

Working for Free: Supreme Court Holds that Fees Incurred Defending Fee Application are not Recoverable

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The Bankruptcy Code allows bankruptcy trustees, debtors in possession, and official committees to hire attorneys, accountants, and other professionals to assist them in carrying out their statutory duties, with their fees to be paid by the bankruptcy estate. However, to get paid, these professionals must obtain approval from the bankruptcy court. But what happens when someone objects to their fees? Can the professionals recover the fees they incur in defending their fee applications? The Supreme Court says no.

In *Baker Botts v. ASARCO*, the Supreme Court rejected law firms' attempts to recoup the fees spent defending their fee applications against objections by the reorganized debtor. The Court began its analysis by citing the American Rule, which states that each litigant pays his own attorney's fees, win or lose, unless a statute or contract provides otherwise. The applicable statute, section 330(a)(1) of the Bankruptcy Code, allows, after notice and a hearing, a court to award to a professional person "reasonable compensation" only for "actual, necessary services rendered." The Court found that "services" ordinarily refers to "labor performed for another" and the phrase necessarily implies loyal and disinterested service in the interest of a client. Since the law firms were only defending their own fees, they were not providing a service to the estate. "Time spent litigating a fee application against the administrator of a bankruptcy estate cannot be fairly described as 'labor performed for' – let alone 'disinterested service to' – that administrator." Although the Bankruptcy Code explicitly allows fees for preparing a fee application, it does not allow fees for defending one. The Court held that because the statute neither specifically nor explicitly authorizes courts to shift the costs of adversarial litigation from one side to the other, it would not deviate from the American Rule.

It remains to be seen how broadly this decision will be construed. Will it apply to all professionals whose fees must be approved or only to attorneys? Although the American Rule addresses attorneys' fees, the statute governs *all professionals* whose fees are paid by the bankruptcy estate.

If you are a creditor, this decision means that objections to fee applications and time spent defending them will not dilute your ultimate recovery in the bankruptcy. Every dollar spent in fees is a dollar less for the bankruptcy estate and the creditors. However, this may mean that, recognizing the risks of increased objections and diluted fees, professionals may increase their rates.

If you are an attorney or other professional, then you run the risk of incurring tactical objections to your fees. Professionals may begin adding new contract language to retention agreements requiring the clients to cover the costs associated with defending the fee applications. However, whether courts will approve such attempts to contract around *ASARCO* is questionable.