No. ____

IN THE

Supreme Court of the United States

CLIFTON CAPITAL GROUP, LLC,

Petitioner,

v.

BRADLEY SHARP,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

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January 29, 2024

QUESTION PRESENTED

Petitioner is one of the largest creditors in the Chapter 11 bankruptcy case of East Coast Foods, Inc., manager of the famed Roscoe's House of Chicken & Waffles restaurant. To date—approaching *six* years after the bankruptcy plan was confirmed—Petitioner has not been paid a penny on its claim. Respondent, the former Chapter 11 trustee, on the other hand, not only received payment for the services he charged the bankruptcy estate, but a substantial unwarranted bonus ordered by the bankruptcy court.

Petitioner challenged the bankruptcy court's order awarding Respondent's bonus. As one of the largest creditors in the bankruptcy case, the plain text of the Bankruptcy Code permits Respondent as a "party in interest" to "raise" and "be heard on any issue" in the Chapter 11 proceeding. 11 U.S.C. § 109. But the court of appeals did not reach the merits of Petitioner's appeal and instead held that Petitioner lacked standing to challenge the bankruptcy court's order awarding Respondent's bonus.

The question presented is:

If a bankruptcy plan proposes to pay creditors in full with interest, does a creditor who alleges that a bankruptcy court order will delay its receipt of funds state an injury in fact sufficient to confer Article III standing to appeal the order?

PARTIES TO THE PROCEEDINGS AND RULE 29.6 STATEMENT

Petitioner Clifton Capital Group, LLC is one of the largest unsecured creditors in the underlying Chapter 11 bankruptcy case of debtor East Coast Foods, Inc., was a party in interest in the bankruptcy court pursuant to 11 U.S.C. § 1109(b), and was the appellant before the district court and court of appeals. Petitioner has no parent corporation and no publicly held corporation owns 10% or more of its stock.

Respondent Bradley Sharp is the former Chapter 11 trustee appointed in the underlying Chapter 11 bankruptcy case pursuant to 11 U.S.C. § 1104 and was a party in interest in that case. Respondent was the appellee before the district court and court of appeals.

STATEMENT OF RELATED PROCEEDINGS

Pursuant to this Court's Rule 14.1(b)(iii), the following proceedings are directly related to this case:

- *Clifton Capital Group, LLC v. Bradley Sharp (In re East Coast Foods, Inc.)*, No. 21-55967 (9th Cir.) (order and amended opinion entered Sept. 14, 2023);

- *Clifton Capital Group, LLC v. Bradley Sharp (In re East Coast Foods, Inc.)*, No. 2:18-cv-10098 (C.D. Cal.) (order entered Aug. 6, 2021);

- *Clifton Capital Group, LLC v. Bradley Sharp (In re East Coast Foods, Inc.)*, No. 2:18-cv-10098 (C.D. Cal.) (order entered Dec. 18, 2019);

- *In re East Coast Foods, Inc.*, No. 2:16-bk-13852 (Bankr. C.D. Cal.) (order and findings of fact and conclusions of law entered).

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In the Supreme Court of the United States

No.

CLIFTON CAPITAL GROUP, LLC,
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On Petition for Writ of Certiorari
To The United States Court of Appeals
for the Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

Petitioner Clifton Capital Group, LLC respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. 1a) is reported at 80 F.4th 901. The initial (App. 38a) and operative (App. 19a) opinions of the district court are not published but are available at 2019 WL 6893015, and 2021 WL 3473926, respectively. The bankruptcy court's final fee order (App. 54a) and subsequent findings of fact and conclusions of law in support of its final fee order (App. 58a) are not published.

JURISDICTION

The court of appeals issued its judgment on May 8, 2023. The court of appeals denied a timely petition for rehearing and amended its judgment on September 14, 2023. On December 17, 2023, this Court extended the deadline to file a petition for a writ of certiorari to January 29, 2024. The petition is timely filed. This Court has jurisdiction under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Pertinent statutory and constitutional provisions are reproduced at App. 137a.

STATEMENT

This case raises a question of exceptional importance regarding constitutional standing and federal jurisdiction. Petitioner is the former chair of the unsecured creditors committee in the underlying Chapter 11 bankruptcy case and holds one of the largest unsecured claims against the estate. It has yet to receive any payment under a bankruptcy plan confirmed more than five years ago.

After the bankruptcy plan was confirmed, the bankruptcy court awarded Respondent a fee enhancement of approximately $400,000 over Petitioner's objection, to be paid ahead of any payment to creditors. Petitioner appealed, arguing the bonus was unwarranted.

Although no one raised the issue of constitutional standing, and the district court twice found that Petitioner meets the more stringent prudential standing test for bankruptcy cases, the Ninth Circuit *sua*

sponte questioned whether Petitioner suffered an Article III "injury in fact" required to challenge the fee award. After receiving supplemental briefing on the issue, the appeals court held that Petitioner is not injured by any delay in payment the bankruptcy court's enhanced fee order might cause because Petitioner should, at some point, be paid in full with interest. The court thus ordered the appeal dismissed for lack of Article III standing. That decision carves out a new and troubling exception to constitutional standing doctrine, and merits review by this Court.

1. In March 2016, East Coast Foods, Inc. ("ECF"), manager of four locations of the storied Roscoe's House of Chicken and Waffles restaurants in Los Angeles, filed for Chapter 11 bankruptcy. The Office of the United States Trustee appointed a committee of unsecured creditors ("the Committee") to monitor ECF's activities. Petitioner Clifton Capital Group, LLC ("Clifton") was named chair of the Committee. The bankruptcy court later ordered the appointment of a Chapter 11 Trustee to manage ECF's affairs and Respondent Bradley Sharp was appointed as the Chapter 11 Trustee ("the Trustee").

In January 2018, the Committee and ECF's principal jointly proposed a Chapter 11 bankruptcy plan ("the Plan"). The bankruptcy court confirmed the Plan, effective September 2018. The following month, the Trustee submitted a final fee application for approval of his fees and costs.

In his application to the bankruptcy court, the Trustee requested $1,155,844.71, the maximum allowable under the fee cap statute, 11 U.S.C. § 326(a). This amount represented the lodestar for hours worked at the Trustee's hourly rate, $758,955.50, plus

an enhancement of approximately 65%.

Clifton objected to the Trustee's request, arguing the fee was not reasonable or supported by the record. The bankruptcy court overruled Clifton's objection and entered an order approving payment to the Trustee of the full, enhanced amount. App. 40a-42a.

2. Clifton appealed the original final fee order to the district court. The Trustee responded on the merits and asserted that Clifton lacked standing to appeal because it should eventually be paid 100% of its $4,165,000 unsecured claim under the Plan, and thus is not a "party aggrieved" by the order. (Being a "party aggrieved" is a judicially-created prudential prerequisite to appeal a bankruptcy court's order, separate and apart from Article III constitutional standing. *See In re P.R.T.C., Inc.*, 177 F.3d 774, 777 (9th Cir. 1999).)

The district court rejected the Trustee's prudential standing argument, holding that Clifton is directly and adversely affected by the final fee order because the Trustee's bonus (paid for with estate funds that would otherwise go to creditors like Clifton) will further subordinate Clifton's claim as a creditor. The district court also agreed with Clifton that the bankruptcy court did not make sufficient findings to support the fee enhancement and remanded for imposition of a lodestar fee award or entry of detailed findings to support an enhanced payout. App. 46a-48a.

3. On remand, the bankruptcy court again awarded the Trustee the maximum compensation allowable under the fee cap statute, this time including findings of fact to support its order. App. 58a. Clifton again appealed the fee order, and the Trustee reiterated its prudential standing argument. The district

court again found that Clifton is a party aggrieved with standing to appeal, but—relying on the newly entered findings—affirmed the bankruptcy court's fee order. App. 25a-35a.

4. Clifton appealed to the Ninth Circuit Court of Appeals, arguing, *inter alia*, that the bankruptcy court erred under controlling precedent by awarding the Trustee nearly $400,000 more than the lodestar amount. In addition to responding on the merits, the Trustee briefly re-raised its claim that Clifton lacks prudential standing because, regardless of the size of the fee award, Clifton eventually purportedly should be paid in full under the bankruptcy plan.

Clifton rejoined that the Trustee's standing argument makes no sense because it would allow improper fee awards to go unchallenged regardless of whether they delay payment to creditors. As Clifton explained, under the Trustee's rationale, had the bankruptcy court awarded $1 million to an individual who had nothing to do with the case, no creditor could object because the Plan proposed payment in full to all creditors at some later date—even though the unwarranted $1 million payment necessarily would delay the creditors' recovery.

At oral argument, the appellate panel *sua sponte* raised the question whether Clifton has Article III standing to appeal the fee award. The court requested supplemental briefing on the standing issue, which the parties filed.

Under established precedent, a party has Article III standing to bring a "case" or "controversy" in federal court if it (1) suffered an "injury in fact" that is (2) fairly traceable to the challenged action and (3) likely

redressable by a favorable decision. *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 560-61 (1992); *see* U.S. Const. art. III, § 2, cl. 1.

In its supplemental brief, Clifton explained that it has Article III standing because it suffered an injury in fact when the bankruptcy court awarded the Trustee a substantial fee enhancement, diminishing the likelihood Clifton will be paid on its claim and negatively impacting the timing of any payment. This injury is traceable to the fee order and redressable by a favorable decision because, if the Trustee is required to refund the nearly $400,000 bonus, there will be funds available in the bankruptcy estate to pay Clifton's claim sooner than if the Trustee is permitted to keep the bonus.

The Trustee, however, took the position that even if the fee order delays the estate's payment to Clifton, Clifton suffered no injury in fact because, eventually, it will be paid. In other words, according to the Trustee, where a bankruptcy plan proposes to pay creditors in full with interest, no creditor can appeal an order that adversely affects the timing of those payments.

5. The Ninth Circuit agreed with the Trustee and affirmed the bankruptcy court's fee order in a published opinion, which the court later amended in response to Clifton's petition for rehearing. *In re East Coast Foods, Inc.*, 80 F.4th 901 (9th Cir. 2023) (as amended). According to the court, Clifton cannot demonstrate Article III standing to challenge the fee order because the Plan provides that all creditors, in-

cluding Clifton, will eventually be paid in full with interest.[1] This promise of full payment forecloses Clifton's claim that it suffered an injury in fact when the bankruptcy court ordered the estate to pay the extra $400,000 to the Trustee. In the Ninth Circuit's view, Clifton is not guaranteed payment within a certain timeframe, and therefore will not be injured by any delay in payment the enhanced fee award might cause. App. 16a-17a.

Because the court held that Clifton cannot establish the injury in fact required for Article III standing, it did not reach the other prongs of the constitutional standing test, the prudential standing question, or the merits. App. 18a.

REASONS FOR GRANTING THE PETITION

This Court has never directly addressed whether a delay in payment is an injury in fact sufficient to confer Article III standing. Before the Ninth Circuit's opinion in this case, lower federal courts generally recognized that it could be. Those decisions partly rest on the accepted principle that a dollar today is worth more than a dollar tomorrow, and that late payment deprives the recipient of the time value of money. This line of reasoning is not particularly controversial, and even the Ninth Circuit adopted it.

But the Ninth Circuit has now carved out a new and troubling exception to this common-sense understanding of injury in fact. According to the appeals court, if a party eventually will be paid with interest

[1] Clifton disputes the Ninth Circuit's factual premise—that it will be paid in full with appropriate interest—but does not rely on that factual disagreement in seeking this Court's review.

on some unspecified future date, then a delay in payment causes no injury at all, and the party has no standing to complain. This holding conflates the related but distinct concepts of injury and damages, and ignores cognizable harms of delayed payment—including the shear inability to use funds to which a party is otherwise entitled. This is particularly important in the context of bankruptcy cases, where creditors are frequently forced to wait years before being paid on their claims, if at all.

As a result, parties in nine states and two territories with justiciable federal claims will be wrongly denied standing to bring them. That is a matter of exceptional importance that merits this Court's review.

A. The Ninth Circuit's decision carves out a new and problematic exception to constitutional standing doctrine

The lower courts are in general agreement that a delay in payment is an injury in fact sufficient to confer standing and invoke federal jurisdiction. *See*, *e.g.*, *MSPA Claims 1, LLC v. Tenet Fla., Inc.*, 918 F.3d 1312, 1318 (11th Cir. 2019) (holding party that received delayed reimbursement suffered Article III injury in fact, specifically, "[t]he inability to have and use money to which a party is entitled"); *Dieffenbach v. Barnes & Noble, Inc.*, 887 F.3d 826, 828-29 (7th Cir. 2018) (holding "[l]osing the use of money for three days" due to delay in receiving refund is injury in fact that confers standing); *Habitat Educ. Ctr. v. U.S. Forest Serv.*, 607 F.3d 453, 457 (7th Cir. 2010) (holding party wrongfully required to post bond suffers injury in fact that confers standing—the "loss of the use of" that money—even if bond will be returned); *Ensminger v. Credit L. Ctr., LLC*, No. 19-CV-02147-

TC-JPO, 2023 WL 6313680, at *4 (D. Kan. Sept. 28, 2023) (holding party charged fee one month early was "deprived . . . of the use of his funds" and thus suffered Article III injury in fact); *Nunez v. Exec. Le Soleil New York LLC*, No. 22 CIV. 4262 (KPF), 2023 WL 3319613, at *2-5 (S.D.N.Y. May 9, 2023) (holding "temporary deprivation of money to which a plaintiff has a right"—here, delayed receipt of wages—"constitutes a sufficient injury in fact to establish Article III standing" (alteration and internal quotation marks omitted)) (collecting similar cases); *cf. In re U.S. Off. of Pers. Mgmt. Data Sec. Breach Litig.*, 928 F.3d 42, 66 (D.C. Cir. 2019) (per curiam) (holding delay in receipt of funds is a tangible injury). *But see Taylor v. Fed. Aviation Admin.*, 351 F. Supp. 3d 97, 102-03 (D.D.C. 2018) (questioning whether premature collection of $5 gives rise to an Article III injury in fact).

These cases rest on the common-sense notion that a party deprived of access to its funds loses the opportunity to use those funds, and on the economic concept of the time value of money, which holds that a dollar today is worth more than a dollar tomorrow. *See Stephens v. U.S. Airways Grp., Inc.*, 644 F.3d 437, 442 (D.C. Cir. 2011) (Kavanaugh, J., concurring in the judgment) ("Money later is not the same as money now."); Catherine Cote, *Time Value of Money (TVM): A Primer*, Harvard Business School Online Business Insights Blog (June 16, 2022), https://online.hbs.edu/blog/post/time-value-of-money (last visited Jan. 26, 2024). They are consistent with this Court's holdings that an employee deprived of pay for 37 days but later recompensed suffers an "injury or harm," *Burlington N. & Santa Fe Ry. Co. v. White*, 548 U.S. 53, 67, 72-73 (2006), and that delay in receipt of attorney's fees "can cause considerable hardship,"

Missouri v. Jenkins by Agyei, 491 U.S. 274, 282-84 & n.6 (1989).

Even the Ninth Circuit recognizes that "the temporary deprivation of money gives rise to an injury in fact for purposes of Article III standing." *Van v. LLR, Inc.*, 962 F.3d 1160, 1161 (9th Cir. 2020) (per curiam). But, the Ninth Circuit now says, this principle only holds if the injured party purportedly will not, at some unspecified later point in time, be paid in full with interest. And so, in the instant case, even assuming the Trustee's bonus delays Clifton's receipt of its $4,165,000, "the Plan's guarantee that Clifton will be paid with interest precludes a finding of injury in fact" and deprives Clifton of standing to appeal. App. 16a.

The Ninth Circuit's exception is wrong for two reasons and establishes a troubling limitation on constitutional standing.

First, the Ninth Circuit conflates the related but distinct concepts of injury and damages. *Cf. TransUnion LLC v. Ramirez*, 594 U.S. 413, 427-28 (2021) (explaining party can have statutory right to damages but lack injury in fact). Interest is one form of damages meant to compensate a party that has been injured by delayed payment. But the anticipated, not-yet-realized prospect of receiving damages does not metaphysically undo the antecedent injury.

Second, interest (damages), while intended to make the injured party whole for the lost time value of funds, does not necessarily compensate for the broader injury of lost opportunity to use funds that may be needed now not later for consumption, emergencies, and the like. This deprivation—the shear inability to use one's own money—is itself a cognizable

injury in fact. *See MSPA Claims 1, LLC*, 918 F.3d at 1318 ("The inability to have and use money to which a party is entitled is a concrete injury."); *cf. Lucas v. S.C. Coastal Council*, 505 U.S. 1003, 1012 n.3 (1992) (holding temporary taking of property is an Article III injury in fact).

The Ninth Circuit has thus created a new and problematic exception to constitutional standing doctrine.

B. The standing question is exceptionally important and squarely presented

As a result of the Ninth Circuit's decision in this case, parties in nine states and two territories with justiciable claims will be tossed out of court, incorrectly, for lack of standing. That is a matter of exceptional importance that merits this Court's review.

This standing question is also important because it is likely to arise repeatedly in the context of bankruptcy cases across the nation. Confirmed Chapter 11 bankruptcy plans, even those that may propose to pay creditors the full amount of their claims, often require creditors to wait long periods of time, years even, before any payment is made. Under the Ninth Circuit's decision, if a plan proposes to pay creditors in full with interest but no payment is to be made for years, creditors have no standing to object.

There are no bars to the Court's consideration of the question presented, which—although not raised by either party in the lower courts—was independently introduced and squarely resolved by the court of appeals. There are no relevant factual disputes, and the standard of review is de novo. *See Jones v. Ford Motor Co.*, 85 F.4th 570, 573 (9th Cir. 2023)

(per curiam).

C. The Decision Below Is Erroneous

Congress conferred a broad participatory right to any party with a stake in a bankruptcy reorganization. Section 1109(b) of the Bankruptcy Code grants any "party in interest," which includes "the debtor, the trustee, a creditors' committee, an equity security holders' committee, [and] a creditor" to appear and be heard on any issue" in a Chapter 11 bankruptcy case. 11 U.S.C. § 1109(b). Some lower courts have held that this statutory standing under the Bankruptcy Code is "effectively coextensive" with Article III standing. *In re Global Industrial Technologies, Inc.*, 645 F.3d 201, 211 (3d Cir. 2011).

There is no dispute that Clifton is a party in interest under 11 U.S.C. § 1109(b). Not even the Trustee has ever argued otherwise.

Clifton is entitled to be paid under the confirmed plan. But that payment only comes after other claimants and creditors are paid, including the Trustee. Clifton is impaired under the bankruptcy plan and did not vote to accept it. *See* 11 U.S.C. §1126. *After* the bankruptcy plan was confirmed, the Trustee filed his fee application in which he requested a substantial and unwarranted fee enhancement bonus. The bankruptcy court ordered that bonus to be paid, and it has been—but more than five years later, Clifton still has not received a penny on its claim. Clifton's lost use of its money is an actual, concrete, and particularized injury. Clifton has Article III standing .

* * * * *

This case presents the question whether a delay in payment to a creditor under a bankruptcy plan constitutes an injury in fact sufficient to confer Article III standing on the creditor. That question is of extraordinary constitutional and practical importance. This case is an ideal vehicle for the Court's review. The Court should therefore grant the petition for certiorari and, on the merits, hold that Petitioner has Article III standing.

CONCLUSION

The petition for a writ of certiorari should be granted.

January 29, 2024

Respectfully submitted,

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APPENDIX

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Appendix E

Appendix A

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

NO. 21-55967

IN THE MATTER OF: EAST COAST FOODS, INC.,
Debtor

CLIFTON CAPITAL GROUP, LLC,
Appellant,

V.

BRADLEY D. SHARP, FORMER CHAPTER 11 TRUSTEE,
Appellee

Filed: September 14, 2023

Before: SMITH, JR. AND NELSON, CIRCUIT JUDGES, AND DRAIN,* DISTRICT JUDGE

*The Honorable Gershwin A. Drain, United States District Judge for the Eastern District of Michigan, sitting by designation.

ORDER

The opinion filed on May 8, 2023, and appearing at 66 F.4th 1214, is amended as follows: On slip opinion page 4, lines 7–8, delete <Plan's assets contained within the Plan Collateral Package> and replace with <Collateral Package>.

On page 13, line 6, delete footnote 9.

On page 13, line 8, replace footnote 10 with <The disclosure statement requires that the plan include a classification of claims and how each class of claims will be treated under the plan. *See* 11 U.S.C. § 1123. Creditors whose claims are "impaired" generally vote on the plan before it is approved by the bankruptcy court. *See id.* at § 1126. Here, however, Clifton waived that right in a stipulation approved by the bankruptcy court and the plan was subsequently approved pursuant to § 1128.>.

On page 14, line 10, delete <Plan's assets contained within the Plan> and replace with <Package>.

On page 16, line 6, delete <Given Clifton's consent to the Plan, and b> and replaced with <B>.

With these amendments, Judges M. Smith and R. Nelson vote to deny the petition for rehearing en banc, and Judge Drain so recommends. The full court was advised of the petition for rehearing en banc, and no judge of the court has requested a vote on whether to rehear the matter en banc. The Petitions for Rehearing and Rehearing En Banc are DENIED. No further

petitions for rehearing will be accepted.

AMENDED OPINION

R. NELSON, Circuit Judge:

Creditor Clifton Capital Group, LLC challenges the district court's order affirming the bankruptcy court's enhanced fee award of over $1 million dollars to the trustee in a funded bankruptcy. Because Clifton has failed to show that the enhanced fee award will diminish its payment under the bankruptcy plan, Clifton lacks standing. We thus reverse the district court's order finding standing and remand with instructions to dismiss the appeal for lack of Article III standing.

I

This is not a normal bankruptcy. Roscoe's House of Chicken & Waffles is a landmark Los Angeles restaurant chain. Building on a staple menu predating the American Revolution—Thomas Jefferson served his guests chicken and waffles—Roscoe's has garnered celebrity attention since opening in 1975. President Obama enjoyed chicken wings and a waffle there in 2011, with "Obama's Special" added to the menu.[1] Several movies have referenced Roscoe's.[2] And

[1] Adrian Miller, The Layered Legacy of Roscoe's House of Chicken & Waffles, RESY Blog (Sept. 8, 2020) https://blog.resy.com/2020/09/thelayered-legacy-of-roscoes-house-of-chicken-waffles/.

[2] *See id.* ("The restaurant has gotten a mention in films including: Tapehead (1988), Swingers (1996), Jackie Brown (1997), Rush Hour (1998), Soul Plane (2004). In 2004, Roscoe's got more

numerous songs have memorialized the restaurant, including one by Ludacris who suggests that the listener "roll to Roscoe's and grab somethin' to eat."[3] Despite its cultural ubiquity, even Roscoe's was not immune to a $3.2 million judgment in a racial discrimination case.[4] This significant judgment, along with other debt, threatened to impair Roscoe's ability to pay its creditors.

But fear not. The public can still indulge in Roscoe's famous soul food. As part of the bankruptcy plan, the restaurants remain open and founder Herb Hudson has guaranteed payment to Roscoe's creditors. As a failsafe, Snoop Dogg suggested buying the chain to keep it in business.[5]

In 2016, East Coast Foods, Inc. (ECF), manager of the four Roscoe's locations, filed for Chapter 11 bankruptcy. The Office of United States Trustee appointed an official committee of unsecured creditors (Committee) to monitor ECF's activities, of which Clif-

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than a mention on the big screen: It got its own eponymous feature-length film.").

[3] LUDACRIS, CALL UP THE HOMIES (Def Jam Recordings 2008).

[4] *See Beasley v. East Coast Foods, Inc. et. al.*, No. BC509995 (L.A. Sup. Ct.); *see also* Shan Li, *Parent Company of Roscoe's House of Chicken and Waffles Files for Bankruptcy Protection*, LA Times (Mar. 29, 2016) https://www.latimes.com/business/la-fi-roscoes-chicken-wafflesbankruptcy-20160329-story.html.

[5] Farley Elliott, *Snoop Dogg Says He'll Save Roscoe's Chicken N' Waffles if it Comes to That*, LA Eater (Mar. 31, 2016) https://la.eater.com/2016/3/31/11338382/snoop-dogg-buy-roscoeschicken-waffles.

ton Capital Group, LLC (Clifton) was named chair. After an examiner found that ECF could not meet its fiduciary obligations, the court appointed Sharp as trustee, the de facto head of ECF for two years.

The Committee and ECF's principal submitted a Chapter 11 bankruptcy plan (the Plan), effective September 2018. The Plan granted $450 per hour plus expenses for Sharp's services as trustee.

The Plan guaranteed the creditors full payment with interest secured by a "Collateral Package," which included all of the ECF's assets, and up to a $10 million contribution from Hudson. The Plan's appraiser estimated the value of the Collateral Package at over $39.2 million with $23.4 million of net equity, far exceeding the claims to be paid under the Plan.

In his final fee application filed in October 2018, Sharp requested $1,155,844.71, the maximum allowable under the fee cap statute, 11 U.S.C. § 326(a). This amount represented the lodestar (1,692.2 hours worked times an hourly rate of $448.50, for $758,955.50) plus a 65% enhancement for exceptional services.

Clifton objected in the bankruptcy court, arguing the fee cap was not presumptively reasonable as the record did not support an enhancement beyond the lodestar. The court disagreed, holding that the fee cap was presumptively reasonable and, in the alternative, that the case was exceptional and merited deviation from the lodestar.

Clifton then appealed to the district court and moved to strike the Fee Order. Sharp countered that Clifton lacked standing to appeal because it was not a

"party aggrieved." The district court found Clifton aggrieved because there was insufficient capital in the estate to pay all creditors. *In re E. Coast Foods, Inc.*, No. CV 18-10098, 2019 WL 6893015, at *3 (C.D. Cal. Dec. 18, 2019). It held that "[b]ecause the increased compensation to the Trustee will further subordinate Clifton Capital's claim, the Court concludes that Clifton Capital is directly and adversely affected by the Final Fee Order." *Id.* The district court further held that the lodestar was the starting point for reasonable compensation and vacated and remanded for the bankruptcy court to award fees equal to the lodestar or "make detailed findings sufficient to justify a higher amount." *Id.* at *4, 6.

On remand, the bankruptcy court again found that Sharp was "entitled to an enhancement because the results in this case were truly exceptional." The bankruptcy court again awarded the statutory maximum. Clifton again appealed and the district court this time affirmed. Clifton now appeals to this court.

II

The question of whether a party has standing is a threshold issue that must be addressed before turning to the merits of a case. *Horne v. Flores*, 557 U.S. 433, 445 (2009). To appeal a bankruptcy court's order, a party must establish Article III standing and that it is "aggrieved" by the order. *In re Fondiller*, 707 F.2d 441, 443 (9th Cir. 1983).

