting Agendas: Pursuant to the plain terms of Section 1102(b)(3), any creditor who holds a claim "of the kind represented by that committee" is entitled to access the committee's information. However, in some cases, the creditor seeking the information may have special self-interested, ulterior purposes in mind and providing the applicable information may potentially harm or impact the estate. For example, (a) creditors who are embroiled in disputes or litigation with the debtor-in-possession, trustee or committee, (b) creditors, including claims traders, interested in selling or buying claims and (c) creditors who are business competitors with the debtor may desire to obtain information vis-à-vis Section 1102(b)(3) in order to further their own interests and goals, which in some cases may be inconsistent with the interests and goals of the committee, the estate and its creditors. While courts' general limitation on the dissemination of confidential, privileged or otherwise non-public, sensitive information under Section 1102(b)(3) (as reflected in the comfort orders discussed herein) goes a long way to preventing an improper use of a committee's information, extensive and costly litigation may be initiated by creditors seeking more disclosure under Section 1102(b)(3) for their own agendas.

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Order, p. 3 (same); *Riverstone* Order, ¶ 7, pp. 5-6 (after good faith effort to meet and confer with committee representative, creditor may move for additional disclosure).

<sup>8</sup> See, e.g., *Global Home* Order, p. 4; *Pliant* Order, p. 3; *Riverstone* Order, ¶ 11, pp. 8-9 (exculpation provision also covering debtor). Compare with *FLYi* Order (no exculpation provision).

(ii) Third Party Technological/Administrative Services: Although Section 1102(b)(3) is silent on whether a committee may delegate its obligations thereunder, at least in part, to a third party such as a claims/noticing agent or similar bankruptcy services consulting firm, arguably such delegation (at least as to more ministerial functions) should be viewed as proper and warranted (especially in mega cases), given, *inter alia*, the powers of committees to employ and use professionals and other agents under Section 1103.<sup>9</sup> To reach a large number of creditors in an effective manner, committees' use of special websites, public-accessible databases, mass email notices and other technology will in all likelihood increase in response to the new affirmative obligations under Section 1102(b)(3), in which case consulting and technological services firms will benefit from additional demand and business, with corresponding cost increases for committees (and ultimately for the estates).

(iii) Post-Order Litigation: It is important to note that the orders discussed herein were preemptive comfort orders and evidently not the result of any specific request by a creditor for information or other contested matter or litigation. Further, as discussed above, creditors' rights to seek additional disclosure are not categorically precluded, and thus, creditors may move for the disclosure of specific, confidential information. Case-by-case exceptions may be made to the court-approved procedures and protocols, although fleshed out through possibly lengthy and expensive litigation.

(iv) Scope of Notice: Based on a review of the applicable pleadings and certificates of service, it appears that in many of the cases cited above the comfort orders and related motions were served only on those creditors and parties requesting special notice under Bankruptcy Rule 2002, instead of all known creditors of the debtor.<sup>10</sup> Because the relief provided in such orders is largely as to committee members themselves, an argument could perhaps be made that the underlying motions and (at a minimum) the entered orders should be served on all creditors. Absent such broad service and notice, questions may possibly be raised as to whether such orders are or should be binding on any and all creditors.<sup>11</sup>

(v) Solicitation of Creditor Comments: Many courts dealing with this matter seem to basically wrap the new codified obligation of committees under Section 1102(b)(3) to "solicit and receive comments" from creditors, into

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<sup>9</sup> See, e.g., May 26, 2006 Order entered in *In re Oneida Ltd.*, Case No. 06-10489 (ALG) (Bankr. S.D.N.Y.), pp. 2-3 (committee authorized, without further notice or filing of application, to utilize services of debtors' claims/noticing agent to establish and maintain committee's website).

<sup>10</sup> *But see, e.g., Global Home Order*, p. 4 (order must be served on all creditors).

<sup>11</sup> *Cf. In re Spiegel*, 292 B.R. 748, 751 (Bankr. S.D.N.Y. 2003) ("Generally, this Court allows service on a committee of unsecured creditors, in lieu of service on the unsecured creditors themselves, because a creditors' committee will represent the interests of all class members in reviewing proposed orders and applications. In this case, however, the relief sought is for the Committee members themselves – to be excused from their fiduciary duty [with respect to post-petition securities and claims trading] – and therefore the Application must be served on every member of the affected class.").

committees' information-sharing obligation under that statute. That is, some courts appear to simply require, or allow in their discretion, committees to set up websites and/or distribute notices (mail or electronic) permitting creditors to send in comments to the committee.<sup>12</sup> The question may be raised, depending on the circumstances of the particular case, whether the foregoing is enough by itself (especially if no website is established), or whether more proactive (and costly) solicitation measures should be taken by committees. It should also be noted that, depending on the particular solicitation mechanism implemented, perhaps some classes or subclasses of creditors may be more aggressively solicited, potentially skewing this comment process in favor of that particular class' or subclass' interests.<sup>13</sup> Moreover, certain solicitation measures taken under Section 1102(b)(3) may relate to plan related matters, in which case courts, committees and parties in interest should be mindful of any potential interplay between Section 1102(b)(3) and Section 1125 (with its restrictions on parties soliciting acceptance or rejection of a plan).<sup>14</sup>

These and other issues may have to be looked at and considered by committees and courts alike, and resolved appropriately so as to effectuate the mandate under Section 1102(b)(3) in a reasonable, efficient and effective manner.

