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USA:
The US Supreme Court rejects attorneys' fees in Chapter 11

On 15 June 2015, the US Supreme Court ruled that a law firm could not recover fees it incurred in defending its own fee application.

The ASARCO Case

The case involved the copper company ASARCO LLC that filed for Chapter 11 protection in 2005 to deal with cash flow and environmental issues, among others.

ASARCO retained Baker Botts ("law firm") to represent it in the Chapter 11 case. Among other services, the law firm pursued fraudulent transfer claims against ASARCO's parent, obtaining a judgment for \$7 billion – \$10 billion, arising from the parent's forced sale of another subsidiary.

The judgment facilitated a successful Chapter 11 reorganisation, where creditors were paid in full.

The law firm filed a fee application for \$120 million, and the parent-controlled debtor objected to the fees. The Bankruptcy Court overruled the Debtor's objections and approved the law firm's fee application, as well as \$5 million in fees incurred defending the law firm's fee application.

On appeal, the District Court affirmed the approval of the law firm's fee application. However, the Court reversed approval of the \$5 million of fees for defending the fee application. The US Supreme Court agreed.

Takeaways

The ruling no doubt evokes a visceral satisfaction as fees in Chapter 11 cases have come under fire recently as often disproportionately high compared to the value generated for the estate. However, the facts of the ASARCO case indicate that the value generated for the estate was substantial, apparently a multiple of the fees incurred.

The US Supreme Court's ruling was based on and highlights the "American Rule" regarding legal fees, that litigants shall be responsible for their own legal fees, unless a statute or a contract provision shifts the risk to one party. For example, most states have adopted some form of an unfair and deceptive trade practices statute, which normally provide for the plaintiff to recover attorneys' fees for pursuing such claims from the defendant, as well as damages.

It is also common for commercial contracts (including sales contracts, loan agreements, license agreements, leases, etc.) to contain a provision shifting the responsibility for attorneys' fees to the party who breaches a contract. For example, a commercial sales contract often provides:

"in the event this contract or the obligations of the buyer in the contract must be enforced against the buyer, the seller may recover its reasonable attorneys' fees from the buyer."

State and Federal courts generally enforce such provisions

against a buyer without hesitation.

Shifting responsibility for attorneys' fees can have material impact on litigation and the incentives of the parties involved in litigation. If a buyer in a commercial sales contract knows that it will be liable for not only the obligation owed to the seller for goods or services sold or provided, but also for the seller's attorneys' fees (especially when coupled with a robust default interest), the buyer has incentive to resolve the litigation. Merely asserting defences to delay payment of obligations owed will cost the buyer if it is responsible for the seller's attorneys' fees, not to mention its own attorneys' fees.

In the competitive global business environment, companies are challenged to deliver value to stakeholders. Minimising risks and shifting costs where possible helps this challenge. It is prudent for companies to maximise the business opportunities presented by the "American Rule" by reviewing their contracts to ensure appropriate attorneys' fees provisions are included.



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