We review Article III standing determinations de novo. *Tailford v. Experian Info. Sols., Inc.*, 26 F.4th 1092, 1098 (9th Cir. 2022). But we review the factual determination that Clifton was a person aggrieved for

clear error. *In re Point Ctr. Fin., Inc.*, 890 F.3d 1188, 1191 (9th Cir. 2018).

III

A

Our authority under Article III is dispositive. Because the Constitution limits our jurisdiction to "cases" and "controversies," standing is an "essential and unchanging" requirement. *In re Sisk*, 962 F.3d 1133, 1141 (9th Cir. 2020) (quoting U.S. Const. art. III, § 2, cl. 1; *Lujan v. Defs. of Wildlife*, 504 U.S. 555, 560, 112 S.Ct. 2130, 119 L.Ed.2d 351 (1992)). Accordingly, a party must establish an Article III case or controversy before we exert subject matter jurisdiction. *Cetacean Cmty. v. Bush*, 386 F.3d 1169, 1174 (9th Cir. 2004) ("A suit brought by a plaintiff without Article III standing is not a 'case or controversy,' and an Article III federal court therefore lacks subject matter jurisdiction." (citation omitted)).

In the bankruptcy context, we have historically bypassed the Article III inquiry, instead analyzing whether a party is a "person aggrieved." *See Fondiller*, 707 F.2d at 443. This standard is a prudential requirement initially found within the Bankruptcy Act of 1898, which permitted appeal by any "person aggrieved by an order of a referee." 11 U.S.C. § 67(c) (1976) (repealed 1978). The "person aggrieved" standard was designed to limit appeals in bankruptcy proceedings because such cases invariably implicate the interests of various stakeholders, including those not formally parties to the litigation. *See Fondiller*, 707 F.2d at 443. Even after Congress repealed and re-

placed the Bankruptcy Act of 1898, however, we continued to apply the "person aggrieved" standard.[6] *See id.*; *In re Com. W. Fin. Corp.*, 761 F.2d 1329, 1334 (9th Cir. 1985).

It is unclear why we continued to apply the person aggrieved rule in the absence of the statute providing the basis for doing so. We appear to have recast the pre-1978 statutory standard and applied it as a principle of prudential standing. But the Supreme Court has since questioned prudential standing, noting it "is in some tension with [the Court's] recent reaffirmation of the principle that 'a federal court's obligation to hear and decide' cases within its jurisdiction 'is virtually unflagging.' " *Susan B. Anthony List v. Driehaus*, 573 U.S. 149, 167, 134 S.Ct. 2334, 189 L.Ed.2d 246 (2014) (quoting *Lexmark Int'l, Inc. v. Static Control Components, Inc.*, 572 U.S. 118, 125–26, 134 S.Ct. 1377, 188 L.Ed.2d 392 (2014)). Still, our bankruptcy cases have historically addressed prudential standing with little attention to Article III standing. *See, e.g., Fondiller*, 707 F.2d at 441–43; *In re Int'l Env't Dynamics, Inc.*, 718 F.2d 322, 326 (9th Cir. 1983); *Klein v. Rancho Mont. De Oro, Inc.*, 263 F.2d 764, 772 (9th Cir. 1959); *Com. W. Fin.*, 761 F.2d at 1334.

After the Supreme Court's decision in *Driehaus*, however, we have returned emphasis to Article III standing. *See, e.g., Sisk*, 962 F.3d at 1141–43.

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[6] The Bankruptcy Reform Act of 1978 replaced the Bankruptcy Act of 1898. It governs the relationship between creditors and debtors when debtors can no longer pay their debts. Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C. § 101).

And determining our Article III jurisdiction before any prudential considerations does not offend our precedent. *See, e.g., In re P.R.T.C., Inc.*, 177 F.3d 774, 777–79 (9th Cir. 1999) (addressing Article III standing before person aggrieved prudential standing). We thus first examine Article III standing, which we find lacking here.

B

As the party invoking federal jurisdiction, Clifton "bears the burden of establishing" the elements of Article III standing. *Lujan*, 504 U.S. at 561, 112 S.Ct. 2130. A party must establish "such a personal stake in the outcome of the controversy as to warrant *his* invocation of federal-court jurisdiction." *Horne*, 557 U.S. at 445, 129 S.Ct. 2579 (quoting *Summers v. Earth Island Inst.*, 555 U.S. 488, 493, 129 S.Ct. 1142, 173 L.Ed.2d 1 (2009) (emphasis in original)). Clifton must therefore show that it has: (1) suffered an "injury in fact" that is concrete, particularized, and actual or imminent, (2) the injury is "fairly traceable" to the defendant's conduct, and (3) the injury can be "redressed by a favorable decision." *Lujan*, 504 U.S. at 560–61, 112 S.Ct. 2130 (alterations in original omitted).

1

Injury in fact is the "[f]irst and foremost" of the three standing elements. *Sisk*, 962 F.3d at 1142 (quoting *Steel Co. v. Citizens for a Better Env't*, 523 U.S. 83, 103, 118 S.Ct. 1003, 140 L.Ed.2d 210 (1998)). Clifton argues that it suffered an injury-in-fact because the Plan established the expectation that it would receive

full payment of its claim, which has not yet occurred and which the Fee Order exacerbates. The Plan estimates that Clifton would "receive a *pro rata* share of Available Cash[7] in the annual sum of $1,816,701 in 2022, $2,996,321 in 2023, and $634,634 in 2024 ... " To date, Clifton notes that this totals millions of dollars in payments that have not been made. Clifton argues that the Fee Order's grant of the $400,000 trustee bonus harms both the likelihood and timing of any payment by further subordinating it.

This, Clifton contends, suffices as an injury 'fairly traceable' to the wrongful conduct of the excessive fee award because its "injury need not be financial," *P.R.T.C.,* 177 F.3d at 777 (citation omitted), and because, under 11 U.S.C. § 330, payment of the fee award has priority and must be paid in full before unsecured creditors like Clifton receive any distribution. Clifton thus argues that it suffered a traceable and redressable injury in fact because a favorable decision would result in the excessive fees being returned to the ECF estate to pay out claims, and therefore would "increase the likelihood and timing" of payment to Clifton.

Sharp counters that Clifton's alleged injury is too conjectural and hypothetical to establish an injury

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[7] "Available Cash" is defined as cash in the estate from various sources, less (among other things) "the amount necessary or estimated and reserved to pay in full [] any Allowed Administrative Expense Claims," which includes the Trustee's awarded compensation pursuant to the Fee Order. *See* 11 U.S.C. § 503(b)(2) (providing that an administrative expense claim includes "compensation and reimbursement awarded under [11 U.S.C. § 330(a)].").

in fact because there is no diminished likelihood that Clifton will be paid in full. The Plan's Collateral Package[8] guarantees Clifton full payment with interest. Sharp further argues that Clifton cannot claim injury arising from the Plan's estimates because Clifton approved the Plan understanding that the timing of its distributions depended on the allowed amounts of senior claims, meaning payment could be delayed by any increase in any Allowed Non-Subordinated Claims. Thus, Sharp asserts that Clifton's alleged harm is no harm at all because Clifton's payment is certain, and the only question at issue is when payment will occur.

2

We conclude that Clifton's alleged injury is too conjectural and hypothetical to establish an injury in fact for Article III standing. We similarly conclude that Clifton is wrong that the fee award both impaired the likelihood and delayed the timing of its payment. The district court erroneously concluded that the fee award would further subordinate Clifton's claim.

a

We first address the likelihood of payment. The district court concluded that Clifton had standing because it was an aggrieved party. Noting that Clifton had not been paid on any of its Allowed Claim, the court adopted Clifton's argument that "[t]here are not

[8] As discussed below, the Collateral Package protects against any risks of nonpayment and includes all of the Reorganized Debtor's assets.

yet enough funds on hand to pay all creditors, including Clifton Capital, in full" and that "there are outstanding contingencies under the Plan that must occur before those funds become available." *E. Coast Foods*, 2019 WL 6893015, at *3. Sharp pointed out, however, that because Clifton was guaranteed 100% payment of its alleged claim under the Plan, it was not aggrieved. *Id.* at *2–3.

The district court seemingly concluded, without explicitly stating, that the Plan concerns a limited fund. *See id.* at *3. It found that the alleged lack of sufficient capital to pay all claims would further subvert Clifton's claim and thereby adversely affect its payment. *Id.* Therefore, the district court held that Clifton was aggrieved because it was appealing an order disposing of assets from which it (the claimant) seeks to be paid. *Id.* (citing *Int'l Env't Dynamics*, 718 F.2d at 326).

The district court relied on our precedent that in cases involving competing claims to a limited fund, "a claimant has standing to appeal an order disposing of assets from which the claimant seeks to be paid." *Id.* (quoting *P.R.T.C.*, 177 F.3d at 778). A limited fund necessarily concerns a finite pool of assets to pay claims, thus creating the risk that creditors will not be paid, either in full or at all. In the limited fund context, changes to any allotment or transfer of funds, including an enhanced fee award, would materially affect the likelihood of any potential payment and therefore directly implicate creditor interests. Along these lines, we have found a party aggrieved when limited fund plans "eliminated" a party's interest in estate assets from which they sought payment. *Com. W. Fin.*,

761 F.2d at 1335. We have also found standing when a bankruptcy court's order transferred all significant assets out of the estate, effectively barring a creditor's claim. *P.R.T.C.*, 177 F.3d at 778–79.

In contrast, in *Klein*, we found that plaintiffs challenging an order seeking payment of their attorney fees lacked standing because the plan specified that there were "additional monies" available, even though the plan did not expressly contemplate payment of their claims. 263 F.2d at 771–72. The plaintiffs challenged orders confirming a plan which they asserted disregarded compensation for legal services to which they were entitled. *See id.* Plaintiffs argued that because the plan disposed of the estate's assets, the plan rendered payment impossible. *Id.*

Our court rejected both arguments. Even though the plan did not expressly contemplate the plaintiffs' compensation claims, the plan provided that "additional monies are available if need(ed) ... to ... pay off the unsecured creditors their claims in full." *Id.* at 772 (alterations in original). At judgment, the court noted that "if the sum which is actually available to pay appellants' claims as finally allowed proves insufficient, the court has only to enforce the provisions of the plan ... requiring that additional monies be deposited or accrued in the registry." *Id.*

Even though *Klein* was decided under the "person aggrieved" standard, it is most analogous to this case. As in *Klein*, the Plan here does not relate to a limited fund because there is no finite amount of assets from which all creditors could be paid. *See id.* Rather, "the Plan is a reorganizing plan that **proposes to pay all Allowed Claims in full** (unless otherwise

agreed) from the Debtor's ongoing operations and non-Estate sources."

The Plan's mandatory "disclosure statement" which outlines the Plan, its risk factors, and its financial projections bolsters this conclusion.[9] *See* 11 U.S.C. §§ 1121, 1125. The Plan makes clear that Clifton's claim will be paid in full with interest after all other allowed unsecured claims and penalty claims are satisfied. Clifton understood these terms: its principal Sam White testified that "the Plan was proposed to move this case forward and to ensure 100% payment to creditors as quickly as possible."

Indeed, the Plan's promise of full payment with interest is unconditionally guaranteed and secured by a "Collateral Package," which includes all of ECF's assets. The Debtor's principal (Hudson) is responsible for contributing up to $10 million to the Plan to affect the payment of claims. ECF is required to contribute to the Plan roughly $110,000 per month plus the excess free cash flow from its post-confirmation operations. Additional funds are available from other entities owned by Hudson which are to contribute about $130,000 per month to the Plan. Payments from ECF and Hudson will continue until all claims are paid in full with interest.

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[9] The disclosure statement requires that the plan include a classification of claims and how each class of claims will be treated under the plan. See 11 U.S.C. § 1123. Creditors whose claims are "impaired" generally vote on the plan before it is approved by the bankruptcy court. See id. at § 1126. Here, however, Clifton waived that right in a stipulation approved by the bankruptcy court and the plan was subsequently approved pursuant to § 1128.

The Package further ensures enough available collateral to pay the Plan's covered claims in full, plus a 35% equity cushion. The Plan's appraiser estimated the value of the Package at over $39.2 million with 23.4 million of net equity, exceeding the claims to be paid under the Plan by about $17.3 million (the 35% equity cushion).

Given the detailed Plan which guarantees payment to creditors plus interest, and the net equity in the Plan, the district court's finding that the estate is a limited fund and that "there are not sufficient funds to pay back all the creditors," is clearly erroneous. *E. Coast Foods*, 2019 WL 6893015, at *3. Moreover, even if Sharp receives the contested $400,000 bonus, this will not impact Clifton's ability to be paid because there are other sources from which to make Clifton's payment at the appropriate time.

b

We similarly disagree with Clifton's assertion that it suffered injury to the timing of its payment. In agreeing to the Plan, Clifton knew from the start that the timing of its payment could be longer or shorter than the Plan's initial estimates depending on the amounts owed to senior claimants. The Disclosure estimates that all Allowed Unsubordinated Claims would be paid in full within four years, by mid-2022. But the Statement also notes that "[t]he term of the Plan can be shorter or longer than expected depending on the amount of the Allowed Claims."

The Plan further estimates that allowed claims could be paid within six years, but "for every $1 million change in allowed claims, the term of the Plan

will change by 3.3 months." Sharp points to specific unresolved allowed claims that have delayed payment, such as a pending priority claim by the IRS for over $10.2 million which it asserts Clifton knew was present at the time the Plan was approved, and for which $15 million is being held in reserve to pay. Sharp also points to the effects of COVID-19 and a missing $1.5 million payment from Hudson as reasons that Clifton has not been paid yet. Sharp has entered into a series of forbearance agreements to give Hudson additional time to pay the balance due. No evidence suggests that payment will not occur. And in any event, this potential default is not traceable to the Fee Order itself.

Given these uncertainties, the Plan estimated that the distribution timeframe for subordinated claims, such as Clifton's, would be between 2022 and 2024. But these were only estimates. Ultimately, the Plan's guarantee that Clifton will be paid with interest precludes a finding of an injury in fact now even though these estimates thus far have proven inaccurate.

Clifton's alleged harms are thus conjectural at best. It remains possible that Clifton will be paid within the Plan's initial estimated window before the end of 2024. Because this period has not passed, Clifton has failed to establish that the timing of its payment has been harmed beyond what the Plan initially provided. Since the Plan did not guarantee Clifton payment by a specific date (it merely provided an estimated window which has not passed), and the estimated timing of payment was subject to change based

on priority claims, Clifton has not yet shown an actual injury. That is particularly true where Clifton is entitled to interest on the payments that are due. As such, Clifton has failed to establish the negative impact of any delayed payment not already addressed by the Plan.

This remains the case even where Sharp receives his payment before Clifton is paid. The Plan anticipates fulfilling Clifton's claims even if Sharp receives the challenged bonus. As we held in *Klein*, the availability of additional funds to satisfy plaintiffs' claims foreclose standing. 263 F.2d at 771. The same is true here.

This is not to say that no potential remedy would exist should the Plan prove insufficient. We agree with our prior analysis in *Klein* that Clifton, if necessary, could sue to enforce those provisions of the Plan. At that time, there may be an actual injury that is both fairly traceable and would be easily redressable by ordering additional money deposited into the estate to pay Clifton's claims. *See id.* at 766. But such facts do not presently exist. And standing must exist from the start of an action. *See, e.g., Friends of the Earth, Inc. v. Laidlaw Env't Servs. (TOC), Inc.*, 528 U.S. 167, 170, 120 S.Ct. 693, 145 L.Ed.2d 610 (2000) ("The requisite personal interest that must exist at the commencement of the litigation (standing) must continue throughout its existence...."). As such, Clifton has failed to establish actual injury thus far and therefore lacks Article III standing to challenge the

Fee Award.[10]

IV

Because Clifton currently lacks an injury in fact, we reverse the district court's order and remand with instructions to dismiss the appeal for lack of Article III standing.

REVERSED.

[10] Because Clifton lacks Article III standing, we need not address the prudential "person aggrieved" standard. See Gov't Emps. Ins. Co. v. Dizol, 133 F.3d 1220, 1222–23 (9th Cir. 1998) (holding that a suit seeking declaratory judgment must first pass constitutional and statutory muster as presenting a case-or-controversy before the court exercises its prudential discretion).

APPENDIX B

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

NO. CV 20-10982 MWF

IN RE EAST COAST FOODS, INC.,
Debtor

Filed: August 6, 2021

ORDER RE: CONSOLIDATED APPEAL FROM THE UNITED STATES BANKRUPTCY COURT'S ORDERS

MICHAEL W. FITZGERALD, United States District Judge:

Before the Court is an appeal from the United States Bankruptcy Court (the Honorable Sheri L. Bluebond, United States Bankruptcy Judge). Appellant Clifton Capital Group, LLC ("Clifton Capital") appeals two orders of the Bankruptcy Court: (1) the Order Granting the Application for Payment of Final Fees and/or Expenses (the "Second Fee Order") in the amount of $1,155,944.71; and (2) the Order Granting Motion to Strike Declarations of John L. Sadd, Jed

Sanford, and Sam White Filed by Clifton Capital Group, LLC ("Clifton Capital"), in Opposition to Trustee's Final Fee Application (the "Strike Order") (collectively, the "Orders"). The Bankruptcy Court entered the Orders in connection with its granting of the Fourth and Final Application for Compensation and Reimbursement of Fees and Expenses (the "Final Fee Application"), filed by Bradley D. Sharp, the former chapter 11 trustee (the "Trustee") in the bankruptcy case of East Coast Foods, Inc. ("ECF").

Appellant Clifton Capital submitted its Opening Brief ("OB") on February 2, 2021. (Docket No. 15). On May 14, 2021, Appellee Bradley D. Sharp, Chapter 11 Trustee, submitted his Reply Brief ("AB"). (Docket No. 16). On June 11, 2021, Clifton Capital submitted its Reply Brief ("RB"). (Docket No. 23). The Court has read and considered the papers filed in this appeal and held a Zoom video hearing on July 7, 2021.

For the reasons discussed below, the Court rules as follows:

- The Second Fee Order is **AFFIRMED**. The Bankruptcy Court neither erred nor abused its discretion in awarding the Trustee a fee enhancement above the lodestar figure.
- The Strike Order is **AFFIRMED**. The Bankruptcy Court neither erred nor abused its discretion in granting the Trustee's motion to strike Clifton Capital's declarations submitted in connection with its supplemental brief on remand because the Trustee did not introduce any new evidence in his supplemental brief.

I. BACKGROUND

On November 18, 2018, the Bankruptcy Court

granted the Trustee's Final Fee Application (the "First Fee Order"), on the basis that the requested fee was reasonable because it equaled the amount set forth under 11 U.S.C. § 326(a), or alternatively, because "this was an exceptional case" warranting compensation in excess of the lodestar figure. *See In re East Coast Foods, Inc.*, CV 18-0098 MWF, 2019 WL 6893015 at *4 (C.D. Cal. Dec. 18, 2019).

On December 19, 2019, the Court entered the Order Re the Bankruptcy Court's Order (the "Prior Order"), reversing and remanding the Bankruptcy Court's order on the basis that Bankruptcy Court did not make detailed findings as to why the Trustee is entitled to an amount significantly higher than the lodestar figure. (*Id.*).

In so doing, the Court held as follows: (1) the lodestar approach is "presumptively reasonable" for purposes of determining the Trustee's compensation under 11 U.S.C. § 330; (2) the Trustee must "come forward with specific evidence showing why the results obtained were not reflected in either his standard hourly rate or the number of hours allowed" and "must also show that the bonus is necessary to make the award commensurate with compensation for comparable nonbankruptcy services"; and (3) if the Bankruptcy Court determines that a bonus is justified, it must make detailed findings that actually support that determination. (*Id.*) (citing *In re Manoa Finance Co., Inc.*, 853 F.2d 687, 692 (9th Cir. 1988)). The Court also noted that "while the Bankruptcy Court observed that the Trustee faced various challenges in this action, it is not clear why such considerations would not have been encompassed in the lodestar figure, or would justify such a substantial bonus." (*Id.* at *4).

On remand, the parties provided supplemental briefing in light of this Court's ruling, and the Bankruptcy Court held a continued hearing on the Trustee's Final Fee Application (the "Fee Application"). At that hearing, the Bankruptcy Court stated:

> It's difficult for a lower court on remand to adjudicate an issue when it firmly believes the appellate court made an error of law on appeal. This court remains of the view that Congress intended for the compensation formula set forth in Section 326(a) to be presumptively reasonable and generally in the nature of a commission ... and that the citations offered by the District Court are not on point.

(Excerpts of Record ("ER") 7-8) (Docket No. 16)). The Bankruptcy Court nonetheless acknowledged that this Court's prior decision was "law of the case" and that the Bankruptcy Court "need[s] to follow it, but it kind of makes it a little bit — you know, I have to do it with a couple of brain cells tied behind my back. It makes [it] a little more challenging." (ER 8-9).

The Bankruptcy Court ultimately determined on remand that the lodestar amount in this case is $758,951.70 (the "Lodestar"). (ER 10-12, 30-31). The Bankruptcy Court then awarded the Trustee compensation with the same fee enhancement as before, in the total amount of $1,155,844.71. (ER 17-18, 42-44). The Bankruptcy Court also entered findings of fact and conclusions of law in support of the Second Fee Order. (ER 45-100). Finally, the Bankruptcy Court entered the Strike Order, striking certain declarations submitted by Clifton Capital. (ER 101-102).

The Court incorporates by reference the factual and procedural background set forth in the Prior Order as if fully set forth herein. (*See* Prior Order at 2-4).

II. STANDARD OF REVIEW

A bankruptcy court's conclusions of law are reviewed de novo, and findings of fact are reviewed for clear error. *Zurich Am. Ins. Co. v. Int'l Fibercom, Inc.*, 503 F.3d 933, 940 (9th Cir. 2007). Pertinent to this appeal, a bankruptcy court's award of professional fees "will not [be] disturb[ed] ... unless the bankruptcy court abused its discretion or erroneously applied the law." *In re Strand*, 375 F.3d 854, 857 (9th Cir. 2004). "A bankruptcy court abuses its discretion if it applies the wrong legal standard or its findings are illogical, implausible or without support in the record." *In re Cook Inlet Energy LLC*, 583 B.R. 494, 500 (B.A.P. 9th Cir. 2018).

III. LEGAL STANDARD

Pursuant to § 330, a bankruptcy court "may award to a trustee, ... or a professional person employed under section 327 or 1103 (A) reasonable compensation for actual, necessary services rendered by the trustee ...; and (B) reimbursement for actual, necessary expenses." 11 U.S.C. § 330(a)(1)-(2).

In determining reasonable compensation for a chapter 11 trustee, courts shall consider

> the nature, the extent, and the value of such services, taking into account all relevant factors, including — (A) the time spent on such services; (B) the rates charged for such services; (C) whether the services were necessary to the administration of, or beneficial at

> the time at which the service was rendered toward the completion of, a case under this title; (D) whether the services were performed within a reasonable amount of time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed; (E) with respect to a professional person, whether the person is board certified or otherwise has demonstrated skill and experience in the bankruptcy field; and (F) whether the compensation is reasonable based on the customary compensation charged by comparably skilled practitioners in cases other than cases under this title.

Id. § 330(a)(3). Section 326(a) sets a statutory cap for chapter 11 trustee compensation depending on the amount disbursed to creditors. *Id.* § 326(a).

A trustee has the burden of demonstrating that its requested compensation is reasonable and satisfies these requirements. *See Hale v. United States Trustee* (*In re Basham*), 208 B.R. 926, 931-32 (B.A.P. 9th Cir. 1997).

The primary method used to determine a reasonable fee under § 330(a)(3) is to calculate the lodestar. *See In re Buckridge*, 367 B.R. 191, 201 (Bankr. C.D. Cal. 2007) (citing *In re Eliapo*, 468 F.3d 592, 598 (9th Cir. 2006); *Yermakov v. Fitzsimmons* (*In re Yermakov*), 718 F.2d 1465, 1471 (9th Cir. 1983)). The lodestar is computed by multiplying the number of hours reasonably expended by a reasonable hourly rate. *See Hensley v. Eckerhart*, 461 U.S. 424, 433, 103 S. Ct. 1933, 1939, 76 L. Ed. 2d 40 (1983).

IV. DISCUSSION

A. Standing

As a preliminary matter, the Court rejects the Trustee's argument that Clifton Capital lacks standing to bring this appeal. (*See* AB at 43). In the Prior Order, faced with the exact same evidence and argument, the Court concluded that Clifton Capital had standing to bring this appeal because the record indicated that the estate did not have sufficient capital to pay all creditors:

> Although neither party provides case law directly on point on the issue, the Court finds Clifton Capital's argument to be more persuasive. Clifton Capital's claim is "subordinated to ... all allowed and secured and unsecured claims and approved administrative expenses." (SER 46; AB at 15-16). This is important because to date**, *there is not sufficient capital to pay all creditors.*** Because the increased compensation to the Trustee will further subordinate Clifton Capital's claim, the Court concludes that Clifton Capital is directly and adversely affected by the Final Fee Order, giving it standing to pursue this appeal. *See Salomon v. Logan (In re International Envtl. Dynamics, Inc.)*, 718 F.2d 322, 326 (9th Cir. 1983) ("[I]n a case involving competing claims to a limited fund, a claimant has standing to appeal an order disposing of assets from which the claimant seeks to be paid."); *In re P.R.T.C., Inc.*, 177 F.3d 774, 778 (9th Cir. 1999) ("A creditor does ... have a direct pecuniary interest in a bankruptcy court's order transferring assets of the estate.").

(Prior Order at 5) (emphasis added).

The Trustee acknowledges that the Court previously rejected this argument and that "no new facts have arisen that bear on this question." (AB at 4). Because the Court has already rejected this argument, the Court declines to address it in detail here. The Court is satisfied that Clifton Capital has standing for the same reasons set forth in the Prior Order.

B. Specific Evidence in Support of Fee Enhancement

Clifton Capital argues that the Bankruptcy Court erred in awarding the Trustee a fee enhancement above the lodestar figure of $758,951.70 because the Trustee failed to show that (1) the bonus was necessary to make the award commensurate with compensation for comparable nonbankruptcy services; and (2) the quality of the results obtained were not reflected in its standard hourly rate or the number of hours allowed. (OB at 19-20) (citing Prior Order at 4).

In *In re Manoa Finance Co., Inc.*, the Ninth Circuit explained that "[t]here is a strong presumption that [an award based on the lodestar] was 'reasonable compensation.' " 853 F.2d at 692. Therefore,

> [i]n order to justify a bonus [beyond the lodestar figure], appellant must come forward with specific evidence showing why the results obtained were not reflected in either his standard hourly rate or the number of hours allowed. He must also show that the bonus is necessary to make the award commensurate with compensation for comparable nonbankruptcy services.