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<sup>12</sup> This, of course, is in addition to comments and inquiries typically received by committees and/or their counsel from creditors on an *ad hoc* basis.

<sup>13</sup> It is well-established that a creditors' committee owes a fiduciary duty to its entire creditor constituency and thus, a committee would be in violation of its fiduciary duty if it pursued the interests of a single creditor or group of creditors over those of the entire class. *See generally Woods v. City Nat'l Bank & Trust Co.*, 312 U.S. 262 (1941) (committee member undertakes to act in fiduciary capacity on behalf of members of entire class he or she represents), *reh'g denied by* 312 U.S. 715 (1941); *Pan Am Corp. v. Delta Airlines Inc.*, 175 B.R. 438, 514 (S.D.N.Y. 1994) (creditors' committees have fiduciary duty to entire class of creditors); *In Drexel Burnham Lambert Group*, 138 B.R. 717, 722 (Bankr. S.D.N.Y. 1999) ("The duty [of the committee and its counsel] extends to the class as a whole, not to its individual members."), *aff'd*, 140 B.R. 347 (S.D.N.Y. 1992).

<sup>14</sup> *See, e.g., FLYi Order*, ¶ 5, p. 3 (committee permitted to include on website "documents pertaining to any plan of reorganization in the Debtors' cases").

Appendix

***Proposed Local Bankruptcy Rule 2003-1  
for the Bankruptcy Court for the District of Massachusetts***

- (a) In satisfaction of the requirements of § 1102(b)(3)(A) of the Bankruptcy Code, and subject to subparagraphs (b) and (c) below, the official committee of general unsecured creditors (hereinafter the “Creditors Committee”) shall respond to written, telephonic and/or electronically transmitted inquires received from any general unsecured creditor and provide to such creditor access to documents, pleadings and other materials by any means that the Creditors Committee believes, in its reasonable business judgment, are relevant and informative. Subject to such enlargement of time as the Court may order, no later than twenty (20) days after appointment of its counsel, the Creditors Committee may advise all general unsecured creditors of the preferred means to make any inquires (e.g., by letter, by telephone, by email, through any website) to the Committee.
- (b) The Creditors Committee is not authorized or required, pursuant to § 1102(b)(3)(A) of the Bankruptcy Code, to provide access to any Confidential Information of the Debtor or the Creditors Committee to any creditor. For the purposes hereof, the term “Confidential Information” shall mean any nonpublic information which is the subject of a written confidentiality agreement between the Creditors Committee and the Debtor or another entity or any other nonpublic information, the confidentiality of which in the reasonable business judgment of the Creditors Committee is necessary in order to successfully perform its duties under § 1103(c) and was: 1) otherwise furnished, disclosed, or made known to the Creditors Committee by the Debtor, whether intentionally, unintentionally and in any manner, including in written form, orally, or through any electronic facsimile or computer-related communication or 2) developed by professionals employed by the Creditors Committee and the disclosure of which the Creditors Committee reasonably believes would impair the performance of its duties. Notwithstanding the foregoing, Confidential Information shall not include any information or portion of information that: (i) is or becomes generally available to the public or is or becomes available to the Creditors Committee on a non-confidential basis, in each case to the extent that such information became so available other than by a violation of a contractual legal or fiduciary obligation to the Debtor; or (ii) was in possession of the Creditors Committee prior to its disclosure by the Debtor or the Creditors Committee’s professionals and is not subject to any other duty or obligation to maintain confidentiality.
- (c) The Creditors Committee is not authorized or required, pursuant to § 1102(b)(3)(A) of the Bankruptcy Code, to provide access to any Privileged Information of the Creditors Committee to any creditor. For the purposes hereof, the term “Privileged Information” shall mean any information subject to the attorney-client privilege or any other state, federal, or other privilege, whether such privilege is solely controlled by the Creditors Committee or is a joint privilege with the Debtor or some other party. Notwithstanding the foregoing, the Creditors Committee shall be permitted, but not required, to provide access to Privileged Information to any party so long as: (1) such Privileged Information

is not Confidential Information, and (b) the relevant privilege is held and controlled solely by the Creditors Committee.

- (d) In the event that a creditor is dissatisfied with the failure or refusal of the Creditors Committee to provide requested access or information, the creditor may file a motion seeking to compel the Creditors Committee to produce documents and/or information. The dispute shall be deemed to be a discovery dispute and the parties shall comply with the provisions of MLBR 7037-1, insofar as applicable.

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