

The Banking Law Journal

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Delaware Bankruptcy Court Approves Indenture Trustee Fees in Face of Fee Objection by Certain Noteholders

*Adam F. Jachimowski and Alessandra Glorioso**

In In re Nortel Networks Inc., et al., the bankruptcy court addressed the issue of whether an indenture trustee is entitled to recover, under an indenture and applicable law, additional fees incurred in defending amounts due under the indenture, concluding that the indenture trustee was entitled to recover the fees in question. The authors of this article discuss the decision and the practical result.

The U.S. Bankruptcy Court for the District of Delaware has issued a decision in *In re Nortel Networks Inc., et al.*,¹ that addresses the issue of whether an indenture trustee is entitled to recover, under an indenture and applicable law, additional fees incurred in defending amounts due under the indenture. Considering the indenture and the U.S. Supreme Court's decision in *Baker Botts L.L.P. v. ASARCO LLC*,² the bankruptcy court concluded that the indenture trustee was entitled to recover the fees in question.

BACKGROUND

The proceedings in *Nortel* leading up to the court's decision spanned eight years and involved extensive litigation regarding the allocation of \$7.3 billion dollars in proceeds from sales of the debtors' assets. Two investment funds holding 90 percent of certain outstanding notes issued by the debtors (the "Objecting Noteholders") participated in the negotiation of a Settlement Plan Support Agreement ("SPSA"), which resolved the allocation disputes. The court confirmed a plan drafted in accordance with the SPSA which obligated the debtors to pay up to \$4.25 million in fees and expenses, and preserved the indenture trustee's right to exercise its charging lien with respect to any fees and

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¹ 2017 Bankr. LEXIS 674 (Bankr. D. Del. Mar. 8, 2017).

² 135 S. Ct. 2158 (2015).

expenses in excess of that amount. A charging lien gives the trustee the right to prioritize payment of its fees and expenses over distributions to noteholders from funds held by the trustee other than funds held as principal and interest on debt. Here, the indenture trustee was a member of the official committee of unsecured creditors and had participated in the case both through the committee and independently on behalf of itself and all of the noteholders. For such efforts, the indenture trustee asserted it was owed fees and expenses in the amount of approximately \$8.1 million.

The Objecting Noteholders opposed approximately \$4.4 million of the overall fees and expenses asserted by the indenture trustee and sought, among other things, an order by the bankruptcy court determining the portion of such fees permitted under the indenture. The Objecting Noteholders argued that fees incurred by the indenture trustee:

- (i) as a member of the creditors' committee;
- (ii) for participating in proceedings related to the allocation dispute; and
- (iii) for defending its fees should not be charged to the noteholders.

They contended further that such work did not directly benefit the noteholders and went beyond the scope of the indenture trustee's duties on behalf of the noteholders under the indenture and New York law.

THE BANKRUPTCY COURT'S DECISION

The bankruptcy court reviewed whether the indenture trustee acted prudently in assigning outside counsel to their tasks and whether the work performed by such counsel was reasonable, as required by the indenture. The court reduced the indenture trustee's requested fees by approximately \$914,000 as a result of findings that more than one attorney attended to certain committee work and that one law firm engaged in poor conduct, as well as voluntary reductions by certain law firms. The fees of the indenture trustee and its attorneys were otherwise approved, thereby allowing the indenture trustee to seek payment of the remainder of its \$8.1 million asserted fees and expenses.

Lastly, the bankruptcy court considered whether the indenture trustee's attorneys were entitled fees for their work relating to the fee dispute. The court considered the "American Rule" that requires a litigant to pay its own attorneys' fees, as well as the exception to application by a court of the American Rule where a statute or contract provides otherwise. The bankruptcy court also considered the U.S. Supreme Court's holding in *ASARCO*, which determined that lawyers cannot recover fees incurred defending their fees in a bankruptcy case. In *ASARCO*, the Supreme Court held that the Bankruptcy Code's

provisions regarding the payment of professionals did not amount to a *statutory* exception to the American Rule. As a departure from *ASARCO*, the bankruptcy court in *Nortel* concluded that the indenture provided for a *contractual* exception to application of the American Rule. Specifically, the bankruptcy court found that two provisions in the indenture provided for payment of the fees incurred in connection with the fee dispute. The first was a provision obligating the debtors to indemnify the indenture trustee for “costs and expenses of defending itself.” The second was a provision granting the indenture trustee a lien prior to the notes on money or property held by the trustee, and not held in trust to pay principal and interest on the notes, or a “charging lien,” to secure payment on the debtors’ obligations.³

THE PRACTICAL RESULT

The practical result of the bankruptcy court’s decision is that the indenture trustee could exercise its charging lien to satisfy fees it incurred in the bankruptcy case, including expenses incurred as a result of the fee dispute initiated by the Objecting Noteholders. The court’s ruling allows for the indenture trustee to seek amounts in excess of \$4.25 million for fees and expenses, notwithstanding that the payment of such additional amounts would reduce funds available for distribution to the noteholders.

The court’s holding is a positive one for indenture trustees and their counsel, especially in the wake of *ASARCO*, which has been a source of consternation for bankruptcy professionals since it was decided in June 2015. From a practice perspective, the *Nortel* decision should remind trustees and their counsel of the importance to include specific charging lien and indemnification provisions in any indentures, plans and settlement agreements.

³ As of the date of this publication, the *Nortel* decision has been cited and distinguished for factual grounds by one bankruptcy court decision. See *In re Capitol Litho Printing Corp.*, 2017 Bankr. LEXIS 2209, at *6-7 (Bankr. D. Ariz. July 28, 2017).