Id. "If the bankruptcy court determines that a bonus

is justified, it must make ***detailed*** findings in support of that determination." *Id.* (emphasis added).

When granting a fee enhancement, courts may not rely on factors subsumed within the initial calculation of the lodestar. *In re Buckridge*, 367 B.R. at 204 (citing *Blum v. Stenson*, 465 U.S. 886 (1984)). Factors typically subsumed into the lodestar, and which cannot serve as an independent basis for an upward adjustment, include: (1) the novelty and complexity of the issues, (2) the special skill and experience of the professional, (3) the quality of the services, and (4) the results obtained. *Id.* at 202; *see also In re Manoa Fin. Co., Inc.*, 853 F.2d at 691. Because these factors are ordinarily accounted for in the lodestar figure, "they can support an upward adjustment only when it is shown by specific evidence that they are not fully reflected in the lodestar." *In re Manoa Fin. Co., Inc.*, 853 F.2d at 691 (citations omitted).

With respect to the first requirement — that the award be commensurate with compensation for comparable nonbankruptcy services — the Court notes that there is no direct analog to a chapter 11 trustee outside of bankruptcy, and there is no easy benchmark against which to measure. On the one hand, Clifton Capital points out that the Trustee repeatedly represented below that "[t]he rates provided are the normal hourly rates which [the Trustee] charges to its regularly paying, non-bankruptcy clients for similar services." (ER 933). On the other hand, the Bankruptcy Court reasoned that, outside of the bankruptcy context, a professional performing services similar to the Trustee might be entitled to a fee enhancement:

Unlike with attorneys and other profession-

> als who provide services outside of bankruptcy similar to those they provide in bankruptcy cases, there is no such thing as a chapter 11 trustee outside of bankruptcy. The closest analog may be a chief restructuring officer hired to run a company. It is not uncommon for such non-bankruptcy professionals to be entitled to success fees or bonuses when they deliver exceptional results. For a company such as the Debtor, a CRO could easily be entitled to additional compensation in the form of a success fee or bonus in excess of the fee enhancement sought by the Trustee in this case.

(ER 95).

The Court determines that this reasoning is sound, and that the Bankruptcy Court's conclusion therefore was not an abuse of discretion. *See In re Cook Inlet Energy LLC*, 583 B.R. at 500 ("A bankruptcy court abuses its discretion if it applies the wrong legal standard or its findings are illogical, implausible or without support in the record.").

With respect to the second requirement — that the quality of the result obtained was not already reflected in the Lodestar calculations — the Bankruptcy Court explained that this was an exceptionally difficult and complex case, and that the complexities of this case did not necessarily result in an increase in the number of hours spent by the Trustee and its staff. (ER 14). Specifically, the Bankruptcy Court found this to be an exceptional case for the following reasons:

> [t]he trustee assumed control over an operating business with several locations and was

> called upon to keep those restaurants operating in a profitable manner while dealing with the fact that there were effectively no internal controls, no reliable accounting methods or records, a toxic corporate culture that had resulted in large employee tort claims, years of unfiled tax returns and unpaid sales taxes, an owner who had siphoned off and was attempting to continue to siphon off estate assets and resources to benefit or support other business and his competing restaurants, numerous related party contracts and a principal who failed to cooperate in discovery or obey court orders. The analogy that comes to mind here is of the plate-spinners that used to appear on the Ed Sullivan show who worked furiously to keep multiple plates in the air at the same time.

(ER 86).

The Bankruptcy Court reasoned that, "[i]n light of the high level of expertise and experience required to perform these tasks in the manner in which they were performed," "[t]he number of hours spent working on the case is not a measure of the difficulty or skill level required to perform the required services in an exceptional manner." (*Id.*). The Bankruptcy Court specifically noted that, "if the complexities merely increased the number of hours that the trustee spent working on the case, this would be reflected in, and therefore compensated by, the lodestar calculation." (*Id.*).

Given that the complexity of the case and the special skill of the professional are typically subsumed into the lodestar, the question becomes whether the

Trustee has shown "by specific evidence" that they are ***not*** fully reflected in the Lodestar. *See In re Manoa Fin. Co., Inc.*, 853 F.2d at 691.

The Bankruptcy Court's thorough analysis of the record demonstrates that the Bankruptcy Court relied on the specific evidence set forth above in concluding that the complexity is not accurately reflected in the Lodestar. This is a factual question and the Bankruptcy Court is in the best position to make this determination. Because the Bankruptcy Court's conclusion is based on specific evidence and is neither implausible nor illogical, the Court determines that the Bankruptcy Court did not abuse its discretion.

C. <u>Risk of Underpayment or Loss</u>

Clifton Capital argues that the Bankruptcy Court erred by basing its award of a bonus to the Trustee on a risk of underpayment or loss. (OB at 22). Specifically, Clifton Capital argues that (1) risk of underpayment or loss cannot be considered as a matter of law under § 330; and (2) even if it could be considered, the record establishes that there was no risk of nonpayment in this case. (*Id.*).

With respect to the first point, *Burlington v. Dague*, 505 U.S. 557 (1992), and *In re Cedic Dev. Co.*, 219 F.3d 1115 (9th Cir. 2000), are instructive. In *Burlington*, the Supreme Court held that enhancements to the lodestar figure are not permitted based on risk of loss or contingency risk. 505 U.S. at 564-67 ("[E]nhancement for contingency is not permitted under the fee-shifting statutes at issue."). In *Cedic*, the bankruptcy court awarded a fee enhancement because the attorney's hourly rates did not take into account the results obtained or the risk of nonpayment. 219

F.3d at 1116. The district court reversed the bankruptcy court, interpreting *Burlington* as prohibiting enhancements based on risk of nonpayment. *Id.* The Ninth Circuit expressly rejected that reading of *Burlington*, reversed the district court, and reinstated the fee award. *Id.* at 1116-17. The Ninth Circuit distinguished Burlington as a case about contingent fees:

> *City of Burlington* is a case about contingent fees. It holds that the risk created by a contingency fee does not justify an increase beyond the lodestar. The case is not controlling here, because the risk of nonpayment by Cedic was not created by any contingency in the merits of the litigation but by the conduct of Cedic that suggested that it didn't like to pay its lawyers.

Id. (citations omitted). The Ninth Circuit explained "that the general principles applicable to fee-shifting statutes 'may require some accommodation to the peculiarities of bankruptcy.' " *Id.* at 1116-17 (quoting *Manoa*, 853 F.2d at 691).

Here, the Bankruptcy Court explained that the risk of underpayment stemmed from (1) the risk of the Trustee being awarded less in fees than the Trustee might be awarded on an hourly fee basis, and (2) the risk that the Trustee may receive only a pro rata distribution of fees if the estate has insufficient funds to pay for the full cost of services rendered:

> [I]n addition to the inherent risk of underpayment faced by all chapter 11 professionals, chapter 11 trustees face an additional underpayment risk because of § 326(a). In the Court's experience, because of § 326(a), chapter 11 trustees are very often

> awarded less fees than they would be awarded on hourly-fee bases.
>
> This was true in this case for the first two interim periods. For the first interim period, the Trustee requested fees of $252,997.09, while hours spent multiplied by hourly rates charged for non-trustee matters totaled $347,741.50. After the second interim period, the Trustee had been paid $524,184.36 pursuant to § 326(a), while hours spent multiplied by hourly rates charged for non-trustee matters totaled $566,133.00. If the case had faltered during those interim periods, the fee awarded would have been less than any amount calculated in accordance with hourly rates charged by the Trustee's firm for non-trustee matters.
>
> Because of § 326(a), chapter 11 trustees face a double risk of underpayment. First, the amount of fees awarded is very often less than the amount they would be awarded if their fees were based on hourly rates charged by their firms for their non-trustee services. Second, based on that already-reduced amount, the trustee may receive only a pro rata distribution. This double risk is not "priced into" the normal hourly rate charged by a firm for the trustee's non-trustee services.

(ER 88-91).

On the one hand, the inherent risk of underpayment here faced by all chapter 11 professionals does somewhat resemble a contingent fee: the Trustee's entitlement to a fee award here is contingent upon the quality of his performance because he may receive only a pro rata distribution of fees if the estate has insufficient funds to pay for the full cost of services

rendered. The Bankruptcy Court explained that "this inherent risk of underpayment is already priced into the hourly rates identified by attorneys, accountants, and other estate professionals when they are being employed under § 327(a) of the Code." (ER 89).

On the other hand, the Trustee faces an additional risk of underpayment because of § 326(a): the Trustee may be awarded less in fees than he would be awarded on an hourly-fee basis. The Bankruptcy Court recognized that this "double risk is not 'priced into' the normal hourly rate charged by a firm for the trustee's non-trustee services." (ER 91).

Given that the Trustee here faced two different types of underpayment risk, and that this "double risk" was not priced into the normal hourly rate, the Court determines that the risk of underpayment here is likely not the type of "contingent fee" that cannot justify an increase beyond the Lodestar pursuant to *Burlington*. *See Burlington*, 505 U.S. at 559 (a contingent fee is one where the party's attorneys assume "the risk of receiving no payment at all for their services"). This conclusion is consistent with the Ninth Circuit's determination in *Cedic* that "the general principles applicable to fee-shifting statutes 'may require some accommodation to the peculiarities of bankruptcy.' " 219 F.3d at 1116-17 (quoting *Manoa*, 853 F.2d at 691). Therefore, the Court determines that the Bankruptcy Court did not err by basing its Lodestar enhancement on a risk of underpayment or loss.

With respect to Clifton Capital's second point, Clifton Capital argues that there was never a ***real*** risk of underpayment here because the Trustee inherited "an operating, successful, and profitable business generating millions of dollars in revenue and more

than sufficient funds to pay the Trustee and estate professionals." (OB at 24). Clifton Capital points out that, "[a]t the time of each of Trustee's four fee applications, the estate had more than enough cash on hand to pay not only the Trustee's requested fees and expenses, but all administrative fees and costs." (*Id.*). Clifton Capital is essentially arguing that the Trustee's job in managing the business here was not difficult enough to create a significant risk of the business becoming insolvent.

This argument does not even attempt address the specific factual findings set forth by the Bankruptcy Court as to why the managing the business was particularly difficult here:

> In light of the numerous challenges this trustee faced and the manner in which the trustee rose to the occasion to resolve these challenges, producing exceptional results, this Court finds that the trustee utilized in connection with the administration of this estate levels of strategic thinking and diplomacy above and beyond those normally employed by a trustee in a chapter 11 case. The trustee assumed control over an operating business with several locations and was called upon to keep those restaurants operating in a profitable manner while dealing with the fact that there were effectively no internal controls, no reliable accounting methods or records, a toxic corporate culture that had resulted in large employee tort claims, years of unfiled tax returns and unpaid sales taxes, an owner who had siphoned off and was attempting to

> continue to siphon off estate assets and resources to benefit or support other business and his competing restaurants, numerous related party contracts and a principal who failed to cooperate in discovery or obey court orders.

(ER 86). In light of all of the difficulties faced by the Trustee, the fact that the estate had enough cash on hand to pay the Trustee's requested fees and expenses, as well as all administrative fees and costs, appears to ***support***, rather than discount, the Bankruptcy Court's conclusion that the Trustee produced exceptional results under these circumstances. And Clifton Capital has failed to explain why the difficulties identified by the Bankruptcy Court did not put the business in any real danger of insolvency. The Bankruptcy Court's factual findings are supported by the record. Therefore, the Court is not convinced by Clifton Capital's conclusory assertion that there was no real risk of underpayment here.

Accordingly, the Second Fee Order is **AFFIRMED**.

D. <u>Strike Order</u>

Clifton Capital argues that the Bankruptcy Court erred by striking the declarations that Clifton Capital submitted in response to the Trustee's supplemental brief on remand. (OB at 52). Specifically, Clifton Capital argues that it is entitled to present countervailing evidence because the Trustee's supplemental brief cited to evidence not previously submit in connection to the Final Fee Application. (*Id.*) (citing *In re Colusa Reg'l Med. Ctr.*, 604 B.R. 839, 852 (B.A.P.

9th Cir. 2019) ("Typically, a party must have an adequate opportunity to address the evidence against it and an opposing party should have both the ability to do so in writing and to produce counterevidence.")). The Court disagrees.

Clifton Capital acknowledges that the Trustee's supplemental brief did not introduce new evidence. (OB at 53). The supplemental brief cited to the same evidence introduced in the Trustee's original reply brief, *i.e.*, evidence that was already in the record. (*Id.*) ("Clifton Capital took issue with these 'four pages of things' at the original hearing on the Final Fee Application, pointed out that the Trustee had raised new arguments and purported evidence in his reply, and requested the opportunity to respond before the Court ruled.").

When discussing this precise issue before the Bankruptcy Court on remand, Clifton Capital represented to the Bankruptcy Court that it was comfortable with the record as it currently existed, and that it would seek additional discovery only in the event that the Trustee attempted to provide additional evidence in the supplemental brief:

> So if we're limited to the record as is, we're comfortable with that. To the extent, however, that Mr. Sharp attempts to provide any additional evidence that's not currently in the record to support an enhancement, we feel that we should be entitled to discovery on that additional evidence, and then a supplement — and then a briefing schedule that's — flows from that.

(ER 2109). Because the Trustee's supplemental brief

cited to evidence previously submitted in connection with its reply brief, the Trustee's supplemental brief did not introduce ***new*** evidence.

Even assuming that the Bankruptcy Court should have stricken the evidence submitted in connection with the Trustee's reply brief in the first place — a conclusion this Court does not endorse — Clifton Capital failed to raise this issue in its first appeal, and has therefore waived its right to make that argument here.

Accordingly, the Strike Order is **AFFIRMED**.

V. CONCLUSION

The Second Fee Order is **AFFIRMED**. The Bankruptcy Court neither erred nor abused its discretion in awarding the Trustee a fee enhancement above the Lodestar.

The Strike Order is **AFFIRMED**. The Bankruptcy Court neither erred nor abused its discretion in granting the Trustee's motion to strike Clifton Capital's newly submitted declarations because the Trustee did not introduce any new evidence.

IT IS SO ORDERED.

DATED: AUGUST 6, 2021

/s/ Michael W. Fitzgerald
United States District Judge

CC: Bankruptcy Court

APPENDIX C

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

NO. 18-10098 MWF

IN RE EAST COAST FOODS, INC.,
Debtor

Filed: December 18, 2019

ORDER RE: BANKRUPTCY COURT'S ORDER

MICHAEL W. FITZGERALD, United States District Judge:

Before the Court is an appeal from the United States Bankruptcy Court (the Honorable Sheri L. Bluebond, United States Bankruptcy Judge). Appellant Clifton Capital Group, LLC ("Clifton Capital") appeals from the Bankruptcy Court's Order granting the Trustee's Fourth and Final Application for Compensation and Reimbursement of Fees and Expenses (the "Final Fee Application") in the amount of $1,155,944.71. The Order was issued on November 19, 2018.

Clifton Capital submitted its Opening Brief

("OB") on March 6, 2019. (Docket No. 11). On May 22, 2019, Appellee Bradley D. Sharp, Chapter 11 Trustee, submitted his Brief ("AB"). (Docket No. 16). On July 1, 2019, Appellant submitted its Reply Brief ("RB"). (Docket No. 23). The Court has read and considered the papers filed in this appeal, and held a hearing on November 6, 2019.

The Order is **AFFIRMED *in part*, REVERSED *in part***, and **REMANDED** for further proceedings. The Bankruptcy Court did not make the required findings to determine that the Trustee is entitled to a fee award that exceeds the lodestar figure. However, the Bankruptcy Court did not abuse its discretion in awarding compensation for services performed by Development Specialists, Inc. ("DSI").

I. BACKGROUND

On March 25, 2016, East Coast Foods, Inc. (the "Debtor") filed for bankruptcy under Chapter 11. (Appellant's Excerpts of Record ("ER") 60 (Docket No. 11)). On April 29, 2016, the Office of United States Trustee (the "U.S. Trustee") appointed the Official Committee of Unsecured Creditors (the "Committee"). (ER 84). Clifton Capital is a member of the Committee. (*Id.*).

On September 28, 2016, the Bankruptcy Court appointed Bradley D. Sharp as the Chapter 11 Trustee (the "Trustee"). (ER 90). The Trustee handled numerous issues during his appointment, including state court actions, tax disputes, landlord disputes, accounting practices, and return of intellectual property assets. (ER 967-70; AB 10-14). The Trustee employed his company, DSI, to help him perform some of

his duties as the Trustee. (ER 102, 258, 331, 879).

On July 3, 2018, the Bankruptcy Court entered an order confirming a joint Plan of Reorganization (the "Plan"). (ER 715-26). On September 10, 2018, the court granted non-material modifications to the Plan, and on September 14, 2018, the Plan became effective. (ER 715-34).

The Trustee filed four fee applications during the bankruptcy case. In the first three applications, the Trustee sought approval of fees and costs on an interim basis. (ER 102 *et seq.*, ER 258 *et seq.*, ER 331 *et seq.*). In the fourth and final application, the Trustee sought final approval of his fees and costs. (ER 879 *et seq.*).

In each Fee Application, the Trustee sought fees incurred by himself as well as by DSI personnel. Specifically, each Application contained the disclosure: "This Application includes the time records for employees of [DSI] ... who assisted the trustee in the performance of his duties of this case." (ER 102, 258, 331, 879).

The Committee filed an objection to the First Fee Application, arguing that the court never authorized DSI's employment, and therefore, fees to DSI totaling $202,767.59 should be disallowed. (ER 189). The Bankruptcy Court overruled the Committee's objection and approved the First Fee Application in full. (SER 41). The Committee did not object to DSI's fees in the second and third applications, and the Bankruptcy Court approved both Fee Applications in full. (SER 43-44; ER 52-53; AB 20).

The Trustee filed the Final Fee Application in October 2018. The Final Fee Application disclosed that the Trustee and his staff at DSI had worked 1,692.2 hours during the case, which would equate to $758,955.50 if billed at normal hourly rates. (ER 885). However, the Trustee requested a fee of $1,155,844.71, which is the maximum fee permitted under 11 U.S.C. § 326(a) ("§ 326(a)"). (*Id.*).

Clifton Capital filed an objection to the Final Fee Application. (ER 936 *et seq.*). It did not object to the Trustee's request for fees associated with work performed by his staff at DSI. However, Clifton Capital argued that the Trustee should not be paid the maximum amount under § 326(a), which is a limit and not a presumption of reasonableness. (ER 942-44). Clifton Capital argued that the Trustee had the burden of establishing his requested compensation was reasonable under 11 U.S.C. § 330(a) ("§ 330(a)"), and that the proper way to establish reasonable compensation is by applying the lodestar method. (*Id.*).

The Bankruptcy Court granted the Trustee's Final Fee Application and entered an order granting the Final Fee Application (the "Final Fee Order"). (ER 58). The court provided two alternative grounds for granting the Fee Application. First, the court determined that the requested fee was reasonable because it equaled the amount set forth under § 326(a). The court explained: "Congress has really tried to be pretty clear that trustee compensation, it's really more in the nature of commission" and "it takes some pretty extraordinary circumstances for me to revisit the Trustee compensation that's provided by formula"

under § 326(a). (ER 47).

The court then provided an alternative basis for its decision: "[I]n the alternative – aside from my discussion of how I read the compensation formula for trustees, in the alternative, even if I look at it simply as reasonable compensation, I think this was an exceptional case." (ER 51). The court noted that "[t]his case was a mess," and "there were a number of problems with the way Mr. Hudson had run the business, resulting in multi-million dollar judgments and tax claims." (*Id.*). Because the Trustee ran the Debtor's business in a professional manner, "had an awful lot of cleanup to do and an awful lot of challenges facing him in doing that," the court held that the compensation the Trustee was seeking as "reasonable for the circumstances, under the circumstances and for the results achieved." (ER 52).

Appellant filed the instant appeal of the Final Fee Order.

II. STANDARD OF REVIEW

A bankruptcy court's conclusions of law are reviewed de novo and findings of fact are reviewed for clear error. *Zurich Am. Ins. Co. v. Int'l Fibercom, Inc.*, 503 F.3d 933, 940 (9th Cir. 2007). Pertinent to this appeal, the bankruptcy court's award of professional fees "will not [be] disturb[ed] ... unless the bankruptcy court abused its discretion or erroneously applied the law." *In re Strand*, 375 F.3d 854, 857 (9th Cir. 2004). "A bankruptcy court abuses its discretion if it applies the wrong legal standard or its findings are illogical, implausible or without support in the record." *In re*

Cook Inlet Energy LLC, 583 B.R. 494, 500 (B.A.P. 9th Cir. 2018).

III. DISCUSSION

A. Standing

"In order to have standing to appeal, a party must be directly and adversely affected pecuniarily by the bankruptcy court decision." *In re 240 N. Brand Partners, Ltd.*, 200 B.R. 653, 657 (B.A.P. 9th Cir. 1996). The Trustee argues that Clifton Capital is not an "aggrieved person" because it "is guaranteed to be paid 100% of its alleged claim" under the Plan. (AB at 6). In support of this claim, the Trustee points to a declaration made by Clifton Capital's principal, who testified that the Plan "ensure[s] 100% payment to creditors." (AB at 6; SER 63).

In response, Clifton Capital argues that it is aggrieved because "[t]here are not yet enough funds on hand to pay all creditors, including Clifton Capital, in full, and there are outstanding contingencies under the Plan that must occur before those funds become available." (RB at 3). In fact, Clifton Capital notes that it "has not been paid any amount on its allowed claim." (*Id.*). At the hearing, Clifton Capital confirmed that there are not sufficient funds to pay back all the creditors. Clifton Capital further argues that "[a]llowing the Trustee to receive and retain compensation beyond which he is entitled subordinates Clifton Capital's claim more than it should be." (RB at 4).

Although neither party provides case law directly on point on the issue, the Court finds Clifton

Capital's argument to be more persuasive. Clifton Capital's claim is "subordinated to ... all allowed and secured and unsecured claims and approved administrative expenses." (SER 46; AB at 15-16). This is important because to date, there is not sufficient capital to pay all creditors. Because the increased compensation to the Trustee will further subordinate Clifton Capital's claim, the Court concludes that Clifton Capital is directly and adversely affected by the Final Fee Order, giving it standing to pursue this appeal. *See Salomon v. Logan (In re International Envtl. Dynamics, Inc.*), 718 F.2d 322, 326 (9th Cir.1983) ("[I]n a case involving competing claims to a limited fund, a claimant has standing to appeal an order disposing of assets from which the claimant seeks to be paid."); *In re P.R.T.C., Inc.*, 177 F.3d 774, 778 (9th Cir. 1999) ("A creditor does ... have a direct pecuniary interest in a bankruptcy court's order transferring assets of the estate.").

The Court thus turns to the merits.

B. <u>The Fee Order</u>

Clifton Capital argues that the Fee Order was an abuse of discretion for two reasons. First, Clifton Capital argues that the Bankruptcy Court erred in determining that the Trustee's requested fees were reasonable. Second, Clifton Capital argues that the Bankruptcy Court erred in awarding the Trustee compensation for services performed by DSI. The Court agrees with Clifton Capital that the Bankruptcy Court erred in determining that the Trustee's requested fees were reasonable because the court did not make detailed findings as to why the Trustee is

entitled to an amount significantly higher than the lodestar figure. However, the Court concludes that the Bankruptcy Court did not abuse its discretion in awarding the Trustee compensation for services performed by DSI.

1. Reasonableness of the Trustee's Fee

Clifton Capital argues that the Bankruptcy Court committed two errors when it determined the reasonableness of the Trustee's fee.

The Wrong Legal Standard: Clifton Capital first argues that the Bankruptcy Court applied the wrong legal standard. (OB at 12-19). According to Clifton Capital, the Bankruptcy Court concluded that the Trustee's requested fee was reasonable because it equaled the amount provided under § 326(a). (OB at 12-13). But § 326(a) sets a statutory cap for trustee compensation, not what is presumptively reasonable compensation. Therefore, Clifton Capital argues that the Bankruptcy Court should have considered "all relevant factors" listed under § 330(a) to determine whether the Trustee's requested compensation was reasonable. (OB at 15-16). In response, the Trustee argues that the Bankruptcy Court did precisely that; it provided an alternative ground for finding the requested fee to be reasonable under all relevant factors as stated in § 330(a). (AB at 27-28).

The Court does not find Clifton Capital's argument to be persuasive. The Bankruptcy Court provided two separate bases for determining the reasonableness of the Trustee's requested fees. The Bankruptcy Court first determined that the requested fee

was reasonable because the fee should be treated as a "commission" that is equal to the § 326(a) statutory cap. (*See* ER 47-48). If this was the only basis for the Bankruptcy Court's determination, Clifton Capital's argument would have merit.

However, the Bankruptcy Court also provided an alternative basis for its decision. The Bankruptcy Court stated: "in the alternative, even if I look at it simply as reasonable compensation, I think this was an exceptional case." (ER 51). The Bankruptcy Court then explained the challenges the Trustee faced in this case and concluded that "the compensation that [the Trustee] is requesting here in accordance with the formula is reasonable for the circumstances, under the circumstances and for the results achieved." (ER 52). Even Clifton Capital appears to acknowledge that this is the correct legal standard for determining the reasonableness of the Trustee's fees. Therefore, the Court determines that the Bankruptcy Court did not err by applying the wrong legal standard.

Exceeding the lodestar figure: Even if the Bankruptcy Court articulated the correct legal standard, Clifton Capital further argues that the court erred by awarding a fee amount that far exceeded the lodestar figure without providing sufficient reasoning for the deviation. (RB at 15-19). Both parties appear to agree that the Bankruptcy Court was not required to apply the lodestar. (*See* RB at 11). Nonetheless, Clifton Capital argues that lodestar approach is the "primary method" for determining reasonableness of the Trustee's compensation and argues that the court should not have granted the Trustee an award beyond the lodestar amount without "specific evidence that

an award based on his standard hourly rate and actual hours worked does not fairly compensate for the work done." (OB at 28).

In response, the Trustee argues that the Bankruptcy Court has provided sufficient reasoning for why this case was exceptional. The Trustee notes that the Bankruptcy Court explained that "there were a number of problems with the way Mr. Hudson had run the business, resulting in multi-million dollar judgments and tax claims," "[t]here were other labor problems," and "it was apparent to this Court that [the Debtor] did not know how to run a business with multiple locations in a professional manner." (ER 51-52). The Bankruptcy Court also observed that the Trustee came in and ran the business and "had an awful lot of cleanup to do and an awful lot of challenges facing him in doing that." (ER 52). According to the Trustee, this record demonstrates that the Bankruptcy Court considered the circumstances of this case and appropriately determined a reasonable amount of fees.

The Court agrees with Clifton Capital. In *In re Manoa Finance Co., Inc.*, the Ninth Circuit explained that "[t]here is a strong presumption that [an award based on the lodestar] was 'reasonable compensation.' " 853 F.2d 687, 692 (9th Cir. 1988). Therefore, "[i]n order to justify a bonus [beyond the lodestar figure], appellant must come forward with specific evidence showing why the results obtained were not reflected in either his standard hourly rate or the number of hours allowed. He must also show that the bonus is necessary to make the award commensurate with compensation for comparable nonbankruptcy services." *Id.* Moreover, [i]f the bankruptcy court determines that a bonus is justified, it must make ***detailed***

findings in support of that determination." *Id.* (emphasis added).

Here, the parties dispute what the correct lodestar amount is. However, after correcting for a typographical error in the Final Fee Application, it appears that the lodestar amount would have been $758,977.50. (AB at 22; RB at 16, n.10). It is undisputed that the Bankruptcy Court awarded $1,155,844.70. Therefore, the Bankruptcy Court appears to have determined that a significant enhancement or bonus to the lodestar figure was appropriate. However, the Court cannot identify any detailed findings in support of this determination in the record. Moreover, while the Bankruptcy Court observed that the Trustee faced various challenges in this action, it is not clear why such considerations would not have been encompassed in the lodestar figure, or would justify such a substantial bonus.

Accordingly, the Court vacates the Order granting $1,155,944.71 in fees to the Trustee. On remand, the Bankruptcy Court should either (i) definitively establish the lodestar figure and award fees accordingly, or (ii) make detailed findings to determine whether a fee award beyond the lodestar figure is warranted.

2. Compensation for Services Performed by DSI

Clifton Capital also argues that the Bankruptcy Court erred in awarding the Trustee compensation for services performed by DSI, which were not properly employed pursuant to 11 U.S.C. § 327. (OB at 29). Clifton Capital argues that DSI was never employed by the bankruptcy estate, but still billed and

was awarded $286,998 for its services. (*Id.*). Clifton Capital argues that this award was reversible error.

As a preliminary matter, the Trustee argues that Clifton Capital's objection has been waived because it did not raise this argument in its objection to the Final Fee Application. (AB at 35). Even though the Trustee disclosed that he was seeking fees for services rendered by DSI personnel, and even though Clifton Capital recognized this fact, Clifton Capital did not object to the Final Fee Application on those grounds. (*Id.*). In fact, the Trustee asserts that Clifton Capital did the opposite by asking the Bankruptcy Court to approve the Trustee's fees in the amount of $810,661.24, which included compensation for services rendered by DSI personnel. (*Id.*)

In response, Clifton Capital argues that "there was no reason—or need—to continue to raise the issue on each subsequent fee application." (RB at 20, n.11). Clifton Capital argues that it did not need to raise this issue because the Committee had raised this exact objection in the First Fee Application, but the Bankruptcy Court overruled the objection and approved the award to DSI. (*See* SER 41).

Although Clifton Capital did not raise this objection to DSI in response to the Final Fee Application, the Court determines that the argument was sufficiently raised for the Bankruptcy Court to rule on it in the First Fee Application. *See In re Mercury Interactive Corp.*, 618 F.3d at 922. ("Although no bright line rule exists to determine whether a matter has been properly raised below, an issue will generally be deemed waived on appeal if the argument was not

raised sufficiently for the trial court to rule on it.") (internal quotation marks and citation omitted). Accordingly, the Court examines the merits.

"In bankruptcy proceedings, professionals who perform services for a debtor in possession cannot recover fees for services rendered to the estate unless those services have been previously authorized by a court order." *In re Atkins*, 69 F.3d 970, 973 (9th Cir. 1995); *see* 11 U.S.C. § 327(a) (with court approval, the trustee may employ "professional persons" who do not hold an adverse interest to the estate). "The bankruptcy courts in this circuit possess the equitable power to approve retroactively a professional's valuable but unauthorized services," but "such retroactive approval should be limited to situations in which 'exceptional circumstances' exist." *In re Atkins*, 69 F.3d at 973-74. "To establish the presence of exceptional circumstances, professionals seeking retroactive approval must satisfy two requirements: they must (1) satisfactorily explain their failure to receive prior judicial approval; and (2) demonstrate that their services benefitted the bankrupt estate in a significant manner." *Id.* at 974.

Here, it is undisputed the Trustee never filed an employment application under § 327 for DSI. Nonetheless, the Trustee argues that it was not required to employ DSI under § 327 because there is no prohibition on a trustee utilizing the services of his or her staff to assist him or her in performing administrative tasks. (AB at 35-36). The Trustee further notes that Clifton Capital did not show that any of the services provided by DSI personnel did not constitute trustee services. (*Id.* at 37-38). Finally, the Trustee argues that even if he should have formally sought to

employ DSI, his failure to do so was harmless because there can be no question that the Bankruptcy Court would retroactively authorize DSI's employment. (*Id.* at 38).

In response, Clifton Capital argues that DSI should still have been employed under § 327 because under the plain language of the statute, a professional cannot be paid by the bankruptcy estate unless the services rendered were previously approved by court order. (RB at 20). Clifton Capital further argues that DSI personnel are professionals.

The critical issue appears to be whether DSI personnel should be considered a "professional" within the meaning of § 327(a). Neither party has provided a clear definition of the term, and there appears to be limited case law on the issue. However, the Court notes that "[n]ot every person employed by a trustee is a 'professional person' within the meaning of § 327." *In re Blair*, 329 B.R. 358 (B.A.P. 9th Cir. 2005). "A 'professional person' is one who takes a central role in the administration of the bankruptcy estate and in the bankruptcy proceedings[.]" *Id.* (internal quotation marks and citation omitted). "Individuals or entities that perform mechanical, nondiscretionary tasks are not 'professional persons' within the meaning of § 327." *Id.*; *see also In re Fretheim*, 102 B.R. 298, 299 (Bankr. D. Conn. 1989) (To qualify as a professional under § 327(a), "it must be determined whether an employee is to be given discretion or autonomy in some part of the administration of the debtor's estate.").

Here, the Trustee detailed the services that

DSI personnel provided to assist him, and the Bankruptcy Court determined that these services should be included as part of trustee services and should be paid as part of the trustee fees. (SER 41). Therefore, it appears that the Bankruptcy Court implicitly determined that DSI personnel are not professionals that must be employed under § 327. The Court determines that this finding was neither illogical nor implausible. It appears that the DSI personnel assisted the Trustee by performing mostly administrative tasks, including implementing new cash controls, a point of sale system, and improved financial reporting. (ER 113-114). Even Clifton Capital does not appear to dispute that the nature of the services conducted by DSI personnel were administrative. While Clifton Capital emphasizes that the DSI personnel's hourly rates are higher than what one would expect from lower-hourly rate staff, the Court does not find this fact to be determinative.

Accordingly, the Bankruptcy Court did not abuse its discretion in awarding the Trustee compensation for services performed by DSI.

IV. CONCLUSION

The Final Fee Order is **AFFIRMED *in part*, REVERSED *in part***, and **REMANDED** for further proceedings consistent with this Order. Specifically, the Bankruptcy Court in its discretion may either enter an order awarding fees consistent with the lodestar figure (which may be recalculated) or make detailed findings sufficient to justify a higher amount.

IT IS SO ORDERED.

DATED: December 18, 2019

/s/ Michael W. Fitzgerald
United States District Judge

CC: Bankruptcy Court

APPENDIX D

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

NO. 2:16-13852 BB

IN RE EAST COAST FOODS, INC.,
Debtor

Filed: November 18, 2020

ORDER ON APPLICATION FOR PAYMENT OF FINAL FEES AND/OR EXPENSES (11 U.S.C. § 330)

1. Name of Applicant (specify): Bradley D. Sharp, former Chapter 11 Trustee

2. This proceeding was heard at the date and place set forth above and was ☒Contested ☐Uncontested

3. Appearances were made as follows:

a. ☒ Applicant present in court

b. ☒ Attorney for Applicant present in court (name): John N. Tedford, IV (Danning, Gill, Israel & Krasnoff, LLP)

c. ☐ Attorney for United States trustee present in court

d. ☒ Other persons present as reflected in the court record

4. Applicant gave the required notice of the Application on (specify date): October 24, 2018

5. The court orders as follows:

a. ☐ Application for Payment of Interim Fees is approved as follows:

(1) ☐ Total amount allowed: $

(2) ☐ Amount or percentage authorized for payment at this time:

b. ☐ Application for Reimbursement of Interim Expenses is approved and authorized for payment:

☐ Total amount allowed: $

c. ☒ Application for Payment of Final Fees is approved in the amount of: $1,155,844.71.

d. ☒ Application for Reimbursement of Final Expenses is approved and authorized for payment: Total amount allowed: $5,107.32.

e. (1) ☐ Application is denied

☐ in full

☐ in part

☐ without prejudice

☐ with prejudice

(2) Grounds for denial (specify):

f. ☒ The court further orders (specify):

On October 24, 2018, Bradley D. Sharp, the former chapter 11 trustee (the "Trustee") for the estate of East Coast Foods, Inc. (the "Debtor"), filed his final application for compensation and reimbursement of expenses (the "Final Fee Application") (docket entry no. 1134). On November 19, 2018, the Court entered an omnibus order on final applications by the Trustee and others for approval of their fees and expenses (docket no. 1192). Clifton Capital Group, LLC ("Clifton Capital") appealed the Court's approval of the full amount of fees sought by the Trustee. On or about December 18, 2019, the District Court entered an order affirming in part, reversing in part, and remanding for further proceedings. The Trustee filed a supplemental brief on June 17, 2020 (docket no. 1372), Clifton Capital filed a supplemental brief on September 9, 2020 (docket no. 1385), and the Trustee filed a supplemental reply brief on October 7, 2020 (docket no. 1398). A hearing on the Final Fee Application was held on November 4, 2020, the Honorable Sheri Bluebond, United States Bankruptcy Judge, presiding. John N. Tedford, IV, of Danning, Gill, Israel & Krasnoff, LLP, appeared by Zoom on behalf of the Trustee; Anthony R. Bisconti of Bienert Katzman PC, appeared by Zoom on behalf of Clifton Capital; and all other appearances were as noted on the record at the hearing.

The Court having considered the Final Fee Application, the supplemental papers filed

by the Trustee and Clifton Capital on remand except the declarations of John L. Sadd, Jed Sanford and Sam White filed by Clifton Capital in support of its supplemental brief, the District Court's order, and all of the other pleadings on file in this case relevant to these proceedings, having heard the statements of counsel at the hearing, for the reasons stated in this Court's separately filed Findings of Fact and Conclusions of Law in Support of Order Approving Former Chapter 11 Trustee's Final Application for Approval of Fees and Expenses and on the record at the hearing, for good cause appearing, the Court approves the Final Fee Application and, on a final basis, awards the Trustee fees and costs in the amounts set forth above.

DATED: NOVEMBER 18, 2020

/s/ Sheri Bluebond

United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

NO. 2:16-13852 BB

IN RE EAST COAST FOODS, INC.,
Debtor

Filed: November 18, 2020

FINDINGS OF FACT AND CONCLUSIONS OF LAW IN SUPPORT OF ORDER APPROVING FORMER CHAPTER 11 TRUSTEE'S FINAL APPLICATION FOR APPROVAL OF FEES AND EXPENSES

The matter of the final application for compensation and reimbursement of expenses (the "Final Fee Application") of Bradley D. Sharp, the former chapter 11 trustee (the "Trustee") for the estate of East Coast Foods, Inc. (the "Debtor"), came on for hearing before the undersigned United States Bankruptcy Judge on November 4, 2020. Appearances were as reflected in the record.

The Court having read and considered the Trustee's supplemental brief and proposed findings of fact and conclusions of law in support of the Final Fee Application (docket no. 1372), Clifton Capital Group, LLC's supplemental brief and declaration of Anthony R. Bisconti, but not the declarations of Sam White, John L. Sadd, and Jed Sanford (docket no. 1385), the Trustee's supplemental reply (docket no. 1398), and all other pleadings and papers that have been filed and brought before the Court during this case, having presided over all hearings conducted in this case since its inception in March 2016, and having heard and considered the arguments of counsel at the hearing, hereby makes the following findings of fact and conclusions of law:

I. FINDINGS OF FACT THE DEBTOR'S BUSINESS

1. In 1976, Herbert Hudson ("Hudson") established Roscoe's House of Chicken & Waffles in Hollywood, California. [Dkt no. 911, p. 13.] Over the years, Hudson expanded the business and had seven locations by the time the Debtor filed its bankruptcy petition in March 2016. [*Id.*] The first four locations were operated by the Debtor (Gower Street in Hollywood; Pico Boulevard in Los Angeles; 106 Manchester Avenue in South Los Angeles; and Lake Avenue in Pasadena). [Dkt no. 911, pp. 13, 75.] The other three are separately incorporated and owned by Hudson. [Dkt no. 911, p. 13.]

PREPETITION LITIGATION AGAINST THE DEBTOR

2. In 2013, a former employee, Daniel Beasley ("Beasley"), filed a wrongful termination suit against the Debtor. [POC 12, p. 2.] In October 2015, the state

court entered a Judgment on Jury Verdict awarding Beasley over $3.2 million. [POC 12, pp. 2, 6-7.] The Debtor appealed, but was unable to obtain an appeal bond that would prevent any levy or execution on its assets. [Dkt no. 56, p. 2.]

3. Also in 2013, a class action lawsuit was filed against the Debtor, alleging claims related to the Debtor's alleged violations of California's Labor Code. [Dkt no. 122, pp. 11-12.] The matter was settled for $900,000, and in February 2016 the state court granted final approval of the settlement. [Dkt no. 122, p. 12.] The settlement payment was due in April 2016. [Dkt no. 122, p. 13.]

4. In February 2016, a half dozen plaintiffs sued the Debtor and other entities, asserting claims for, among other things, discrimination and failure to accommodate. [See POC 25-1, p. 5.] This action was in its infancy when the Debtor filed for bankruptcy.

FRAUDULENT TRANSFER OF THE DEBTOR'S MOST VALUABLE ASSETS

5. In February 2016, Hudson formed a new entity called Roscoe's Intellectual Properties, LLC ("Roscoe's IP"). [AP Dkt no. 19-8, pp. 28-29; AP Dkt no. 19-14, p. 2.] Hudson was the sole owner of Roscoe's IP. [AP Dkt no. 19-8, p. 28.]

6. On March 10, 2016 – 15 days before filing this case – the Debtor transferred its most valuable assets – intellectual property, including the Roscoe's Chicken N' Waffles trademark – to Roscoe's IP. [AP Dkt no. 19-7, pp. 12-27.] The transfer was structured as if it was a "sale" for $3.5 million, plus up to an additional $2.5 million depending on a future appraisal of the assets' value. [AP Dkt no. 19-7, p. 14.] Roscoe's

IP purportedly agreed to pay the full sale price over 15 years. [AP Dkt no. 19-7, pp. 14-15.]

7. Also on March 10, 2016, the Debtor entered into a Trademark License Agreement with Roscoe's IP, in which the Debtor purportedly "licensed" its intellectual property back from Roscoe's IP. [AP Dkt no. 19-7, pp. 29-40.] The term was only for five years, and the Debtor agreed to pay Roscoe's IP 1.5% of its quarterly net sales. [AP Dkt no. 19-7, pp. 29-30.]

8. At the § 341(a) meeting of creditors conducted in this case, Hudson admitted, under oath, that the transfer was made because judgment creditors were trying to get hold of the Debtor's intellectual property. [AP Dkt no. 19-8, p. 39.] According to Hudson, "we figured it'd be better just to take it out of East Coast's name and put it in an LLC." [*Id.*]

9. The assignment of the Debtor's trademark was registered with the U.S. Patent and Trademark Office on March 23, 2016 – only two days before the Debtor filed this case. [AP Dkt no. 19-13, p. 2.]

10. On May 4, 2016, without seeking Court approval, the Debtor and Roscoe's IP purportedly amended the agreement to increase the purchase price to $5.5 million, to be paid over 15 years. [AP Dkt no. 19-7, pp. 41-47.] The first payment of $223,140 (less amounts allegedly due under the licensing agreement) purportedly would be made on July 10, 2016, with the balance paid in monthly payments of $55,785. [AP Dkt no. 19-7, p. 42.]

11. Roscoe's IP failed to pay the amounts it purportedly agreed to pay under the sale agreement. [AP Dkt no. 19, pp. 32-33.]

THE DEBTOR'S BANKRUPTCY FILING

12. On March 23, 2016, Beasley levied on the Debtor's bank accounts. [Dkt no. 56, pp. 2-3.] This precipitated the Debtor's bankruptcy filing. [Dkt no. 56, p. 3.]

13. On March 25, 2016 (the "Petition Date"), the Debtor filed a voluntary petition for relief under chapter 11 of the United States Code (the "Code"). [Dkt no. 1]

14. On March 29, 2016, the Debtor filed a motion for authority to use cash collateral. [Dkt no. 4.] In that motion, the Debtor stated that it intended to file a chapter 11 plan that would be "based on the continuing operation of Debtor and at least partial repayment of all creditors." [Dkt no. 4, p. 3.]

15. The Debtor filed its schedules on April 8, 2016. [Dkt no. 38.]

16. In its schedule of assets, the Debtor stated that it had no patents, copyrights, trademarks, or trade secrets. [Dkt no. 38, p. 10.] It disclosed that, a few months earlier, it had transferred its intellectual property rights to the Roscoe's Chicken and Waffle name and mark to Roscoe's IP. [Dkt no. 38, p. 28.] According to the schedules, the Debtor had "intellectual property receivables (in installments)" worth $3.5 million. [Dkt no. 38, p. 10.]

17. In its schedule of assets, the Debtor stated that it had no internet domain names or websites. [Dkt no. 38, p. 10.]

THE DEBTOR'S INABILITY TO PROVIDE ADEQUATE FINANCIALS

18. From the start, the Debtor's financial accounting and budgeting was extremely problematic. Hudson himself seemed to acknowledge that he did

not run the business in a normal way. At a meeting of creditors conducted on April 25, 2016, Hudson reportedly testified that "[i]t is a unique operation. It's not like any other operation. I run an unorthodox business." [Dkt no. 186, p. 2.]

19. In support of the cash collateral motion filed a few days after the Petition Date, Hudson provided only a one-page "budget" that purportedly showed anticipated monthly revenues and expenses for 90 days. [Dkt no. 4-2, p. 2.] Some problems the Court and others had with the budget, including the lack of detail, were later identified in a pleading filed by Beasley. [Dkt no. 37, p. 2.] The Debtor eventually filed more detailed budgets, but they continued to raise questions. [*See, e.g.*, Dkt no. 52, p. 4.]

20. Serious questions also were raised about payments made to Hudson prior to the Petition Date. For example, even though the Statement of Financial Affairs did not disclose any payment made to Hudson during the year prior to the Petition Date, the Debtor served a notice of setting/increasing insider compensation which stated that he had been paid the equivalent of $240,000 per year during that time period. [Dkt no. 38, p. 26; Dkt no. 55, p. 21.]

21. Bank of Hope asserted a $600,000-plus lien on all of the estate's assets and the IRS asserted a blanket lien for about $75,000. [Dkt no. 489, pp.14-24; POC 2-4.] The Court entered orders authorizing the Debtor to use cash collateral on an interim basis, but only granted such authority for limited periods. [Dkt nos. 27, 54, 86, 129.] In April 2016 the Court granted the Debtor authority to use cash collateral for a month but required the Debtor to, among other things, file a report of its income and expenses for the first few

weeks of the case, and required that the report be "accompanied and backed up by evidence and declaration of a person knowledgeable of the facts stated therein." [Dkt no. 54, p. 3.]

22. Section 1104(c) of the Code provides that a court may appoint an "examiner" to "conduct such an investigation of the debtor as is appropriate, including an investigation of any allegations of fraud, dishonesty, incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the debtor of or by current or former management of the debtor." In this Court's experience, an examiner is rarely appointed.

23. In July 2016, the U.S. Trustee and the Debtor entered into a Stipulation Directing the Appointment of an Examiner. [Dkt no. 128.] As reflected in the stipulation: Debtor filed a motion for cash collateral and included a budget that did not provide a detail[ed] break-out of expenses or income by location. Subsequent budgets did not include adequate accounting documentation. There was also discussion at the cash collateral hearings about Debtor's transactions with insiders and discussions at the meeting of creditors about internal controls and accounting procedures. [Dkt no. 128, pp. 1-2.] In the hope that an examiner's report would provide confidence in its internal controls, accounting systems, and management, the Debtor agreed to appointment of an examiner. [Dkt no. 128, p. 2.]

24. On July 21, 2016, the Court entered an order approving the Debtor's stipulation with the U.S. Trustee. [Dkt no. 139.] A hearing on the status and timing of the examiner's review was set for September

28, 2016. [Dkt no. 139, p. 2.] The U.S. Trustee appointed Christopher Barclay (the "Examiner") as the examiner. [Dkt no. 148.]

THE COMMITTEE'S INVOLVEMENT PRIOR TO THE TRUSTEE'S APPOINTMENT

25. On April 29, 2016 (about one month after the Petition Date), the U.S. Trustee filed its notice of appointment of a committee of creditors holding unsecured claims (the "Committee"). [Dkt no. 58.] The five creditors on the Committee were Beasley, Sergio Borgognone, Choice Foods, Clifton Capital Group, LLC ("Clifton Capital"), and Asaf Law APC. [*Id.*]

26. In a case such as this one, with questionable financial reporting, large payments to insiders prior to and after the petition date, so many insider dealings, and the transfer of valuable assets to a related party shortly before the petition was filed, a committee typically exercises its authority to "investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business . . . and any other matter relevant to the case or to the formulation of a plan." 11 U.S.C. § 1103(c)(2). With court approval, the Code allows committees to employ attorneys, accountants, and other agents to help committees perform their duties. 11 U.S.C. § 1103(b). In most cases, committees hire counsel to represent them.

27. Shortly after the Committee was appointed, Beasley pointed out that the Debtor was projecting rent payments to landlords (including some owned by Hudson) that were far more than the amounts historically paid by the Debtor. [Dkt no. 60, p. 3.] Estimates for future payroll were substantially more than historical costs. [Dkt no. 60, pp. 3-4.] The Debtor planned

to pay $10,000 per month to a company allegedly owned by Hudson for an energy drink. [Dkt no. 60, p. 4.] Beasley also expressed concern that the Debtor was paying various expenses incurred by Hudson's other entities, not just the Debtor. [Dkt no. 60, pp. 4-5.] Beasley also pointed out that the Debtor had transferred away its intellectual property shortly before filing for bankruptcy, and the transfer was likely avoidable. [Dkt no. 60, p. 5.] The Committee did not at that time hire counsel or a financial advisor.

28. In June 2016, the Debtor filed motions for authority to "assume" leases with one of Hudson's other entities, Waffle Plaza Properties, Inc. ("Waffle Plaza"). [Dkt nos. 99 and 102.] By assuming the leases, the Debtor not only would have been required to pay rent going forward, it also would have been required to "cure" defaults by paying past-due rent as an administrative claim of the estate. See 11 U.S.C. § 365(b). According to the motions, the past-due rent for one location was approximately $1.85 million and the past-due rent for the other was approximately $310,000. [Dkt no. 99, p. 3; Dkt no. 102, p. 3.] The Committee did not oppose or otherwise respond to the Debtor's request for approval of the transaction.

29. In July 2016, Beasley filed a motion for authority to conduct an examination of the Debtor pursuant to Federal Rule of Bankruptcy Procedure 2004. [Dkt no. 123.] The Court granted the motion, and ordered the Debtor to produce certain documents by August 8, 2016, and appear for an oral examination on August 15, 2016. [Dkt no. 131.]

30. In September 2016, Beasley filed a motion to hold the Debtor in contempt for failing to comply with the Court's order authorizing the 2004 exam.

[Dkt no. 168.] Evidence submitted in support of the motion showed that the Debtor had not produced any documents by the required deadline. [Dkt no. 168, p. 10.] At the oral examination, Hudson refused to answer some questions, and allegedly failed to provide meaningful answers to many others. [Dkt no. 168, p. 5.] The Court granted the motion and issued an OSC why the Debtor and Hudson should not be held in contempt. [Dkt no. 168.] The Committee did not take any position with respect to Hudson's failure to provide documents and answer questions.

THE DEBTOR'S PLAN FILED PRIOR TO APPOINTMENT OF THE TRUSTEE

31. On September 15, 2016, the Debtor filed its first proposed chapter 11 plan and accompanying disclosure statement. [Dkt nos. 171-172.] According to the disclosure statement, the Debtor intended to pay creditors in full over a period of 8 years. [Dkt no. 171, pp. 17-18.] However, because no independent financial advisor was involved in the process of developing the plan, the Debtor's projections were highly suspect.

32. The Debtor intended to reject the lease for the store located at 106 West Manchester and close the store. [Dkt no. 172, p. 24-25.] This would eliminate local competition for another Roscoe's store, located at 621 W. Manchester Blvd., which was operated by one of Hudson's other non-debtor entities. [Dkt no. 186, p. 4.] After he was appointed, the Trustee determined that it was not in the estate's best interests to close this location.

THE EXAMINER'S REPORT AND THE TRUSTEE'S APPOINTMENT

33. On September 21, 2016, the Examiner filed a status report. [Dkt no. 186.] The Examiner painted

a devastating picture of mismanagement, financial irregularities, insider dealing, and other problems that an active committee likely would have uncovered early on. The status report stated, among other things:

> (a) The Debtor had failed to fully cooperate with the Examiner, and obstructed the Examiner's investigation. [Dkt no. 186, p. 3.] For example, Hudson refused to consent to the Debtor's outside accountants providing the Examiner information and records held by them. [Dkt no. 186, p. 9.]
>
> (b) The Debtor's procedures did not conform to reasonable accounting norms, "or any semblance of responsible management." [Dkt no. 186, p. 2.] At least until the Debtor filed for bankruptcy, the Debtor did not maintain a general ledger and did not reconcile its bank account statements. [Dkt no. 186, p. 10.]
>
> (c) When the Examiner compared sales receipts for January through March 2016 (the 3 months prior to the Petition Date) to the bank statements, he "concluded that a material portion of the cash sales receipts for [the Debtor's] Hollywood and Pico stores during the early part of 2016 were not deposited into [a Debtor] bank account. These funds have not been accounted for by [the Debtor]." [Dkt no. 186, p. 11.]
>
> (d) The Examiner also identified at least $615,000 of transfers made by the Debtor to Hudson's other entities during the three months prior to the Petition Date, which were not disclosed by the Debtor in its schedules or

elsewhere. [Dkt no. 186, p. 18.] Even after the Petition Date, the Debtor failed to disclose transfers to insiders and related parties, including transfers of $150,000 to Waffle Plaza and $45,000 to Hudson himself. [Dkt no. 186, pp. 18-19.]

(e) The Examiner also identified over $40,000 in postpetition cash sale proceeds that had not been deposited into the Debtor's bank accounts. [Dkt no. 186, p. 19.] With Hudson's knowledge, the funds had been deposited into another entity's bank account. [Dkt no. 186, p. 19.]

(f) Even though the Debtor maintained multiple bank accounts prior to the Petition Date, "for all practical purposes only one bank account was included in the Quickbooks data file." [Dkt no. 186, p. 11.]

(g) The Debtor lacked a "formally developed, organized system of internal accounting controls." [Dkt no. 186, p. 2.] In fact, the Examiner said it would be a misnomer to suggest that the Debtor's operating and accounting procedures and policies actually constitute an internal control system. [Dkt no. 186, p. 9.]

(h) "The limited controls that [did] exist appear[ed] (by intentional design) to assure Hudson's personal access to [the Debtor's] cash funds while minimizing the accountability for same." [Dkt no. 186, p. 2.]

(i) For Hudson and the bookkeeper, "formalized accounting procedures [were] not central to their management culture. They favored

instead an environment that is the antithesis of accountability and transparency." [Dkt no. 186, p. 11.]

(j) The Debtor did not maintain inventory records. [Dkt no. 186, p. 2.]

(k) The profitability of each location was "somewhat uncertain due to material errors evident in the financial statements prepared by [the Debtor's] unskilled bookkeeping staff." [Dkt no. 186, p. 2.] For example, the Examiner was able to determine that the Debtor overstated its sales and net income in April, May and June 2016 by entering the same data into QuickBooks two or three times. [Dkt no. 186, p. 14.]

(l) The bookkeeping manager, who worked for the Debtor for over 25 years, was "remarkably incurious about specific . . . cash receipt and cash disbursement transactions and frequently deferred to Hudson for answers to questions about transactions recorded by her or under her supervision." [Dkt no. 186, p. 7.]

(m) There were a number of "observable irregularities involving management" relating to the chapter 11 case. "The shear scope of the identified irregularities suggests a high likelihood that further investigation would yield additional findings." [Dkt no. 186, p. 2.]

(n) The California State Board of Equalization ("SBE") audit found that the Debtor had underreported sales and sales tax collections for many years. [Dkt no. 186, p. 16.] Based on the audit, the SBE asserted a claim against the

estate for more than $2.1 million. [Dkt no. 186, p. 16.] The SBE "was openly critical of the Debtor's accounting practices and exposed a long-term pattern of significant shortcomings in [the Debtor's] historical recordkeeping and record retention practices." [Dkt no. 186, p. 16.]

(o) When it filed its schedules, the Debtor failed to disclose the existence of a then-pending complaint brought by the U.S. Department of Homeland Security, Immigration and Customs Enforcement. [Dkt no. 186, p. 16.] That matter was secretly settled postpetition, with the Debtor paying a settlement amount without obtaining approval of this Court. [Dkt no. 186, p. 16.] By law, court approval of any postpetition settlement was required. Fed. R. Bankr. P. 9019.

(p) The Debtor owned liquor licenses that were being used by non-debtors, including Hudson's entity operating a Roscoe's restaurant in Long Beach. [Dkt no. 186, p. 17.]

(q) The Debtor was "demonstrably wholly incapable of dispending its fiduciary obligations in this Chapter 11 case." [Dkt no. 186, p. 3.]

34. A case status conference had been scheduled for September 28, 2016. On September 27, 2016, after reading the Examiner's status report, the Court sua sponte issued an Order to Show Cause Re Appointment of Chapter 11 Trustee. [Dkt no. 193.] The Court set a hearing on the OSC for the next day. [*Id.*]

35. On September 28, 2016, the Court ordered the U.S. Trustee to appoint a chapter 11 trustee. [Dkt

no. 202.] The next day, the Court approved the appointment of Bradley D. Sharp as the chapter 11 trustee. [Dkt no. 206.] As noted in the Trustee's declaration filed in support of the U.S. Trustee's motion, the Trustee had more than twenty years' experience working with large and small troubled companies. [Dkt no. 204, p. 8.] The Trustee also had been appointed as a chapter 11 trustee in other cases that involved complex issues. [*Id.*]

36. To say this case was a mess when the Trustee was appointed is a significant understatement. Over the months leading to the Trustee's appointment, it was clear that the Debtor's management was untrustworthy and obstructed efforts of the Examiner and Beasley to uncover the truth about its financial affairs. Its financial reporting to the Court was substandard. Its books and record were a disaster. It had engaged in who-knows-how-many insider transactions that could need to be investigated and unraveled. It also had obviously transferred away its most valuable assets in an attempt to keep them out of reach of its creditors, putting the estate in a position of being unable to fund a reasonable plan and distribution to unsecured creditors.

37. With only a few days' warning, the Trustee was made the head of a company with hundreds of employees that had reportedly generated over $1.7 million of sales during August 2016, without an internal accountant he could trust and without knowing who in management he could depend on. He could not continue to depend on the Debtor's accounting department, and needed to immediately install his own staff to establish some internal controls and procedures until a longer-term solution could be found. By any

standard, this was clearly not an easy case where a court appoints a chapter 11 trustee to handle routine business management issues.

SOME OF THE WORK PERFORMED BY THE TRUSTEE

38. In operating chapter 11 cases, it is customary for a trustee to act quickly to employ counsel, communicate with parties involved in the case, recover monies held in the Debtor's bank accounts, and generally get things under control. There is usually a rush of activity within the first few weeks, but then things settle down as the trustee develops controls to ensure that the business is being run properly. Depending on the complexity of the business and trustworthiness of existing management, among other things, the trustee might install a CRO or similar professional to oversee operations and maintenance of books and records. Over the years, the Court has seen this play out in scores of cases.

39. To be sure, many things the Trustee did during this case are things a court would expect of any chapter 11 trustee in this type of case. For example, the Trustee communicated with the Examiner regarding his findings. [Dkt no. 597-1, p. 21.] He hired counsel to represent him in the case. [See Dkt nos. 236, 277.] He obtained continuances of pending matters so he would have time to properly evaluate them. [*See, e.g.*, Dkt nos. 240, 243, 246, 248.] As to some legal matters that could be resolved, they went forward. [*See, e.g.*, Dkt no. 261.] In the first few months, the Trustee evaluated the legal needs of the estate and hired attorneys and experts to serve those needs. [*See, e.g.*, Dkt nos. 338, 418, 441, 551.] He evaluated litigation that had been commenced by the Debtor prepetition

and resolved various discovery disputes pending in this case. [See Dkt no. 597- 1, pp. 20-21, 48.] He prepared monthly operating reports, including for the last period covered by the Debtor's operations. [See Dkt no. 597-1, pp. 13-14.] He took control of the Debtor's books and records, including by securing electronic records. [See Dkt no. 597-1, pp. 3, 12, 27.]

40. The Trustee also acted very quickly to identify, interview and retain an outside firm to manage the Debtor's restaurants. The Trustee's billing records reflect that this process started on the date of his appointment. [See Dkt no. 597-1, pp. 21-24.] Within a week, the Trustee's staff had conducted initial interviews with potential management companies. [See Dkt no. 597-1, p. 22.] Less than one month after he was appointed, the Trustee filed an application to employ The Next Idea [International] LLC ("TNI") to manage the restaurants and Triple Enterprises to provide business-related accounting and bookkeeping services. [Dkt nos. 262-263.] Once they were in place, the Trustee transitioned the accounting role to Triple Enterprises, and then communicated with them regarding management of the business. [See Dkt no. 597-1, pp. 5, 24-25, 27-28, 30.]

41. In the meantime, though, the Trustee and his staff worked to get a handle on the financial situation. The Trustee and/or his staff met with the Debtor's accountant, and spent time at the Debtor's office many times during the first month after the Trustee's appointment. [See Dkt no. 597-1, pp. 4, 16, 23-29.] In the Court's experience, while it is common for a trustee to visit the debtor's site when he or she is appointed, it is uncommon for a trustee (and especially the trustee's staff) to need to spend so much

time on site. The Trustee established accurate tax accounting with respect to 1099's and payroll taxes. [See Dkt no. 597-1, p. 6.] The Trustee also established new cash management controls as recommended by the Examiner. [See Dkt no. 597-1, pp. 27-29.]

42. The Trustee's staff spent substantial time analyzing bank accounts and deposits, performing work that ordinarily would be done by the Debtor's existing personnel but which, in this case, needed to be handled by the Trustee. [See Dkt no. 597-1, pp. 5, 24-25, 27-32.] He and his staff worked to install a new point of sale system to better handle and track credit card transactions. [See Dkt no. 597-1, pp. 31-33.] He and his staff worked to fix internal controls relating to, among other things, the proper handling of cash. [See Dkt no. 597-1, pp. 29-32.] They established cash forecasting processes and actual-to-budget analyses, and later transitioned the budget process to a new operations accountant and operating manager. [See Dkt no. 597-1, pp. 10- 12, 30.]

43. The Trustee was also thrust into an ongoing audit by the IRS, which was a significant issue in the case. The Trustee and his staff worked to obtained required information to quantify the amount of taxes due. The Trustee communicated with the IRS and attempted to locate records responsive to the IRS's requests. [See Dkt no. 597, p. 12; Dkt no. 597-1, pp. 16-17, 27; Dkt no. 1011, p. 32.]

44. Throughout his tenure the Trustee continued to deal with tax issues caused by the Debtor's mismanagement. The Trustee and his staff researched the Debtor's records, and helped reconstruct the Debtor's financial records, to address the Debtor's history of underreporting income, payroll and sales

taxes. [See Dkt no. 808, pp. 20, 29-33; Dkt no. 1011, pp. 12, 28-32; Dkt 14 no. 1134, pp. 10, 22, 27-29.] The extent of the tax problem is exemplified by, among other things, the SBE's proof of claim, in which the SBE asserted a claim for unpaid taxes incurred from 2001 through 2015. [POC 34, p. 4.] Other tax claims included one filed by the IRS for more than $10 million and one filed by the Franchise Tax Board for approximately $3.97 million. [See POCs 2, 32.]

45. With respect to the IRS's claim asserted against the estate: (a) The IRS filed its original proof of claim in April 2016 for $515,198.71. [POC 2-1.] The documents attached to the proof of claim reflect that the IRS used placeholders of $46,510 for 2010, 2011, 2014 and 2015 income taxes (years in which the Debtor had failed to file income tax returns). [*Id.* at p. 4.] The proof of claim also included about $240,000 for FICA taxes owed for the first quarter of 2016. [*Id.*] (b) The IRS amended its proof of claim in June 2016 to omit the FICA taxes. [POC 2-2.] (c) The IRS amended its proof of claim on November 1, 2016, asserting a claim for $277,662.71. [POC 2-3.] The IRS continued to use the $46,510 placeholders for 2010, 2011, 2014 and 2015. [*Id.* at 4.] (d) The IRS amended its proof of claim on November 8, 2016, asserting a claim for $10,239,106.71. [POC 2-4.] The amount stated for each of the 2012 and 2013 tax years was $4,981,722.00. [*Id.* at p. 4.] (e) The IRS amended its proof of claim on May 21, 2018, asserting a claim for $10,608,245.33. [POC 2-5.] The reason for the increase in the claim amount was that the Debtor had failed to pay FICA taxes. [*See id.* at p. 4.]

46. With respect to the federal and state taxes, the Trustee's accountants analyzed, among other

things, tax deductions and creditors that could be properly claimed by the Debtor, and included data regarding such deductions and credits in its analyses. [Dkt no. 813, pp. 4-5, 12-15; dkt no. 1002, pp. 4-6; dkt no. 1133, pp. 9-10.] The accountants also prepared missing tax returns or amended prior tax returns, and spent considerable time dealing with the IRS' audit. [Dkt no. 813, pp. 3, 7-15; dkt no. 1002, pp. 3-4, 6, 8; dkt no. 1133, pp. 4-9.]

47. The Trustee also had to deal with some personnel issues. Of particular note, the Trustee was involved in discussions which led to the replacement of Hudson's daughter as head of human resources and her separation from the Debtor. [See Dkt no. 808, pp. 35-36, 50-51.]

48. The Trustee also was able to efficiently resolve some litigation matters in which the Debtor was involved when the Trustee was appointed. For example, within a few months of his appointment, the Trustee settled claims the Debtor asserted against State Compensation Insurance Fund, CompWest Insurance Company, and Employers Compensation Insurance Company based on their alleged mishandling of workers' compensation insurance claims made against the Debtor. [Dkt nos. 468, 547.] The estate received approximately $775,000 from those settlements. [Dkt no. 468, p. 2.]

COMMITTEE'S INVOLVEMENT AFTER THE TRUSTEE WAS APPOINTED

49. The Committee hired counsel after the Trustee was appointed. The Committee's counsel commenced services on November 1, 2016. [Dkt no. 350, p. 1.] This was about one week after the Trustee filed his applications to employ TNI and Triple Enterprises

to take over management and accounting functions that were previously controlled by Hudson. On November 22, 2016, the Committee filed an application to employ counsel. [Dkt no. 307.] Sam White, the principal of Clifton Capital, executed the application as the Committee's chair. [Dkt no. 307, p. 6.]

50. In March 2017, the Committee filed an application for authority to employ a financial adviser. [Dkt no. 553.] The primary purpose of the advisor's employment was to advise the Committee in connection with the formulation of a plan, exit financing, or offers from potential purchasers or investors. [See Dkt no. 553, pp. 2-3.]

51. The Committee eventually partnered with Hudson to propose a chapter 11 plan that enabled Hudson to retain his ownership of the Debtor and ensures payment to creditors in full.

52. The Trustee met, either in person or telephonically, with the committee and/or its professionals on November 29, 2016, January 21, 2017, February 22, 2017, March 8, 2017, March 22, 2017, April 7, 2017, May 25, 2017, August 3, 2017, November 6, 2017, February 21, 2018, and May 7-8, 2018. [Dkt no. 597-1, p. 45; Dkt no. 808, pp. 47-49; Dkt no. 1011, pp. 32, 41; Dkt no. 1134, p. 23, 37.] The Trustee provided information that would help the Committee's professionals analyze the Debtor's finances, and communicated with them regarding ongoing operations (such as personnel issues and marketing plans) and transition issues. [See Dkt no. 808, pp. 47-50; Dkt no. 1011, pp. 32, 41-42; Dkt no. 1134, p. 23, 37.] The Trustee also provided comments to financial exhibits that the Committee intended to attach to its disclosure statement. [Dkt no. 1011, p. 25.]

TRUSTEE'S REJECTION OF DV MARKETING'S CONTRACT AND DISALLOWANCE OF ITS ALLEGED CLAIM

53. Besides hiring TNI and Triple Enterprises to take over the management and accounting duties, the Trustee was required to take other steps to separate the estate from persons connected to Hudson and his other entities. For example, the Trustee learned that the Debtor had entered into an agreement with DV Marketing ("DV"), who was purportedly the "exclusive" inhouse marketing company for the Debtor. [Dkt no. 450, p. 14.] DV's principal refused to meet with TNI and refused to provide the Trustee login information for all of the Debtor's social media accounts. [Dkt no. 450, p. 9.] She also reportedly instructed vendors like GrubHub and Postmates to pay someone other than the Trustee for food purchased from the Debtor's stores. [Dkt no. 450, p. 10.] The Trustee rejected the Debtor's contract with DV, and was forced to seek discovery from GrubHub and Postmates to obtain information that DV refused to provide. [Dkt nos. 450, 462, 464.]

54. Subsequently, the Trustee sought to expand the scope of TNI's employment to include marketing services. [Dkt no. 658.] The Committee opposed the Trustee's request and argued, among other things, that the Trustee should not launch a new website for the Debtor that would compete with the one controlled by DV and Hudson. [Dkt no. 666.] The Court overruled the objection and granted the Trustee's motion. [Dkt no. 673.]

55. In September 2017, the Trustee objected to DV's alleged claim. [Dkt no. 738.] Although DV filed

an opposition, its counsel failed to appear at the hearing. [Dkt nos. 780, 905.] The Trustee's objection was sustained and DV's alleged claim was disallowed. [Dkt no. 905.]

56. DV's refusal to cooperate was so extreme that the Trustee was forced to file a complaint seeking "turnover" of the Debtor's domain name, website and social media accounts. *Sharp v. Vara*, Adv. No. 2:17-ap-01573-BB. In March 2018, a default judgment was entered against DV. [AP Dkt no. 19.]

TRUSTEE'S AGREEMENT FOR SUBORDINATION OF CLAIMS ASSERTED BY HUDSON'S OTHER ENTITIES

57. Given the amount of self-dealing and the condition of the Debtor's books and records, it would have been appropriate for the Trustee and his counsel to investigate and, where appropriate, object to claims asserted by persons and entities affiliated with Hudson, among others. Very likely, that would have required the estate to incur hundreds of thousands of dollars of fees and expenses in litigation. Instead, knowing that the Committee and Hudson wanted to formulate a plan under which Hudson would retain ownership and control, the Trustee negotiated and entered into stipulations which subordinated certain insider claims to those of third party general unsecured creditors.

58. Hudson-affiliate Waffle Plaza Properties, Inc., filed proofs of claims asserting claims in excess of $2.1 million. [POCs 39-40.] Hudson-affiliate Freeway Foods, Inc., filed a proof of claim for $750,000. [POC 41.] Hudson-affiliate Shoreline Foods, Inc., filed a proof of claim for $1.5 million. [POC 42] Roscoe's IP filed a proof of claim for $22,500. [POC 43.]

59. In August 2017, the Trustee entered into a stipulation that assured that those entities would not be paid before non-insider creditors, while also preserving two of four store leases that were critical to the estate's continued operations. [Dkt no. 698.] Under the stipulation, the Hudson affiliates agreed that their claims would be subordinated to and paid only after all allowed claims against the estate are paid in full, and the estate was not required to pay any amounts required to cure defaults. [Dkt no. 698, pp. 3-4.]

60. The subordination agreement was a creative way to solve the obvious problem that existed with respect to the Debtor's prior motion for authority to assume its real property leases in Hollywood and on Manchester Avenue. The landlords (owned by Hudson) claimed to be owed a substantial amount of back rent that would have to be "cured" upon assumption of the leases. 11 U.S.C. § 365(b)(1). The subordination agreement allowed the Trustee to assume those leases and avoid having to litigate regarding the validity and amount of the alleged claims for back rent. The two leases were assumed as soon as the subordination agreement was approved by the Court. [See Dkt nos. 713, 716.]

61. The Trustee also reached a similar agreement with two members of the Committee, including Clifton Capital, alleviating the need for the estate to incur fees litigating further over the allowance of their alleged claims.

TRUSTEE'S LITIGATION WITH CLIFTON CAPITAL, AND SUBORDINATION OF CLIFTON CAPITAL'S CLAIM

62. In its schedule of creditors who had unsecured claims, the Debtor stated that Clifton Capital Group, LLC, was a creditor and that it was owed $4,165,000. [Dkt no. 38, p. 17.] Based on that alleged claim, Clifton Capital was appointed to the Committee.

63. In February 2017, the Trustee filed a motion for authority to conduct a Rule 2004 examination of Clifton Capital and its principal, Sam White. [Dkt no. 472.] Clifton Capital's claim was based on services allegedly provided with respect to Enterprise Zone Tax Credits; Clifton Capital also allegedly assisted the Debtor with negotiations with the IRS, the FTB and the BOE regarding tax-related disputes. [Dkt no. 472, p. 8.] In the Trustee's view, the information and documents provided by Clifton Capital relating to its alleged claim was inadequate. [Dkt no. 472, p. 10.] The Court granted the Trustee's motion. [Dkt no. 478.] At the same time, the Court granted the Trustee's motion for authority to conduct a Rule 2004 examination of an accountant that had provided services to the Debtor ("Sadd"). [Dkt no. 479.]

64. Mr. White appeared at the oral examination, but failed to bring any documents with him. [Dkt no. 763, p. 22.] When the Trustee's counsel demanded that Clifton Capital comply, Clifton Capital's counsel said that he needed another week to respond. [Dkt no. 763, pp. 23-25.] When no response was received, the Trustee's counsel followed up again. [Dkt no. 763, p. 25.] Clifton Capital refused to provide the vast majority of documents required. [*Id.*]

65. Unlike Clifton Capital, Sadd complied with the Court's order requiring him to produce documents.

[Dkt no. 763, p. 26.] According to the Trustee, the documents produced by Sadd contradicted the representations made by Clifton Capital and Mr. White. [Dkt no. 763, pp. 10, 13-14, 16.]

66. In October 2017, the Trustee filed an objection to Clifton Capital's claim. [Dkt no. 763.] According to the Trustee, although Clifton Capital claimed that the Debtor had agreed to pay Clifton Capital a flat fee for each employee approved with a voucher certificate for the California Enterprise Zone Tax Credit program, and although Mr. White testified that Clifton Capital had not been paid anything for his work, documents obtained by the Trustee from Sadd suggested that the alleged flat fee was highly unreasonable and that Clifton Capital had already been paid for the same work on an hourly fee basis. [*Id.*]

67. Clifton Capital opposed the Trustee's objection. [Dkt no. 789.] According to Clifton Capital, its contract with the Debtor was valid and the rate was reasonable, it performed the work required by the contract, and it had not been paid. [*Id.*]

68. Even though it would have eliminated an alleged $4+ million liability, the disallowance of Clifton Capital's claim might have had a substantial impact on Hudson's ability to confirm a plan to his liking. In fact, notwithstanding the fact that the Trustee had filed objections to a number of claims around the same time, Clifton Capital accused the Trustee of objecting to its claim at that time in order to derail Hudson's and the Committee's efforts to develop a plan. [Dkt no. 789, pp. 4-5.]

69. Clifton Capital contends that its principal (Mr. White) is not really close with Hudson. At the

hearing on the Trustee's objection, addressing Clifton Capital's attorney, the Court commented that it really looks more like your client or the principal of your client is maybe perhaps the good buddy of the principal of the debtor and he is – this is an attempt by the principal of the debtor to deliver significant value to his good buddy. And whether or not any of it is supposed to come back to him, I don't know, but the facts and circumstances are just suspicious because it's the – why would anybody agree to pay $8,215 per application when that's far in excess of any benefit they would obtain from this. [Dkt no. 846, p. 8.] Technically Clifton Capital's counsel did not deny this; instead, she stated that the Trustee had not presented evidence that they were "good buddies." [Dkt no. 846, p. 8.] (The Court was not making any findings at that time regarding the relationship, if any, between Clifton Capital and Mr. White, on the one hand, and Hudson.)

70. In the Court's view, the Trustee's papers made a strong case that Clifton Capital's alleged claim was suspicious. The Court determined that an evidentiary hearing was needed. [Dkt no. 846, pp. 14-15.] In the meantime, the parties could conduct discovery. [*Id.*]

71. After the hearing, counsel for Hudson – not Clifton Capital – requested a transcript of the hearing. [Dkt no. 833.]

72. Consistent with his approach to potentially-objectionable claims asserted by Hudson's other entities, and in light of the terms of a proposed plan then-recently filed by Hudson and the Committee, the Trustee made the economic decision that it would be better to stipulate to allowance of Clifton Capital's

claim than to litigate, as long as Clifton Capital's alleged claim was subordinated to all other general unsecured claims and the Trustee still could object if Hudson's plan was not confirmed. In February 2018, the Trustee and Clifton Capital entered into a stipulation pursuant to which Clifton Capital's claim was subordinated to, and to paid only after, all allowed secured and unsecured claims and approved administrative expenses are paid in full under the then-proposed plan. [Dkt no. 946, p. 2.] The Trustee also reserved the right to re-object to Clifton Capital's claim if Hudson's proposed plan was not confirmed. [Dkt no. 946, p. 3.] The Court approved the stipulation. [Dkt no. 949.]

THE TRUSTEE'S TOLLING AGREEMENTS WITH THE DEBTOR AND CERTAIN OTHER PARTIES

73. Generally, the deadline for a chapter 11 trustee to file complaints to avoid preferential and fraudulent transfers is two years after the petition date. 11 U.S.C. § 546(a)(1). Thus, unless the time was tolled, the deadline for the Trustee to file such actions was March 25, 2018.

74. In March 2018, the Trustee made the prudent decision to enter into tolling agreements with potential defendants rather than initiate litigation. The Trustee entered into tolling agreements with ten of Hudson's affiliates, Clifton Capital, Choice Foods, and Sergio Borgognone. [Dkt nos. 980, 985, 989, 995.]

THE TRUSTEE'S COMPLAINT AGAINST ROSCOE'S IP

75. The Trustee recognized that a successful sale or reorganization required the Trustee to avoid the fraudulent transfer of the Debtor's intellectual property to Roscoe's IP.

76. On September 27, 2016 (the date on which the Court issued its OSC re appointment of a trustee), Beasley filed a motion for an order granting him standing to file a complaint on behalf of the estate against Roscoe's IP. [Dkt no. 197.] Such a motion was appropriate because chapter 11 debtors generally do not sue their principals and affiliates. Unless a trustee has been appointed, one of the major roles of a creditors' committee often is to investigate and pursue avoiding power claims against the debtor's insiders and affiliates. The Committee did not do so in this case. Due to the appointment of the Trustee, Beasley's motion was denied without prejudice. [Dkt no. 269.]

77. The Debtor's transfer of its intellectual property to Roscoe's IP clearly was an avoidable fraudulent transfer, in that the purpose of the transfer was to keep the assets out of reach of creditors. Soon after his appointment, in a commendable attempt to avoid litigation, the Trustee requested that Roscoe's IP return the assets to the estate. [AP Dkt no. 28, p. 10.] Hudson claimed to be considering the Trustee's request, and asked that the Trustee delay filing a complaint. [*Id.*] Ultimately, though, Hudson never agreed to return the assets despite the Trustee's efforts to reach an informal agreement achieving this result. [*Id.*]

78. On January 3, 2017 (a few months after he was appointed), the Trustee filed a complaint against Roscoe's IP, primarily seeking to avoid the transfer of the Debtor's intellectual property as a fraudulent transfer. *Sharp v. Roscoe's Intellectual Properties, LLC*, Adv. No. 2:17- ap-01001-BB (the "Adversary").

79. Despite Hudson's prior admissions, Roscoe's IP filed an answer and objected to the relief sought by the Trustee. [AP Dkt no. 12.]

80. The Trustee promptly filed a motion for summary judgment. [AP Dkt no. 19.] Roscoe's IP opposed the motion. [AP Dkt no. 36.]

81. As noted by the Court in its memorandum decision, because a court may not grant a summary judgment motion where there is a genuine issue of fact, "it is a rare case in which a court may grant summary judgment under an actual fraud fraudulent transfer theory, but this is one such case." [AP Dkt no. 60, p. 2.] As a result, the Court granted summary judgment against Roscoe's IP on the Trustee's claim for avoidance of the transfer. [AP Dkt no. 63.]

82. In September 2017, the Trustee entered into a stipulation with Hudson, giving him a certain amount of time to file and confirm a plan before the Trustee proceeded with an alternative. [Dkt no. 722.] As part of the stipulation, Roscoe's IP agreed to not appeal the judgment avoiding the fraudulent transfer of the Debtor's intellectual property to Roscoe's IP. [Dkt no. 722, p. 3.]

RECONSTRUCTION OF THE DEBTOR'S BOOKS AND RECORDS FOR 2010-2015

83. The Trustee also recognized that a successful sale or reorganization of the Debtor required the Trustee to reconstruct the Debtor's books and records for years prior to the Petition Date. [See Dkt no. 640, p. 4.] The Trustee's staff gathered historical bank statements and other information, and provided documents and information to Triple Enterprises, and

worked with Triple Enterprises to assist in the process. [See Dkt no. 597-1, pp. 10-11, 25-27, 39; Dkt no. 808, pp. 28-32.] This was needed for at least two reasons.

84. First, reconstructing the books and records would enable the Trustee to prepare the Debtor's tax returns for 2010 through 2015. [Dkt no. 640, pp. 3-4.] That, in turn, would allow the Trustee to determine, or at least estimate, the estate's true tax liabilities. [Dkt no. 640, p. 4.]

85. Second, information in the reconstructed books and records would be needed to show potential purchasers a true historical financial history. Representatives for potential buyers started contacting the Trustee the day he was appointed, and continued to communicate with the Trustee from time to time. [Dkt no. 597-1, p. 44; Dkt no. 808, p. 23.] In fact, a potential buyer continued to communicate with the Trustee after the plan was confirmed and Hudson failed to perform his obligations under the plan. [Dkt no. 1134, pp. 25, 38.]

86. Reconstructing the books and records also had the benefit of uncovering previously unknown bank accounts. [Dkt no. 640, p. 4.] The Trustee filed numerous motions seeking authority to subpoena banks for records. [Dkt nos. 504-510, 585, 644-646.]

RESOLUTION OF CERTAIN OTHER ISSUES CAUSED BY THE DEBTOR

87. The Trustee also efficiently accomplished other tasks that cleaned up messes left behind by the Debtor. For example, one of the Debtor's most important stores, located on Pico Boulevard, generated approximately $4 million in gross revenue annually.

[Dkt no. 697, pp. 9-10.] That location was operating under an oral, month-to-month lease, which could be pulled by the landlord at any time. [Dkt no. 697, p. 9.] The Trustee negotiated a new written lease for 12 months with an option to extend the term for 6 months. [Dkt no. 697, pp. 9, 12-67.]

88. Also, the Trustee rejected alleged, previously-undisclosed oral agreements between the Debtor and employees that allowed the employees to design and market merchandise using the Debtor's trademark and related intellectual property without having to pay any royalties. [Dkt nos. 470, 566.]

HUDSON AND THE COMMITTEE'S JOINT PLAN

89. Within a year, the Trustee, his staff and his professionals had accomplished the Trustee's goal of getting the estate in a position to start moving forward with a potential sale or chapter 11 plan. Hudson obviously wanted to retain control of the company. In September 2017, the Trustee entered into a stipulation with Hudson, giving him a certain amount of time to file and confirm a plan before the Trustee proceeded with an alternative. [Dkt no. 722.] As part of the stipulation, Roscoe's IP agreed to not appeal the judgment avoiding the fraudulent transfer of the Debtor's intellectual property to Roscoe's IP. [Dkt no. 722, p. 3.]

90. The stipulation required Hudson to move quickly to propose a meaningful, confirmable plan. The Trustee agreed to provide Hudson estimates of all claims asserted in the case. [Dkt no. 722, p. 2.] Within 60 days after receiving those estimates, Hudson was required to file a proposed plan and disclosure statement. [Dkt no. 722, p. 3.] Hudson was required to obtain approval of the disclosure statement within 45 days after it was filed with the Court. [*Id.*] Hudson

was then required to obtain an order confirming the plan within 45 days after the hearing on the disclosure statement. [*Id.*] These tight time frames could be extended in certain circumstances. [*Id.*] While the agreement was pending, the Trustee agreed not to initiate any proceedings to sell the estate's assets or file a competing plan. [*Id.*] If Hudson failed to comply with the deadlines, the Trustee would have the option to market and sell the estate's assets or proceed as he felt appropriate. [*Id.*]

91. In January 2018, Hudson and the Committee filed a joint plan and disclosure statement. [Dkt nos. 911, 912.]

92. Generally, the proposed plan provided for the creation of a "Plan Trust" with a trustee (the "Plan Trustee") who would collect funds and distribute the funds to creditors. [Dkt no. 911, pp. 59-65.] The Plan Trust would be funded by (a) a cash contribution from Hudson of $10 million "less Excess Cash on Hand," (b) monthly payments of about $115,000 to be made by the reorganized debtor, with the potential for more depending on cash flow, and (c) monthly payments of about $133,333 by some of Hudson's other entities. [Dkt no. 911, pp. 9, 45-47.]

93. Obligations to the Plan Trust under the plan would be secured by a "Collateral Package" worth more than $39.1 million, consisting of the Debtor's intellectual property and real estate owned by Hudson's other entities. [Dkt no. 911, pp. 9, 47-50.] Hudson and the Committee expected that all claims would be paid in full in less than six years. [Dkt no. 911, p. 9.]

94. In terms of future management, the proposed plan provided that the reorganized debtor

would be managed by a third party selected by Hudson with the approval of the Committee and the Plan Trustee. [Dkt no. 911, pp. 9, 57-58.]

95. In March 2018, Hudson and the Committee filed a first amended plan and disclosure statement that made some modifications to the originals. [Dkt nos. 968-969.] The Court approved the disclosure statement. [Dkt no. 977.]

96. In May 2018, Hudson and the Committee filed a motion for approval of some nonmaterial modifications to the proposed plan. [Dkt no. 1058.] The proposed plan provided that the Committee could consent to subordinating the Plan Trust's lien against one or more properties in the Collateral Package to allow Hudson to obtain a loan secured by the property (or properties) for the purpose of funding his initial $10 million contribution. [Dkt no. 969, p. 36.] Hudson and the Committee sought to, among other things, expressly incorporate the terms required by Hudson's lender, SMS Financial, LLC ("SMS"), into the plan. [Dkt no. 1058, pp. 9-13.]

97. In support of confirmation, Hudson executed a declaration in which he stated the plan was proposed "to ensure 100% payment to creditors as quickly as possible." [Dkt no. 1060, p. 2.] In another declaration, Mr. White also testified that the plan "was proposed to move this case forward and to ensure 100% payment to creditors as quickly as possible." [Dkt no. 1061, p. 2.]

98. On July 3, 2018, the Court entered an order confirming the second amended plan. [Dkt no. 1082.]

99. Under the confirmed plan, whether through regular payments or after the Plan Trustee forecloses

on the Collateral Package, creditors (including Clifton Capital) will be paid in full. This is the case regardless of the outcome of Clifton Capital's objection to the Trustee's Final Fee Application.

100. Clifton Capital's claim is part of Class 11 under the confirmed plan. [See Dkt no. 968, pp. 47-48.] The disclosure statement estimated that Class 11 will begin receiving quarterly payments starting in the second quarter of 2022, and receive final payments in 2024. [Dkt no. 968, pp. 48, 170.] Based on projections attached to the disclosure statement, even if the Trustee were to return $396,867.21 to the Plan Trustee, payments to Clifton Capital would not commence earlier. [Dkt no. 968, pp. 170.] The Plan Trustee has not filed updated projections, so the Court is unable to determine whether post-confirmation events have affected the date on which payments to Class 11 may commence.

HUDSON'S IMMEDIATE FAILURE TO FULLY COMPLY WITH THE PLAN

101. The Effective Date of the confirmed plan was scheduled to occur on August 2, 2018. [Dkt no. 1096, p. 3.] As noted above, the Plan required Hudson to contribute $10 million on the Effective Date. [*Id.*]

102. Upon the close of his loan from SMS, Hudson could contribute only $8 million. [Dkt no. 1096, p. 3.] He apparently did not have the funds needed to pay the other $2 million he had agreed to pay. On August 2, 2018, various parties, including the Trustee, stipulated to extend the Effective Date by 30 days to give Hudson time to address the shortfall. [Dkt no. 1096.] In its order, the Court extended the Effective Date 15 days and set a prompt status conference. [Dkt no. 1097.]

103. On August 7, 2018, Hudson and the Committee reported that they had agreed that the shortfall would be paid as follows: (a) $50,000 would be paid by Hudson by January 3, 2019; (b) $975,000 would be paid by Hudson 10 months after the Effective Date; and (c) $975,000 would be paid by Hudson 12 months after the Effective Date. [Dkt no. 1099, pp. 4-5.] Hudson's failure to make any of these payments would constitute a default as that term is defined in Section IV.D. of the plan. [Dkt no. 1099, p. 5.]

104. On September 10, 2018, the Court entered an order approving this modification of the confirmed plan. [Dkt no. 1114.] As reflected in the order, another one of Hudson's entities, Cactus Ranch Properties, LLC ("Cactus"), guaranteed the shortfall and granted first-priority liens on real property located in Arizona. [Dkt no. 1114, p. 3.]

105. The Effective Date of the plan occurred on September 14, 2018.

106. Hudson failed to make the initial $50,000 on time. [Dkt no. 1251, p. 3.] After the Plan Trustee made demand for payment, Hudson paid the $50,000 on or about January 28, 2019 (over three weeks late). [Dkt no. 1252.]

107. Hudson did not make the second payment ($975,000) on July 15, 2019. [Dkt no. 1299, p. 3.] According to Hudson's status report filed on July 29, 2019, Hudson was negotiating with a new lender which would loan sufficient funds to pay off SMS and provide funds to pay the shortfall. [Dkt no. 1301.]

108. In September 2019, Hudson reported that a letter of intent from a "credible and capable lender"

should be received by September 11, 2019. [Dkt no. 1313.]

109. Hudson did not make the third payment ($975,000) on September 16, 2019. [Dkt no. 1334, p. 2.]

110. As recently as October 9, 2020, the Plan Trustee reported that Hudson still had not made either the second or third shortfall payment. [Dkt no. 1400, pp. 2-4.]

TRUSTEE'S FIRST INTERIM FEE APPLICATION

111. In mid-May 2017, the Trustee and various estate professionals filed interim fee applications. The Trustee's first interim fee application covered services rendered by the Trustee and his staff through March 31, 2017. [Dkt no. 597.] As set forth in the application:

> (a) The application included time records for employees of Development Specialists, Inc. ("DSI"), who assisted the Trustee in the performance of his duties in the case. [Dkt no. 597, pp. 1-2.]
>
> (b) On an interim basis, the Trustee requested that the Court award him fees of $252,997.09 and costs of $2,543.21. [Dkt no. 597, p. 9.]
>
> (c) Pages 10 through 13 contained brief summaries, broken down by activity code, of the services rendered by the Trustee and his staff during the first interim period. [Dkt no. 597, pp. 10-13.]

(d) By far, most of the services rendered by the Trustee and his staff during the first interim period related to managing the Debtor's operations. The Trustee recognized the issues that needed to be immediately addressed upon his appointment, and he and his staff therefore spent significant time understanding and asserting control over the operations. [Dkt no. 597, p. 12.] They implemented new cash controls, a point of sale system, and improved financial reporting. [Dkt no. 597, p. 13.] The Trustee and his staff devoted 537.2 hours in this category. [Dkt no. 597, p. 13.] Detailed billing records describing the services rendered in this category were attached to the application. [Dkt no. 597-1, pp. 21-44.]

(e) In the "Business Analysis" category, the Trustee and his staff incurred 94.1 hours analyzing books and records, discussing the case with the Examiner, preparing forecasts, and providing related services. [Dkt no. 597, p. 11.] Detailed billing records describing the services rendered in this category were attached to the application. [Dkt no. 597-1, pp. 8-12.] (f) In the "Accounting/Auditing" category, the Trustee and his staff incurred 60.2 hours gaining control of the Debtor's books and records and managing the accounting for the Debtor's business operations as well as the estate's expenses, and transitioning those services to Triple Enterprises. [Dkt no. 597, p. 10.] Detailed billing records describing the services rendered in this category were attached to the application. [Dkt no. 597-1, pp. 3-8.] (g) Overall, the Trustee and his staff provided 861.1 hours of services during

> the first interim period. [Dkt no. 597, pp. 14-15.] The Trustee personally spent 238.7 hours working on the case during the first interim period. [Dkt no. 597, p. 14.] (h) Most often, a chapter 11 trustee can get along with using mostly paralegallevel staff to help perform the duties that a trustee is required to provide. See 11 U.S.C. § 1106. In this case, though, because the management and accounting situation was such a disaster when the Trustee was appointed, the Trustee required the assistance of more experienced personnel. The Trustee's application states that services provided by DSI employees Eric Held (258.2 hours), Andrew Park (269.1 hours) and Matt Sorenson (27.6) were included in the fee application. [Dkt no. 597, p. 14.] Their resumes, and resumes for others who provided services, were attached to the application. [Dkt no. 597-1, pp. 56-57, 59.] (i) If measured at hourly billing rates charged by DSI to its non-bankruptcy clients, the value of the services rendered by the Trustee and his staff during the first interim period was $347,741.50. [Dkt no. 597, p. 15.] However, pursuant to § 326(a), the Trustee requested compensation in the amount of $252,997.09. [Dkt no. 597, p. 16.]

112. In total, eight fee applications were filed in mid-May 2017. [Dkt nos. 586, 589, 590, 593, 597, 598, 599, 604.]

113. The only objection was filed by the Committee, which objected to the applications filed by the Trustee, his general bankruptcy counsel, and two other professionals working for the Trustee. [Dkt no.

613.] As to the Trustee, the Committee's primary argument was that the Court should not approve fees for services that were rendered by DSI personnel because DSI was not separately employed under § 327. [Dkt no. 613, pp. 10-13.]

114. The Court overruled the Committee's objection and, on an interim basis, approved the Trustee's fees and costs in full. [Dkt no. 637, p. 3.]

TRUSTEE'S SECOND INTERIM FEE APPLICATION

115. In November 2017, the Trustee and various estate professionals filed interim fee applications. The Trustee's second interim fee application covered services rendered by the Trustee and his staff from April 1 through September 30, 2017. [Dkt no. 808.] As set forth in the application: (a) The application included time records for employees of DSI, who assisted the Trustee in the performance of his duties in the case. [Dkt no. 808, pp. 1-2.] (b) On an interim basis, the Trustee requested that the Court award him fees of $271,187.27 and costs of $1,367.60. [Dkt no. 808, p. 9, 15.] (c) Combined with the $252,997.09 of fees paid to the Trustee for the first interim period, the total fees paid to the Trustee would be $524,184.36. This was the amount allowable under § 326(a) of the Code. [Dkt no. 808, p. 9.] This would still be less than the $566,133.00 of fees incurred by the Trustee and his staff if their fees were based solely on hourly rates charged by DSI to its non-bankruptcy clients. [*Id.*] (d) Pages 10 through 13 contained brief summaries, broken down by activity code, of the services rendered by the Trustee and his staff during the second interim period. [Dkt no. 808, pp. 10-13.] (e) A substantial amount of work performed by the Trustee

and his staff continued to relate to managing the Debtor's operations. During the second interim period, they spent 106.5 hours supervising operations. [Dkt no. 808, p. 12.] They had frequent discussions with TNI and Triple Enterprises. The Trustee approved invoices for payment and approved any significant expenditure before it was incurred. [*Id.*] Detailed billing records describing the services rendered in this category were attached to the application. [Dkt no. 808, pp. 37-47.] (f) Other general categories in which the Trustee and his staff spent significant time during the second interim period included business analysis (88.5 hours), claims analysis and objections (67.9 hours), tax issues (including services relating to the IRS audit) (62.0 hours), and communications with the Committee (38.1 hours). [Dkt no. 808, pp. 11-12.] Detailed billing records describing the services rendered in these and all other categories were attached to the application. [Dkt no. 808, pp. 18-53.] (g) Overall, the Trustee and his staff provided 455.7 hours of services during the second interim period. [Dkt no. 808, p. 13.] The Trustee personally spent 270.3 hours working on the case during the second interim period. [*Id.*] (h) As one would expect, once TNI and Triple Enterprises were in place, the Trustee's more experienced staff members needed to spent less time on the case. Whereas Messrs. Held and Sorenson collectively billed 285.8 hours of time during the first interim period, they billed only 19.5 hours to this case during the second interim period. [Dkt no. 808, p. 13.]

116. No objection to the Trustee's application was filed.

117. On an interim basis, the Court approved the Trustee's fees and costs in full. [Dkt no. 862.]

TRUSTEE'S THIRD INTERIM FEE APPLICATION

118. In April 2018, shortly after the Court approved Hudson and the Committee's disclosure statement, the Trustee and various estate professionals filed interim fee applications. The Trustee's third interim fee application covered services rendered by the Trustee and his staff from October 1, 2017, through February 28, 2018. [Dkt no. 1011.] As set forth in the application: (a) The application included time records for employees of DSI, who assisted the Trustee in the performance of his duties in the case. [Dkt no. 1011, pp. 1-2.] (b) On an interim basis, the Trustee requested that the Court award him fees of $286,476.88 and costs of $611.86. [Dkt no. 1011, pp. 9, 15.] (c) Combined with the $524,184.36 of fees paid to the Trustee for the first two interim periods, the total fees paid to the Trustee would be $810,661.24. This was the amount allowable under § 326(a) of the Code. [Dkt no. 1011, p. 9.] For the first time in the case, the payments to the Trustee would exceed the fees incurred by the Trustee and his staff if their fees were based solely on hourly rates charged by DSI to its non-bankruptcy clients. [*See id.*] (d) Pages 10 through 13 contained brief summaries, broken down by activity code, of the services rendered by the Trustee and his staff during the second interim period. [Dkt no. 1011, pp. 10-13.] (e) A large portion of the work performed by the Trustee and his staff continued to relate to managing the Debtor's operations. During the third interim period, they spent 58.6 hours supervising operations. [Dkt no. 1011, p. 12.] They continued to communicate with TNI and Triple Enterprises, and the Trustee continued to approve invoices for payment and approve any significant expenditure before it was incurred. [*Id.*] Detailed billing records describing the services rendered

in this category were attached to the application. [Dkt no. 1011, pp. 33-41.] (f) Other general categories in which the Trustee and his staff spent significant time during the second interim period included tax issues (89.6 hours) and accounting/auditing (29.8 hours). [Dkt no. 1011, pp. 11-12.] Detailed billing records describing the services rendered in these and all other categories were attached to the application. [Dkt no. 1011, pp. 20-44.] (g) Overall, the Trustee and his staff provided 243.8 hours of services during the third interim period. [Dkt no. 1011, pp. 13.] The Trustee personally spent 110.9 hours working on the case during the third interim period. [*Id.*] (h) As one would expect, the Trustee's more experienced staff members needed to spend less time on emergency-type business and bookkeeping services. In fact, neither Mr. Held nor Mr. Sorenson billed any time to the case during the third interim period. [Dkt no. 1011, p. 13.]

119. No objection to the Trustee's application was filed.

120. On an interim basis, the Court approved the Trustee's fees and costs in full. [Dkt no. 1030.]

TRUSTEE'S FINAL FEE APPLICATION

121. In October 2018, after the Effective Date of the plan, the Trustee and various estate professionals filed final fee applications. The Trustee's final fee application covered services rendered by the Trustee and his staff from March 1 through September 14, 2018, and also sought final approval of previously-allowed fees. [Dkt no. 1134.] As set forth in the application: (a) The application included time records for employees of DSI, who assisted the Trustee in the performance of his duties in the case. [Dkt no. 1134, pp. 1-2.] (b) For the final period, the Trustee requested that

the Court award him fees of $345,183.47 and costs of $581.84. [Dkt no. 1134, pp. 7, 13.] For the entire case, the Trustee requested that the Court award him fees of $1,155,844.71 and costs of $5,107.32. [*Id.*] The fees requested were the amount allowable under § 326(a) of the Code. [*Id.*] (c) Pages 8 through 11 contained brief summaries, broken down by activity code, of the services rendered by the Trustee and his staff during the second interim period. [Dkt no. 1134, pp. 8-11.] (d) Again, a large portion of the work performed by the Trustee and his staff related to managing the Debtor's operations. During the final period, they spent 45.8 hours supervising operations. [Dkt no. 1134, p. 10.] They continued to communicate with TNI and Triple Enterprises, and the Trustee continued to approve invoices for payment and approve any significant expenditure before it was incurred. [*Id.*] Detailed billing records describing the services rendered in this category were attached to the application. [Dkt no. 1134, pp. 30-41.] (e) Other general categories in which the Trustee and his staff spent significant time during the second interim period included plan of reorganization/disclosure statement (relating to, among other things, the Trustee's preparation and review of the transition from the Trustee to the reorganized debtor and the plan trustee) (24.3), and accounting/auditing (23.1 hours). [Dkt no. 1134, pp. 9-10.] Detailed billing records describing the services rendered in these and all other categories were attached to the application. [Dkt no. 1134, pp. 16-39.] (f) Overall, the Trustee and his staff provided 138.6 hours of services during the final period. [Dkt no. 1034, p. 11.] For the entire case, the Trustee and his staff provided 1,692.2 hours of services. [Dkt no. 1134, p. 7.] (g) The Trustee personally spent 100.9 hours working on the case during the final

period. [Dkt no. 1034, p. 11.] For the entire case, the Trustee personally spent 720.8 hours working on the case. [Dkt no. 597, p. 14; 808, p. 13; 1011, p. 13; 1034, p. 11.] (h) Again, the amount of time billed by more experienced staff members was low. Mr. Held billed a total of 4.2 hours and Mr. Sorenson did not bill any time to the case during the final period. [Dkt no. 1134, p. 11.] (i) The application stated, "In determining the value of the Trustee's services to the estate, the Trustee believes that the Court should consider various factors, including that the Trustee's fee should be treated as a commission, as well as that the fee requested is reasonable given the time expended, the novelty and difficulty of the issues presented and the work performed, the skill requisite to perform the services, the time limitations imposed, the amounts involved, and the results obtained." [Dkt no. 1134, pp. 12-13.]

122. The Plan Trustee filed an objection to TNI's final fee application because TNI had failed to disclose that, after being employed by the Trustee in this case, TNI's principal formed two entities which then sold goods and merchandise to the Debtor. [Dkt no. 1155.]

123. The only other party to object to any of the final fee applications was Clifton Capital. Clifton Capital joined in the Plan Trustee's objection to TNI's application, and then also objected to the final fee applications filed by the Trustee, the Trustee's general counsel (who, of course, represented the Trustee in all of his litigation with Clifton Capital, the Committee, and Hudson), and Triple Enterprises. [Dkt no. 1156.]

124. As to the Trustee, Clifton Capital argued that the Trustee was not entitled to the full amount

allowable under § 326(a). [Dkt no. 1156, p. 7.] Clifton Capital argued that the Court must consider "all relevant factors" when evaluating a chapter 11 trustee's requested compensation, and then, after determining the reasonable compensation, the Court should apply the formula set forth in § 326(a). [*Id.*] It argued that, in this circuit, the primary method used to determine a reasonable fee is to calculate the lodestar. [Dkt no. 1156, p. 9.] It argued that once the lodestar is established, there is a strong presumption that the lodestar figure represents a reasonable fee which should be adjusted only in rare or exceptional cases. [Dkt no. 1156, p. 9.] According to Clifton Capital, to calculate the lodestar, the Court should multiply total hours (1,692.2) by the alleged blended rate ($403.83). [*Id.*]

125. In his reply, the Trustee argued that § 330(a) sets forth a non-exclusive list of factors that the Court should consider when determining reasonable compensation of a chapter 11 trustee, and the Court's review is not limited to just hours spent and normal hourly rates. [Dkt no. 1166, p. 5.] He argued that "[i]n light of the complex nature of the issues and dynamics he faced, the valuable services he performed, and the success he achieved, the compensation requested by the Trustee . . . is reasonable and appropriate." [*Id.*] The Trustee wrote: Here, the Court is well aware of the complexity and contentiousness of this case. From his appointment on September 29, 2016 until September 14, 2018 (the effective date), the Trustee dealt with overseeing a multi-employee business with extensive business operations, serious accounting, tax and labor challenges, and pending state and federal litigation, in addition to the normal issues arising in a Chapter 11 case. [Dkt no. 1166, p. 6.] The pages that

followed provided a partial list of the litigation and issues with which the Trustee was involved. [Dkt no. 1166, pp. 9-12.] The Trustee continued, While the Trustee and his firm billed 1,692.20 hours in the course of this case, resulting in $758,977.50 in an hourly fee, this amount does not fully reflect the contributions made by the Trustee in this case. As such, the Court should also consider the novelty and difficulty of the questions presented to the Trustee. As noted above, this was not a routine Chapter 11 operating case. This case involved managing four restaurants with as many as 300 employees, updating the Debtor's inadequate financial and operational systems, at times dealing with a hostile Committee that appeared to be under the influence of the Debtor's owner, litigating to recover the Debtor's most valuable assets, namely the trademarked name, and multiple other actions in state and federal courts. . . .. The Court should also consider the fact that the Trustee obtained favorable results in this case. In the course of the Trustee's service, the Debtor's revenues and profits increased, operational systems were adopted, claims were reduced significantly, prior financial records reconstructed, and the business was primed for either a sale or a Plan of Reorganization. As a result of the Trustee's efforts, this Court approved a Plan that went into effect on September 14, 2018, promising to pay unsecured creditors a 100% distribution. [Dkt no. 1166, p. 12-13.]

126. At the hearing, the Court gave two reasons for approving the Trustee's fee in the full amount requested. First, in this Court's view, Congress intended that a trustee's compensation be in the nature of a commission, determined pursuant to § 326(a), unless extraordinary circumstances warrant revisiting the

compensation provided in the formula. [Dkt no. 1219, p. 48.] Second, even if the Court were to look at it simply as reasonable compensation, this was an exceptional case and the amount sought by the Trustee was reasonable for the services provided by the Trustee and his staff in this case. [Dkt no. 1219, pp. 51-52.]

127. On November 19, 2018, the Court entered an order (the "Final Fee Order") allowing the Trustee's fee request, on a final basis, in full. [Dkt no. 1192, p. 5.]

128. In its opening brief filed in the District Court, Clifton Capital asserted that the second basis for this Court's ruling was "an apparent attempt to justify the fee enhancement it awarded to the Trustee." [App. Dkt no. 11, p. 33.] Lest there be any doubt, the second basis for this Court's ruling was not pretext. The Court agreed with the arguments made by the Trustee in his reply and at oral argument, and for the extensive reasons provided herein the Court concludes still that the amount sought by the Trustee is reasonable compensation for the services rendered by him and his staff in this case.

CLIFTON CAPITAL'S APPEAL

129. On December 3, 2018, Clifton Capital filed a notice of appeal of the Court's final fee order. [Dkt no. 1204.]

130. Clifton Capital originally identified the Trustee, his general counsel, and Triple Enterprises as parties to the appeal. [Dkt no. 1204.] Ultimately, though, Clifton Capital sought only reversal of the Court award of fees to the Trustee.

131. On December 18, 2019, the District Court issued its ruling in Clifton Capital's appeal. The District Court ruled that this Court did not make the required findings to determine that the Trustee is entitled to a fee award that exceeds a lodestar figure. The Court vacated the fee order (at least to the extent that it approved the Trustee's fees) and remanded for this Court to either (a) definitively establish the lodestar figure and award fees accordingly, or (b) make detailed findings to determine whether a fee award beyond the lodestar figure is warranted.

THE PLAN TRUSTEE'S REFUSAL TO PAY THE TRUSTEE AND HIS GENERAL COUNSEL THE FEES ALLOWED BY THIS COURT

132. Under Hudson's and the Committee's plan, the Plan Trustee was Brian Weiss of Force Ten Partners. [Dkt no. 1078, p. 52.] Force Ten Partners (and particularly Mr. Weiss) was the Committee's financial advisor during the bankruptcy case. [*Id.*]

133. The Final Fee Order expressly provided that the Plan Trustee was "authorized and directed" to pay the Trustee and professionals the balance of fees and costs awarded by the Court. [Dkt no. 1192, pp. 3-6 (emphasis added).]

134. Contrary to the Final Fee Order and Section III.B.1.(c) of the confirmed plan, the Plan Trustee initially refused to pay any of the fees and costs awarded to the Trustee, the Trustee's general counsel, and Triple Enterprises, although he did pay Force Ten Partners and all of the other professionals whose fee awards were included in the Final Fee Order. [Dkt no. 1212, p. 2.] This forced the Trustee and his lawyers to file a motion for another order requiring the Plan Trustee to pay the allowed fees and costs, and an ex

parte application for an order shortening time. [Dkt nos. 1212, 1213.] The Court granted the application for an order shortening time. [Dkt no. 1215.]

135. Clifton Capital opposed the Trustee's request that the Court compel the Plan Trustee to comply with the Final Fee Order. [Dkt no. 1223.]

136. The Court granted the motion and entered an order directing the Plan Trustee to immediately pay the Trustee, his general counsel, and any other unpaid professionals the fees and costs allowed pursuant to the Final Fee Order. [Dkt no. 1227.]

DIFFERENCES BETWEEN APPOINTMENT OF A TRUSTEE AND EMPLOYMENT OF A PROFESSIONAL EMPLOYED BY A TRUSTEE

137. The lodestar approach was developed in non-bankruptcy fee shifting cases, in which prevailing parties sought awards of attorneys' fees and costs. It is therefore much easier to apply the lodestar approach to services performed by attorneys providing services to an estate. Applying a lodestar approach is also easier because of the manner in which professionals are employed.

138. A trustee may employ attorneys, accountants, and other professional persons to assist the trustee in carrying out his or her duties under the Code. 11 U.S.C. § 327(a). In a chapter 11 case, a committee may employ attorneys, accountants, and other agents to represent or perform services for the committee. 11 U.S.C. § 1103(a). The professionals employed by a trustee or by a committee may be employed "on any reasonable terms and conditions of employment, including on a retainer, on an hourly basis, on a fixed or percentage fee basis, or on a contingent fee basis." 11

U.S.C. § 328(a). The application for authority to employ a professional must state any proposed arrangement for compensation. Fed. R. Bankr. p. 2014(a). In this district, the written notice of the application must identify the hourly rate of professionals expected to render services. LBR 2014- 1(b)(3)(C). Employment applications and other notices filed by the Trustee and the Committee in this case demonstrate how this is accomplished. [See Dkt nos. 236, p. 22; 287, p. 3; 305, pp. 2-3; 307, pp. 3-4, 22; 553, p. 3.]

139. When a professional is employed, the professional is being hired to do the type of work performed by the professional outside of bankruptcy. Attorneys are hired to do legal work, accountants are hired to do accounting work, financial advisors are hired to provide financial advisory work, etc. Professionals who charge by the hour determine their rates in advance based on many different factors, including the type and complexity of services they typically provide, competition in the local market, operating expenses, and so on. Professionals being employed in a bankruptcy case can adjust those rates depending on the nature of the case, though generally courts do not permit professionals to charge higher rates to debtors, trustees and committees than they do to non-bankruptcy clients.

140. Thus, when an attorney or other professional is employed in a bankruptcy case on an hourly-fee basis, the professional typically charges the estate the same rate that the professional has determined is appropriate to charge non-bankruptcy clients for the same type of work. Those rates are disclosed up front in the employment application.

141. Chapter 7 and 11 trustees, on the other hand, do not have "trustee" rates that they establish in advance for trustee services. In chapter 7 cases, a trustee's non-trustee hourly rate is irrelevant because trustees receive a commission equal to the maximum amount allowable under § 326(a). See 11 U.S.C. § 326(a), 330(a)(7). In chapter 11 cases, in this Court's experience, trustees also seek, and receive, compensation equal to the amount allowable under § 326(a).

CLIFTON CAPITAL'S ATTEMPTS TO DIMINISH THE TRUSTEE'S EFFORTS AND SUCCESS IN THIS CASE

142. In its objection to the Final Fee Application, Clifton Capital argued that the Court should not award fees above the alleged lodestar amount, "particularly considering, among other things, the fact that the Committee took the laboring oar on negotiating, drafting, and obtaining confirmation of the Plan, and that the Chapter 11 Trustee substantially limited communication with the Committee and its financial advisors over a year ago." [Dkt no. 1156, p. 9 n.28.] Also in its appellate briefs, Clifton Capital continued to credit only the Committee with confirmation of the plan. [App. Dkt no. 11, pp. 5-6.] In its reply brief, Clifton Capital stated: In fact, it was the Committee—not the Trustee—that took the laboring oar in negotiating, drafting, and getting a Plan confirmed. And the Committee, far from being an "advocate" for the Debtor's principal, was able to secure substantial concessions from him to make the Plan viable, including the contribution of substantial personal assets to help collateralize the Plan. Conversely, it appears the Trustee preferred to simply sell the business and be done. See RB at 1:20-21 (describing the Trustee's goal of preparing the business "for a potential sale to a

third party.") and RB 10:12-13 (trying to make the business "attractive to potential buyers"). As a result of the Committee's efforts, led by Clifton Capital's principal, the Debtor's business was allowed to continue on an hundreds of jobs were preserved; had the business been liquidated, it is unclear what impact that would have had on ongoing operations and employees. [App. Dkt no. 23, p. 5.]

143. It is erroneous for Clifton Capital to suggest that the Trustee is not responsible for the positive outcome of this case. The reason Hudson and the Committee could propose a viable plan was because the Trustee cleaned up the huge mess he inherited when he was appointed.

144. Indeed, when Beasley objected to confirmation of Hudson and the Committee's plan, Beasley argued that the plan was not "feasible" because of the Debtor's prepetition financial accounting practices and other issues. [Dkt no. 1048, p. 9.] In response, the Committee contended that the plan was supported by reliable financial projections. [Dkt no. 1058, p. 21.] It noted that historical financial data had been prepared from financial information provided by the Trustee, and that the Committee's financial projections were "based on the Debtor's actual performance under the Trustee's stewardship." [*Id.*] The Committee's financial advisor (and the current Plan Trustee) testified that the Trustee had "provided the Committee with monthly financial statements and reports summarizing such financial information and the Debtor's operational performance and financial condition." [Dkt no. 1059, pp. 2, 9.] He also testified that the Trustee had provided him with estimates of outstanding taxes

owed by the Debtor to the IRS, based on and supported by the Trustee's reconstruction of the Debtor's books and records. [Dkt no. 1059, pp. 4-5.] The Court rejected Beasley's argument. As stated in the Court's tentative ruling, "The trustee was appointed by order entered September 28, 2016 and has been operating the debtor's business since that date. The historical post-petition financial information provided by the trustee is more reliable information and is the data that the court will examine in connection with any feasibility analysis." Thus, it is clear that the Committee, and the Court, heavily relied upon information prepared by the Trustee in connection with confirmation of the plan.

145. Similarly, if the Trustee had not sued and succeeded in avoiding the fraudulent transfer of Debtor's intellectual property to Roscoe's IP, the economic value of the Debtor would have been much lower, diminishing the likelihood that a 100% plan could have be proposed. Once the Trustee recovered the intellectual property, Hudson had no choice but to pledge non-Debtor assets to fund a plan. That likely was the only way he could preserve the trademarks which were critical to the success of his non-Debtor restaurants.

146. This is not to say that the Committee and its professionals do not deserve credit for putting together a viable plan and disclosure statement. But it cannot be forgotten that the Trustee kept the pressure on them to propose a viable plan capable of confirmation . In order to comply with the schedule dictated by the Trustee, Hudson had to make concessions and promises – at least one of which he immediately

breached – to keep the Trustee from pursuing other options.

147. In that regard, Clifton Capital's assertion that the Trustee would have "liquidated" the business and caused employees to lose jobs has no factual basis. Ongoing businesses are sold all of the time pursuant to § 363 of the Code, with the businesses continuing to operate after sale. The Trustee also could have "sold" the Debtor or its assets through a plan. There is no reason to believe that a sale or chapter 11 plan proposed by the Trustee would be the equivalent of a chapter 7 liquidation of the Debtor's parts and dismantling of the business, or that any sale by the Trustee would have not served creditors' interests.

148. Technically, it remains to be seen whether the Committee's decision to support Hudson pays off. The Committee is relying largely on Hudson's other entities to fulfill payment obligations over a period of years. Fortunately, the confirmed plan provides a collateral package that guarantees that all creditors, including Clifton Capital, will be paid in full. As shown by the Plan Trustee's declaration, the existence of the collateral package ensured the feasibility of the plan. [Dkt no. 1059, pp. 7-8.]

THE COURT'S RULING ON NOVEMBER 4, 2020

149. On November 4, 2020, the Court conducted a hearing on the Trustee's Final Fee Application. Prior to the hearing, the Court issued the following tentative ruling:

> It is difficult for a lower court on remand to adjudicate an issue when it firmly believes that the appellate court made an error of law on ap-

peal. This court remains of the view that Congress intended for the compensation formula set forth in section 326(a) to be presumptively reasonable (and generally in the nature of a commission) and that the citations offered by the District Court as support for the contrary position view are not on point. For example, In re Manoa Finance Co., Inc., 853 F.2d 687, 692 (9th Cir. 1988), which the district court cites for the proposition that there is a strong presumption that an award based on a lodestar compensation is the amount to be allowed as reasonable compensation did not even involve trustee compensation. The professional whose fees were at issue in that case was committee counsel. Therefore, Manoa offers no insight whatsoever as to the appropriate interpretation of section 326(a) or the manner in which trustee compensation should be calculated. [Nevertheless], the district court's decision is law of the case, and this court is obliged to follow it.

According to the district court, "On remand, the Bankruptcy Court should either (i) definitively establish the [lodestar] figure and award fees accordingly, or (ii) make detailed findings to determine whether a fee beyond the lodestar figure is warranted."

As a preliminary matter, the court notes that there is some disagreement as to what the lodestar figure actually is here. Due to a typographical error in a portion of the trustee's final fee application, at various points in time, Clifton Capital has argued that the lodestar should be calculated using a blended hourly rate of

$403.83 per hour. The trustee explains that, if based on the regular hourly rates that DSI charges to its clients, the blended rate should be $448.50, but that, for reasons set forth in the trustee's brief, the Court should increase DSI's blended hourly rate to $550 per hour. (Ordinarily, the court does not calculate fees based on a blended hourly rate and uses this figure only for comparison/reference to assess whether a professional has assigned more senior people to a matter than was required; however, the court assumes that the parties are referring to blended rates merely for ease of calculation and that the court could derive the identical figures from looking at the actual billing statements.)

These different hourly rates, multiplied by the total number of hours billed (1,692.2) produces the following figures as possible lodestar calculations:

1692.2 hours @ $403.83 = $683,361.13

1692.2 hours @ $448.50 = $758,955.50 (this is the trustee's figure, but the math actually works out to $758,951.70; the district court identifies this figure as $758,977.50 for reasons that are unclear)

1692.2 hours @ $550.00 = $930,710.00.

The trustee then argues that, in addition to calculating its lodestar fee at a higher hourly rate than that customarily charged by DSI to its clients, the court should apply a multiplier to its fees in the vicinity of 1.5 to 2.0 to bring the total compensation up to the statutory cap of $1,155,844.71. The Court rejects this approach.

The factors identified by the trustee as justification for the increase in the blended rate are relevant to an overall assessment of what a reasonable fee should be for a trustee in a given case . . . , but it muddies the waters to separate out an enhancement to the blended rate from an overall fee enhancement or bonus. The blended hourly rate derived from the trustee's actual fee statements is $448.50. The court will not increase this rate for the purpose of calculating the lodestar fee, but this does not end the analysis as to whether a bonus or fee enhancement is warranted on these facts.

The district court, again quoting from Manoa which has nothing to do with trustee compensation, says that, in order to receive a fee [enhancement], the applicant must come forward with specific evidence showing why the results obtained were not reflected in either his standard hourly rate or the number of hours allowed. He must also show that the bonus is necessary to make the award commensurate with compensation for comparable nonbankruptcy services. Although this court disagrees with the district court's decision to rely on the precise language of Manoa for the reasons outlined above, the Court accepts under the circumstances that the trustee must come forward with facts sufficient to show why a fee beyond the lodestar figure is warranted.

Compensation for a trustee is distinguishable from compensation for a professional, but, in either event, when exceptional results have been achieved or when for other reasons, the amount

of compensation requested fails to adequately compensate for the services rendered [a fee enhancement may be appropriate]. The Court continues to believe that this is was an exceptionally difficult case for a variety of reasons and that the complexities of this case did not necessarily result in an increase in the number of hours spent by the trustee and his staff. (If the complexities merely increased the number of hours that the trustee spent working on the case, this would be reflected in, and therefore compensated by, the lodestar calculation.)

In light of the numerous challenges this trustee faced and the manner in which the trustee rose to the occasion to resolve these challenges, producing exceptional results, this Court finds that the trustee utilized in connection with the administration of this estate levels of strategic thinking and diplomacy above and beyond those normally employed by a trustee in a chapter 11 case. The trustee assumed control over an operating business with several locations and was called upon to keep those restaurants operating in a profitable manner while dealing with the fact that there were effectively no internal controls, no reliable accounting methods or records, a toxic corporate culture that had resulted in large employee tort claims, years of unfiled tax returns and unpaid sales taxes, an owner who had siphoned off and was attempting to continue to siphon off estate assets and resources to benefit or support other business and his competing restaurants, numerous related party contracts and a principal who failed to cooperate in discovery or obey court orders.

> The analogy that comes to mind here is of the plate-spinners that used to appear on the Ed Sullivan show who worked furiously to keep multiple plates in the air at the same time. The number of hours spent working on the case is not a measure of the difficulty or skill level required to perform the required services in an exceptional manner.
>
> In light of the high level of expertise and experience required to perform these tasks in the manner in which they were performed, the court would have no trouble finding that it would be reasonable compensation if the court were to calculate the trustee's compensation utilizing a blended hourly rate of $700 or more per hour. However, that would produce a total award of $1,184,540 or more, which would exceed the cap on trustee compensation set by section 326(a). Therefore, the Court finds that reasonable compensation for the trustee's services in this case is the statutory maximum of $1,155,844.71.

150. After hearing from counsel at the hearing, the Court adopted the tentative ruling.

151. To the extent that any of the Conclusions of Law set forth below constitutes a Finding of Fact, the same is hereby incorporated by this reference.

II. CONCLUSIONS OF LAW

152. To the extent that any of the forgoing Findings of Fact constitutes a Conclusion of Law, the same is hereby incorporated herein by this reference.

153. A voluntary bankruptcy case is commenced when a debtor files a petition for relief under

a particular chapter of the Code. 11 U.S.C. § 301(a). In this case, the Debtor filed a petition for relief under chapter 11 of the Code on March 25, 2016.

154. The commencement of a bankruptcy case creates an "estate." 11 U.S.C. § 541. Generally, the estate is comprised of all property interests of the debtor as of the petition date, the proceeds of that property, and all property acquired by the estate after the petition date. 11 U.S.C. § 541(a).

155. In a chapter 11 case, unless a trustee is appointed, a debtor acts as a "debtor in possession" of the estate and has substantially all of the rights, and is to perform substantially all of the functions and duties, of a chapter 11 trustee. 11 U.S.C. § 1107(a). In this case, the Debtor was a debtor in possession from March 25, 2016, through approximately September 29, 2016.

156. While a debtor is acting as a debtor in possession, with the court's approval, the debtor is authorized to employ attorneys and other professionals to represent or assist the debtor in carrying out its duties. 11 U.S.C. § 327(a). Subject to approval of the Court, professionals receive payment from the estate. 11 U.S.C. §§ 330-331.

157. As soon as practicable after a chapter 11 case is filed, unless it determines that there is no need for a committee or not enough creditors apply to be on the committee, the U.S. Trustee appoints a committee of creditors holding unsecured claims. *See* 11 U.S.C. § 1102(a)(1). The committee, with the court's approval, may employ attorneys and other professionals. 11 U.S.C. § 1103(a).

158. In this Court's experience, in operating cases such as this one, creditors' committees promptly retain attorneys, and often retain financial advisors, soon after they are appointed. In this case and others in which debtors' management transferred away assets prepetition, engaged in selfdealing, failed to follow proper business protocols, and the like, creditors' committees often exercise their authority to "investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan." See 11 U.S.C. § 1103(c)(2).

159. Upon request of a party in interest or the U.S. Trustee, a bankruptcy court must order the appointment of a trustee "for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management," or "if such appointment is in the interests of creditors, any equity security holders, and other interests of the estate." 11 U.S.C. § 1104(a). In this case, the Examiner's status report, as well as the Debtor's actions during the first six months of the case, constituted ample grounds for appointment of a chapter 11 trustee.

160. When a chapter 11 trustee is appointed, the debtor no longer acts as a debtor in possession and is no longer authorized to exercise control over property of the estate. Those rights, as well as the corresponding functions and duties, shift to the trustee. Although the debtor still is a party in interest and has the right to propose a plan, 11 U.S.C. § 1121(a), its professionals cannot be paid by the estate.

161. A creditors committee usually has a limited role, if any, after a chapter 11 trustee is appointed. This is because the trustee fulfills a number of the duties of a committee. Compare 11 U.S.C. § 1106(a) with 11 U.S.C. § 1103(c). In this case, the Committee employed attorneys after the Trustee was appointed. Ultimately the Committee partnered with Hudson to propose a chapter 11 plan that would, among other things, allow Hudson to retain control of the company and pay creditors in full.

162. There is no established hourly rate for services rendered by chapter 11 trustees. When a trustee is appointed, the trustee is not required to (and does not) identify a rate that he or she intends to charge for services to be rendered in the case. The court orders the U.S. Trustee to appoint a trustee, the U.S. Trustee does so, and then in this district the U.S. Trustee files a brief motion so there is an order on the docket approving the U.S. Trustee's choice of trustee. At no point in that process does the court approve hourly rates to be charged by the trustee during the case.

163. This may be contrasted with the procedure applicable to the employment of attorneys and other professionals. When a debtor in possession, trustee or committee seeks to employ a professional, it files an application that sets forth the proposed terms and conditions of employment, "including on a retainer, on an hourly basis, on a fixed or percentage fee basis, or on a contingent fee basis." 11 U.S.C. § 328(a). In this district, a notice of the application is supposed to identify the hourly rate of each professional to render services. LBR 2014-1(b)(3)(C).

164. The risk of underpayment is also different for a chapter 11 trustee than for a professional employed by a debtor, trustee, or committee. For all, there is an inherent risk that if the case is converted to chapter 7 and assets are liquidated by a chapter 7 trustee there will not be sufficient funds to pay administrative expenses in full. When that occurs, chapter 11 trustees and professionals receive a "pro rata" distribution from available funds after payment in full of fees and costs incurred by the chapter 7 trustee and his or her professionals. See 11 U.S.C. § 726(b). There are also other scenarios in which chapter 11 trustees and professionals may receive only a pro rata (if any) distribution. The Court presumes that this inherent risk of underpayment is already priced into the hourly rates identified by attorneys, accountants, and other estate professionals when they are being employed under § 327(a) of the Code.

165. Another risk of underpayment for all professionals, which may or may not be priced into their hourly rates, arises out of the Supreme Court's decision in *Baker Botts LLP v. ASARCO LLC*, 576 U.S. 121 (2015). Before that ruling, estate professionals (trustees, attorneys, etc.) who incurred fees and costs successfully defending their fee requests could seek payment of such fees and costs from the estate. In Baker Botts, the debtor employed two law firms to file a complaint against the debtor's parent company and obtained a judgment worth between $7 and $10 billion. *Baker Botts*, 576 U.S. at 124. That judgment contributed to a successful organization in which the parent company regained control over the debtor. *Id.* at 125. When the law firms filed their final fee applications, the parent company retaliated by causing the

debtor to object to their fee requests. *Id.* The bankruptcy court awarded the firms $120 million for their work, a $4.1 million bonus, plus over $5 million for time spent litigating over their fee applications. *Id.* The Supreme Court ruled that professionals are not entitled to compensation and reimbursement from estates for the fees and costs incurred by them in defending their fee requests. *Id.* at 135. When a trustee or professional has engaged in contentious litigation against a party during a bankruptcy case, it is not uncommon for that party to object to the trustee's and/or professional's fee request when the case ends. Before Baker Botts, the trustee or professional could request payment from the estate for defending against the objection. Now, however, unless the trustee or professional is able to obtain Rule 11 sanctions, the trustee or professional faces the risk of nonpayment of fees and costs incurred in such litigation.

166. However, in addition to the inherent risk of underpayment faced by all chapter 11 professionals, chapter 11 trustees face an additional underpayment risk because of § 326(a). In the Court's experience, because of § 326(a), chapter 11 trustees are very often awarded less fees than they would be awarded on hourly-fee bases.

167. This was true in this case for the first two interim periods. For the first interim period, the Trustee requested fees of $252,997.09, while hours spent multiplied by hourly rates charged for non-trustee matters totaled $347,741.50. After the second interim period, the Trustee had been paid $524,184.36 pursuant to § 326(a), while hours spent multiplied by hourly rates charged for non-trustee matters totaled

$566,133.00. If the case had faltered during those interim periods, the fee awarded would have been less than any amount calculated in accordance with hourly rates charged by the Trustee's firm for non-trustee matters.

168. Because of § 326(a), chapter 11 trustees face a double risk of underpayment. First, the amount of fees awarded is very often less than the amount they would be awarded if their fees were based on hourly rates charged by their firms for their non-trustee services. Second, based on that already-reduced amount, the trustee may receive only a pro rata distribution. This double risk is not "priced into" the normal hourly rate charged by a firm for the trustee's non-trustee services.

169. The court may award to a chapter 11 trustee "reasonable compensation for actual, necessary services rendered by the trustee . . .." 11 U.S.C. § 330(a)(1)(A). "In determining the amount of reasonable compensation to be awarded to a trustee, the court shall treat such compensation as a commission, based on section 326." 11 U.S.C. § 330(a)(7).

170. "In determining the amount of reasonable compensation to be awarded to a . . . trustee under chapter 11 . . . the court shall consider the nature, the extent, and the value of such services, taking into account all relevant factors, including— (A) the time spent on such services; (B) the rates charged for such services; (C) whether the services were necessary to the administration of, or beneficial at the time at which the service was rendered toward the completion of, [the bankruptcy case]; [and] (D) whether the services were performed within a reasonable amount of time commensurate with the complexity, importance,

and nature of the problem, issue, or task addressed . . . ." 11 U.S.C. § 330(a)(3) (emphasis added).

171. A bankruptcy court's award of fees under § 330(a) is a matter of the court's discretion. *In re Newcorp Energy, Inc.*, 764 F.2d 655, 657 (9th Cir. 1985). "At least in part, the bankruptcy court's broad discretion is due to the fact that 'no matter how close the [c]ourt comes to an objective determination of a reasonable fee, [the fee determination] is still, in the final analysis, a substantially subjective exercise.'" *Staiano v. Cain (In re Lan Assoc. XI, LP)*, 192 F.3d 109, 122 (3d Cir. 1999) (quoting *In re Garland Corp.*, 8 B.R. 826, 831 (Bankr. D. Mass. 1981)).

172. Cases analyzing compensation under § 330(a)(3) usually concern professionals employed by trustees, chapter 11 debtors, and committees. Thus, courts look to non-bankruptcy law relating to fee-shifting statutes for guidance. *See Burgess v. Klenske (In re Manoa Fin. Co., Inc.),* 853 F.2d 687 (9th Cir. 1988). In this Court's view, Congress intended for the compensation formula set forth in § 326(a) to be presumptively reasonable compensation for a chapter 11 trustee, and generally in the nature of a commission. However, in accordance with the District Court's ruling, this Court is not following that approach in reaching the conclusions made herein.

173. In non-bankruptcy cases, courts considered many factors in determining the amount of a reasonable fee to be awarded under federal fee-shifting statutes. *In Kerr v. Screen Extras Guild, Inc.,* 526 F.2d 67 (9th Cir. 1976), the court adopted "guidelines" from *Johnson v. Georgia Highway Express, Inc.*, 488 F.2d 714 (5th Cir. 1974): (1) the time and labor required; (2) the novelty and difficulty of the questions involved;

(3) the skill requisite to perform the legal service properly; (4) the preclusion of other employment by the attorney due to acceptance of the case; (5) the customary fee; (6) whether the fee is fixed or contingent; (7) time limitations imposed by the client or the circumstances; (8) the amount involved and the results obtained; (9) the experience, reputation, and ability of the attorneys; (10) the "undesirability" of the case; (11) the nature and length of the professional relationship with the client; and (12) awards in similar cases.

174. Application of the Johnson factors proved difficult. *See Copeland v. Marshall*, 641 F.2d 880, 890-91 (D.C. Cir. 1980). "Simply to articulate those twelve factors . . . does not itself conjure up a reasonable dollar figure in the mind of a district court judge." *Id.* at 890. Indeed, the Ninth Circuit BAP has referred to the Johnson factors as an "obsolete laundry list" which has been "subsumed within more refined analyses." M*eronk v. Arter & Hadden, LLP (In re Meronk)*, 249 B.R. 208, 213 (9th Cir. BAP 2000).

175. The Third Circuit first developed what became known as the "lodestar" approach in *Lindy Bros. Builders, Inc. of Phila. v. Am. Radiator & Standard Sanitary Corp.*, 487 F.2d 161 (3d Cir. 1973). Even then, the Third Circuit noted that while a reasonable hourly rate multiplied by the number of hours worked "should be the lodestar of the court's fee determination," "[t]he court cannot properly fix attorneys' fees merely by multiplying the hourly rate for each attorney times the number of hours he worked on the case." *Lindy*, 487 F.2d at 167. As the Third Circuit noted in a later decision in the same case, its prior decision still "permits an adjustment to the 'lodestar' up or down based on the all-round performance of counsel in the

specific case." *Lindy Bros. Builders, Inc. of Phila. v. Am. Radiator & Standard Sanitary Corp.*, 540 F.2d 102, 118 (3d Cir. 1976).

176. Although it did not use the word "lodestar," the Supreme Court required the same approach in civil rights actions under 42 U.S.C. § 1988. *See Hensley v. Eckerhart*, 461 U.S. 424 (1983). The Court stated that "[t]he most useful starting point for determining the amount of a reasonable fee is the number of hours reasonably expended on the litigation multiplied by a reasonable hourly rate. This calculation provides an objective basis on which to make an initial estimate of the value of a lawyer's services." *Id.* at 433 (emphasis added). The Court continued: "The product of reasonable hours times a reasonable rate does not end the inquiry. There remain other considerations that may lead the district court to adjust the fee upward or downward, including the important factor of the 'results obtained.'" *Id.* at 434 (emphasis added).

177. In *Manoa*, a case involving fees sought by attorneys who represented a creditors' committee, the Ninth Circuit generally held that analyses used when applying federal fee-shifting statutes are relevant to requests for allowance of fees under § 330 of the Code. Thus, a fee award that is based on a reasonable hourly rate multiplied by the number of hours actually and reasonably expended is presumptively a reasonable fee. *Manoa*, 853 F.2d at 691.

178. A few years after *Manoa*, the Ninth Circuit decided *Unsecured Creditors' Comm. v. Puget Sound Plywood, Inc.*, 924 F.2d 955 (9th Cir. 1991). In that case, the bankruptcy court had calculated part of an attorney's fee award based on, among other things, one third of the amount recovered in certain litigation

instead of the attorney's hourly rate. The attorney argued that the court was required to start with the lodestar, and that fee shifting cases in which courts start with the lodestar are binding in bankruptcy cases. The Ninth Circuit rejected his arguments: Although *Manoa* suggests that starting with the "lodestar" is customary, it does not mandate such an approach in all cases. Moreover, *In re Yermakov*, 718 F.2d 1465, 1471 (9th Cir. 1983), states that calculating the "lodestar" is the "primary" method for calculating fees; "primary" is not a synonym for "exclusive." Fee shifting cases are persuasive, but due to the uniqueness of bankruptcy proceedings, they are not controlling. *Puget Sound Plywood*, 924 F.2d at 960.

179. The Ninth Circuit confirmed this approach in two cases decided since Puget Sound Plywood. In 2000, the Ninth Circuit stated that "the general principles applicable to fee shifting statutes 'may require some accommodation to the peculiarities of bankruptcy.'" *Cedic Dev. Co. v. Warnicke (In re Cedic Dev. Co.)*, 219 F.3d 1115, 1117 (9th Cir. 2000) (quoting *Manoa*). In 2006, the Ninth Circuit also observed that the lodestar method is the customary method for assessing a attorney's fee application under § 330(a) of the Bankruptcy Code, but the lodestar method is not mandatory. *Boone v. Derham-Burk (In re Eliapo)*, 468 F.3d 592, 598 (9th Cir. 2006).

180. Numerous courts have observed that application of the lodestar approach, or other factors that have been identified when evaluating the fee for attorney services, to work performed by trustees (as opposed to attorneys for trustees) is not always appropriate. For example, *in In re Rauch*, 110 B.R. 467 (Bankr. E.D. Cal. 1990), the court wrote, "While these

factors are applicable to attorneys, they are not necessarily applicable to trustees. A significant difference exists between the functions performed by attorneys and those functions performed by trustees." *Id.* at 473. Some courts have even questioned whether trustees should have to keep time records. *See In re Greenley Energy Holdings of Pa., Inc.*, 102 B.R. 400, 405 (E.D. Pa. 1989). In any event, usual factors and considerations applied to attorneys' requests for compensation are not irrelevant; they may still be considered. *Rauch*, 110 B.R. at 473.

181. One instructive case is *In re Guyana Dev. Corp.*, 201 B.R. 462 (Bankr. S.D. Tex. 1996). In that case, the chapter 11 trustee had received interim fee payments totaling $585,000. At the end of the case, the trustee requested a total fee of approximately $2.4 million – the full amount permitted under § 326(a). The IRS objected, contending that the hours expended by the trustee did not justify the fee requested, and that the court was required to apply a strict lodestar calculation to calculate the trustee's fee. According to the IRS, the court should have started with an hourly rate of $300 ($100 more than the trustee charged for legal services), then adjust that rate by a multiplier of two (for a total hourly rate of $600), and then multiply that by the number of hours expended. Thus, the IRS requested that the trustee be allowed a fee of approximately $866,000.

182. The court rejected the IRS' argument, stating that "[t]he function of the trustee is different from that of all other professionals working for the estate." *Id.* at 476. It stated that a trustee's fee "'may be computed differently from a professional's reasonable fee. Although most of the reported decisions deal with the

section 326(a) cap, rather than the method of determining trustees' fees when the cap is not a factor, it appears that a majority employ the lodestar approach to trustees' fee determinations. Some courts, however, reject that approach as inappropriate in light of the significant difference between the functions performed by trustees and those performed by the professionals employed by trustees. In these courts especially, the results obtained in the case play a far greater role in determining reasonable compensation for trustees than they do with respect to the compensation of professionals.'" *Id.* at 476 (quoting Am. Bankr. Inst., American Bankruptcy Institute National Report on Professional Compensation in Bankruptcy Cases (G.R. Warner rep. 1991)).

183. Ultimately the Guyana court awarded the trustee's fee request in full. The court looked to multiple factors, including the results obtained. "These extraordinary results, especially given the difficult circumstances under which it was achieved, represent another factor supporting the trustee's proposed compensation in this case." *Guyana*, 201 B.R. at 484.

184. Unlike with attorneys and other professionals who provide services outside of bankruptcy similar to those they provide in bankruptcy cases, there is no such thing as a chapter 11 trustee outside of bankruptcy. The closest analog may be a chief restructuring officer hired to run a company. It is not uncommon for such non-bankruptcy professionals to be entitled to success fees or bonuses when they deliver exceptional results. For a company such as the Debtor, a CRO could easily be entitled to additional compensation in the form of a success fee or bonus in

excess of the fee enhancement sought by the Trustee in this case.

185. The Ninth Circuit has held that § 330 and non-bankruptcy fee-shifting statutes are sufficiently similar to justify applying the same general principles for fee enhancements. *Manoa*, 853 F.2d at 691. Thus, an award that is based on a reasonable hourly rate multiplied by the number of hours actually and reasonably expended is presumptively a reasonable fee. *Id.* "Although upward adjustments of the lodestar figure are still permissible, such modifications are proper only in certain 'rare' and 'exceptional' cases, supported by both 'specific evidence' on the record and detailed findings by the lower courts." *Penn. v. Del. Valley Citizens' Council for Clean Air*, 478 U.S. 546, 565 (1986). Consistent with Supreme Court and Ninth Circuit law, this Court has rarely granted requests for fee enhancements. This case, however, is the rare case in which an enhancement is appropriate.

186. In *Manoa*, the court stated that the novelty and difficulty of the questions involved, the skill requisite to perform the legal service properly, the quality of representation, and the results obtained are subsumed within the loadstar. *Manoa*, 853 F.2d at 691. The court stated, "Because these factors ordinarily are accounted for in either the hourly rate or the number of hours expended, they can support an upward adjustment only when it is shown by specific evidence that they are not fully reflected in the lodestar." *Id.* (emphasis added). This is because the "results obtained" from litigation is "presumably" fully reflected in the lodestar amount. *Pennsylvania*, 478 U.S. at 565.

187. The notion that "results obtained" are included in the lodestar appears to have originated from the Supreme Court's non-bankruptcy decisions in *Hensley v. Eckerhart*, 461 U.S. 424, 434-35 (1983), and *Blum v. Stenson*, 465 U.S. 886 (1984). In Blum, a nonprofit legal aid firm sought an award of attorneys' fees under the Civil Rights Attorney's Fees Awards Act of 1976, which provided that the court, in its discretion, could allow the prevailing party a reasonable attorney's fee as part of its costs. The trial court awarded fees and determined that a bonus was proper because of, among other things, the benefit achieved for the class of plaintiffs in that case. The Court commented, "Because acknowledgment of the 'results obtained' generally will be subsumed within other factors used to calculate a reasonable fee, it normally should not provide an independent basis for increasing the fee award." *Id.* at 900. Particularly in light of the Court's citation to Hensley, the point was that if a plaintiff's attorney successfully litigates 100% of the plaintiff's claims, the attorney may be entitled to recover a fee for 100% of the hours expended; if the attorney does not prevail on all of the claims asserted, work on the unsuccessful claims cannot be deemed to have been expended in pursuit of the result achieved and therefore the reasonable fee to be awarded should not include the hours spent on the unsuccessful claims. *See Hensley*, 461 U.S. at 434-35. In the context of fee-shifting statutes and cases in which multiple claims have been asserted, it therefore makes some sense to say that the lodestar already reflects the number of hours spent achieving the favorable result.

188. In the bankruptcy context, the Ninth Circuit recognizes that it is appropriate to award a fee enhancement based on exceptional results. *See*

Manoa, 853 F.2d at 691-92 (*citing In re Elmendorf Bd. Corp.*, 57 B.R. 580 (Bankr. D.N.H. 1986)). In *Elmendorf*, attorneys for a chapter 11 trustee and committee requested a fee multiplier of 1.75 and 1.50; the U.S. Trustee objected and argued that the multiplier should not exceed 1.25. The court determined that the case was one of the "few and far between" cases that justified a fee enhancement based on results achieved, and awarded the full amounts requested by the professionals.

189. The Ninth Circuit also acknowledged that a bonus could be awarded based on results in *Arter & Hadden LLP v. Meronk (In re Meronk)*, 24 Fed. App'x 737 (9th Cir. 2001). In that case the bankruptcy court had expressly stated that the law firm "had achieved a 'fine' result, but not a 'stupendous' or 'wonderful' one." *Id.* at 738. As noted by the BAP in its underlying decision, "a mere 'fine' result is not sufficient to support the award of a bonus." *Meronk*, 249 B.R. at 214. Unlike *Meronk*, the results achieved by the Trustee in this case were not just "fine." They were stupendous, wonderful, and exceptional. Thus, consistent with the Ninth Circuit's decision in *Meronk*, it is appropriate for the Court to award the Trustee a fee enhancement in this case.

190. Another factor that may justify an upward deviation from the lodestar is risk of loss or underpayment. *See First Nat'l Bank of Chicago v. Comm. of Creditors Holding Unsecured Claims (In re Powerine Oil Co.)*, 71 B.R. 767 (9th Cir. BAP 1986). As noted above, a chapter 11 trustee faces a double risk of underpayment that would not be incorporated into a rate charged by an ordinary estate professional. While that

did not ultimately occur in this case, it was a risk when the Trustee accepted appointment.

191. Based upon the totality of the facts in this case and applicable legal authorities (including decisions of the Supreme Court and the Ninth Circuit, and the decision of the District Court in this case), this Court concludes that the "lodestar" is $758,955.50 and that the Trustee is entitled to an enhancement because the results in this case were truly exceptional within the meaning of *Manoa*, *Meronk*, and other applicable case law.

192. The case was a disaster when the Trustee took over. Among other things, the Debtor was incapable of producing proper budgets, it did not follow basic accounting protocols, it was diverting cash receipts to non-Debtor accounts, it failed to disclose transfers made to Hudson and at least one of Hudson's entities, it lacked proper internal controls and inventory systems, it could not accurately identify the profitability of its four locations, it was overstating its revenues, it owed millions of dollars in taxes to the IRS and State of California, it entered into settlements without court approval, it was allowing Hudson's other entities to use liquor licenses owned by th Debtor, the lease for one of its most important locations was month-to-month, it wanted to close a store that was competing with one of Hudson's other entities, and it was seeking relief (assumption of leases) that would require the Debtor to pay one of Hudson's other entities millions of dollars. The biggest thing the Debtor had going for it was its brand – which the Debtor fraudulently transferred away on the eve of bankruptcy. The prospects that Hudson would fully cooperate with the Trustee seemed small given that

he had failed to fully comply with the Court's order permitting Beasley to conduct a Rule 2004 examination, and was not fully cooperating with the Examiner even though the Debtor had stipulated to the Examiner's appointment.

193. In only about a year, the Trustee had transformed the Debtor into an entity for which a proper plan could be formulated, with realistic historical and projected financial information. He and his staff quickly acted to try to gain control over accounting functions. Among other things, he regained ownership of the intellectual property, he gained control over the website and social media accounts, he hired new management to run the business, he instituted proper accounting and inventory controls, he participation in the recreation of multiple years of financial data to address the Debtor's historical failure to properly report and pay taxes and make the Debtor more saleable, he resolved certain personnel issues, and he efficiently resolved various pending litigation matters. In addition, the decisions made by the Trustee in this case greatly reduced the amount of legal fees that might have been incurred by the estate. Particularly because of the level of self-dealing, some trustees might have been extremely aggressive in suing Hudson, Hudson's entities, and anyone associated with Hudson to recover transfers made to them. The Trustee was much more precise, and ultimately filed only two lawsuits – one against Roscoe's IP to avoid the fraudulent transfer of the Debtor's intellectual property, and one against DV to recover the Debtor's social media accounts. He did not file a host of lawsuits to avoid and recover transfers. Instead of continuing to litigate claim objections, he entered into stip-

ulations that ensured that certain claims were subordinated to the claims of creditors the Trustee determined to hold legitimate claims. Although substantial fees were paid to professionals in this case, the amount of fees could have been much higher had the Trustee not taken the measured approach that he did.

194. The Trustee did not risk complete nonpayment in this case. However, he risked underpayment because of § 326(a). The Trustee and his staff expended substantial time during the first two interim periods, which covered the first full year after the Trustee's appointment. Even after a year of operating the Debtor's business, because of the substantial amount of work required during the first interim period, the amount allowable under § 326(a) still was less than the amount that would have been incurred by the Trustee and his staff at their regular non-trustee rates.

195. Combining the lodestar and an appropriate enhancement, the Court has no trouble finding that the amount of reasonable compensation for the Trustee's services in this case could be calculated utilizing a blended hourly rate of $700 or more per hour. That would produce a total award of $1,184,540 or more.

196. "In a case under chapter 7 or 11 . . . the court may allow reasonable compensation under section 330 of this title of the trustee for the trustee's services, payable after the trustee renders such services, not to exceed 25 percent on the first $5,000 or less, 10 percent on any amount in excess of $5,000 but not in excess of $50,000, 5 percent on any amount in excess of $50,000 but not in excess of $1,000,000, and reasonable compensation not to exceed 3 percent of such

moneys in excess of $1,000,000, upon all moneys disbursed or turned over in the case by the trustee to parties in interest, excluding the debtor, but including holders of secured claims.." 11 U.S.C. § 326(a). In this case, the amount allowable under § 326(a) is $1,155,844.71.

III. CONCLUSION

Based upon the foregoing Findings of Fact and Conclusions of Law, this Court shall enter its order in accordance herewith, granting the Final Fee Application and awarding the Trustee fees, on a final basis, in the total amount of $1,155,844.71.

DATED: NOVEMBER 18, 2020

/s/ Sheri Bluebond

United States Bankruptcy Judge

APPENDIX E

STATUTORY AND CONSTITUTIONAL PROVISIONS INVOLVED

U.S. Constitution

Article III. The Judiciary

Section 1. The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish. The Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behaviour, and shall, at stated Times, receive for their Services, a Compensation, which shall not be diminished during their Continuance in Office.

Section 2. The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority;--to all Cases affecting Ambassadors, other public Ministers and Consuls;--to all Cases of admiralty and maritime Jurisdiction;--to Controversies to which the United States shall be a Party;--to Controversies between two or more States;--between a State and Citizens of another State;--between Citizens of different States,--between Citizens of the same State claiming Lands under Grants of different States, and between a State, or the Citizens thereof, and foreign States, Citizens or Subjects.[1]

In all Cases affecting Ambassadors, other public Ministers and Consuls, and those in which a State shall be Party, the supreme Court shall have original Jurisdiction. In all the other Cases before mentioned, the supreme Court shall have appellate Jurisdiction, both as to Law and Fact, with such Exceptions, and under such Regulations as the Congress shall make.

The Trial of all Crimes, except in Cases of Impeachment, shall be by Jury; and such Trial shall be held in the State where the said Crimes shall have been committed; but when not committed within any State, the Trial shall be at such Place or Places as the Congress may by Law have directed.

Section 3. Treason against the United States, shall consist only in levying War against them, or in adhering to their Enemies, giving them Aid and Comfort. No Person shall be convicted of Treason unless on the Testimony of two Witnesses to the same overt Act, or on Confession in open Court.

The Congress shall have Power to declare the Punishment of Treason, but no Attainder of Treason shall work Corruption of Blood, or Forfeiture except during the Life of the Person attainted.

11 U.S.C. § 326. Limitation on compensation of trustee

(a) In a case under chapter 7 or 11, other than a case under subchapter V of chapter 11, the court may allow reasonable compensation under section 330 of this title of the trustee for the trustee's services, payable after the trustee renders such services, not to exceed 25 percent on the first $5,000 or less, 10 percent on any amount in excess of $5,000 but not in excess of $50,000, 5 percent on any amount in excess of $50,000 but not in excess of $1,000,000, and reasonable compensation not to exceed 3 percent of such moneys in excess of $1,000,000, upon all moneys disbursed or turned over in the case by the trustee to parties in interest, excluding the debtor, but including holders of secured claims.

(b) In a case under subchapter V of chapter 11 or chapter 12 or 13 of this title, the court may not allow compensation for services or reimbursement of expenses of the United States trustee or of a standing trustee appointed under section 586(b) of title 28, but may allow reasonable compensation under section 330 of this title of a trustee appointed under section 1202(a) or 1302(a) of this title for the trustee's services, payable after the trustee renders such services, not to exceed five percent upon all payments under the plan.

(c) If more than one person serves as trustee in the case, the aggregate compensation of such persons for such service may not exceed the maximum compensation prescribed for a single trustee by subsection (a) or (b) of this section, as the case may be.

(d) The court may deny allowance of compensation for services or reimbursement of expenses of the trustee if the trustee failed to make diligent inquiry into facts that would permit denial of allowance under section 328(c) of this title or, with knowledge of such facts, employed a professional person under section 327 of this title.

11 U.S.C. § 330. Compensation of officers

(a)(1)the United States Trustee and a hearing, and subject to sections 326, 328, and 329, the court may award to a trustee, a consumer privacy ombudsman appointed under section 332, an examiner, an ombudsman appointed under section 333, or a professional person employed under section 327 or 1103--

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

(B) reimbursement for actual, necessary expenses.

(2) The court may, on its own motion or on the motion of the United States Trustee, the United States Trustee for the District or Region, the trustee for the estate, or any other party in interest, award compensation that is less than the amount of compensation that is requested.

(3) In determining the amount of reasonable compensation to be awarded to an examiner, trustee under chapter 11, or professional person, the court shall consider the nature, the extent, and the value of such services, taking into account all relevant factors, including--

(A) the time spent on such services;

(B) the rates charged for such services;

(C) whether the services were necessary to the administration of, or beneficial at the time at which the service was rendered toward the completion of, a case under this title;

(D) whether the services were performed within a reasonable amount of time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed;

(E) with respect to a professional person, whether the person is board certified or otherwise has demonstrated skill and experience in the bankruptcy field; and

(F) whether the compensation is reasonable based on the customary compensation charged by comparably skilled practitioners in cases other than cases under this title.

(4)(A) Except as provided in subparagraph (B), the court shall not allow compensation for--

(i) unnecessary duplication of services; or

(ii) services that were not--

(I) reasonably likely to benefit the debtor's estate; or

(II) necessary to the administration of the case.

(B) In a chapter 12 or chapter 13 case in which the debtor is an individual, the court may allow reasonable compensation to the debtor's attorney for representing the interests of the debtor in connection with the bankruptcy case based on a consideration of the

benefit and necessity of such services to the debtor and the other factors set forth in this section.

(5) The court shall reduce the amount of compensation awarded under this section by the amount of any interim compensation awarded under section 331, and, if the amount of such interim compensation exceeds the amount of compensation awarded under this section, may order the return of the excess to the estate.

(6) Any compensation awarded for the preparation of a fee application shall be based on the level and skill reasonably required to prepare the application.

(7) In determining the amount of reasonable compensation to be awarded to a trustee, the court shall treat such compensation as a commission, based on section 326.

(b)(1) There shall be paid from the filing fee in a case under chapter 7 of this title $45 to the trustee serving in such case, after such trustee's services are rendered.

(2) The Judicial Conference of the United States--

(A) shall prescribe additional fees of the same kind as prescribed under section 1914(b) of title 28; and

(B) may prescribe notice of appearance fees and fees charged against distributions in cases under this title;

to pay $15 to trustees serving in cases after such trustees' services are rendered. Beginning 1 year after the

date of the enactment of the Bankruptcy Reform Act of 1994, such $15 shall be paid in addition to the amount paid under paragraph (1).

(c) Unless the court orders otherwise, in a case under chapter 12 or 13 of this title the compensation paid to the trustee serving in the case shall not be less than $5 per month from any distribution under the plan during the administration of the plan.

(d) In a case in which the United States trustee serves as trustee, the compensation of the trustee under this section shall be paid to the clerk of the bankruptcy court and deposited by the clerk into the United States Trustee System Fund established by section 589a of title 28.

(e)(1) There is established a fund in the Treasury of the United States, to be known as the "Chapter 7 Trustee Fund", which shall be administered by the Director of the Administrative Office of the United States Courts.

(2) Deposits into the Chapter 7 Trustee Fund under section 589a(f)(1)(C) of title 28 shall be available until expended for the purposes described in paragraph (3).

(3) For fiscal years 2021 through 2026, the Chapter 7 Trustee Fund shall be available to pay the trustee serving in a case that is filed under chapter 7 or a case that is converted to a chapter 7 case in the most recent fiscal year (referred to in this subsection as a "chapter 7 case") the amount described in paragraph (4) for the chapter 7 case in which the trustee has rendered services.

(4) The amount described in this paragraph shall be the lesser of--

(A) $60; or

(B) a pro rata share, for each chapter 7 case, of the fees collected under section 1930(a)(6) of title 28 and deposited to the United States Trustee System Fund under section 589a(f)(1) of title 28, less the amounts specified in section 589a(f)(1)(A) and (B) of title 28.

(5) The payment received by a trustee under paragraph (3) shall be paid in addition to the amount paid under subsection (b).

(6) Not later than September 30, 2021, the Director of the Administrative Office of the United States Courts shall promulgate regulations for the administration of this subsection.

11 U.S.C. § 1109. Right to be heard

(a) The Securities and Exchange Commission may raise and may appear and be heard on any issue in a case under this chapter, but the Securities and Exchange Commission may not appeal from any judgment, order, or decree entered in the case.

(b) A party in interest, including the debtor, the trustee, a creditors' committee, an equity security holders' committee, a creditor, an equity security holder, or any indenture trustee, may raise and may appear and be heard on any issue in a case under this chapter.

11 U.S.C. § 1124. Impairment of claims or interests

Except as provided in section 1123(a)(4) of this title, a class of claims or interests is impaired under a plan unless, with respect to each claim or interest of such class, the plan--

(1) leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest; or

(2) notwithstanding any contractual provision or applicable law that entitles the holder of such claim or interest to demand or receive accelerated payment of such claim or interest after the occurrence of a default--

(A) cures any such default that occurred before or after the commencement of the case under this title, other than a default of a kind specified in section 365(b)(2) of this title or of a kind that section 365(b)(2) expressly does not require to be cured;

(B) reinstates the maturity of such claim or interest as such maturity existed before such default;

(C) compensates the holder of such claim or interest for any damages incurred as a result of any reasonable reliance by such holder on such contractual provision or such applicable law;

(D) if such claim or such interest arises from any failure to perform a nonmonetary obligation, other than a default arising from failure to operate a nonresidential real property lease subject to section 365(b)(1)(A), compensates the holder of such

claim or such interest (other than the debtor or an insider) for any actual pecuniary loss incurred by such holder as a result of such failure; and

(E) does not otherwise alter the legal, equitable, or contractual rights to which such claim or interest entitles the holder of such claim or interest.

11 U.S.C. § 1126. Acceptance of plan

(a) The holder of a claim or interest allowed under section 502 of this title may accept or reject a plan. If the United States is a creditor or equity security holder, the Secretary of the Treasury may accept or reject the plan on behalf of the United States.

(b) For the purposes of subsections (c) and (d) of this section, a holder of a claim or interest that has accepted or rejected the plan before the commencement of the case under this title is deemed to have accepted or rejected such plan, as the case may be, if--

(1) the solicitation of such acceptance or rejection was in compliance with any applicable nonbankruptcy law, rule, or regulation governing the adequacy of disclosure in connection with such solicitation; or

(2) if there is not any such law, rule, or regulation, such acceptance or rejection was solicited after disclosure to such holder of adequate information, as defined in section 1125(a) of this title.

(c) A class of claims has accepted a plan if such plan has been accepted by creditors, other than any entity designated under subsection (e) of this section, that hold at least two-thirds in amount and more than one-half in number of the allowed claims of such class held by creditors, other than any entity designated under subsection (e) of this section, that have accepted or rejected such plan.

(d) A class of interests has accepted a plan if such plan has been accepted by holders of such interests, other

than any entity designated under subsection (e) of this section, that hold at least two-thirds in amount of the allowed interests of such class held by holders of such interests, other than any entity designated under subsection (e) of this section, that have accepted or rejected such plan.

(e) On request of a party in interest, and after notice and a hearing, the court may designate any entity whose acceptance or rejection of such plan was not in good faith, or was not solicited or procured in good faith or in accordance with the provisions of this title.

(f) Notwithstanding any other provision of this section, a class that is not impaired under a plan, and each holder of a claim or interest of such class, are conclusively presumed to have accepted the plan, and solicitation of acceptances with respect to such class from the holders of claims or interests of such class is not required.

(g) Notwithstanding any other provision of this section, a class is deemed not to have accepted a plan if such plan provides that the claims or interests of such class do not entitle the holders of such claims or interests to receive or retain any property under the plan on account of such claims or interests.