UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEW MEXICO

In re:

FURR'S SUPERMARKETS, INC., Case No. 11-01-10779 SA
Tax I.D. No. 22-3137244,

Debtor.

UNITED STATES TRUSTEE'S MEMORANDUM IN SUPPORT OF OBJECTION TO APPLICATION FOR EMPLOYMENT OF PRICE WATERHOUSECOOPER'S LLP

The United States Trustee for the District of New Mexico hereby submits the following memorandum in support of her objection to the application for employment of PricewaterhouseCoopers LLP (Application). As an initial matter, it is the U.S. Trustee's understanding that most of the points of her objection filed here on March 8, 2001, have been resolved as set out in the amended objection filed herein. This leaves two issues for resolution. The first relates to the retainer which PricewaterhouseCoopers LLP (hereafter PWC) received from the Debtor. The second relates to the reasonableness of hourly fees which PWC proposes in this matter.

I. Statement of Facts

PWC received a retainer of $200,000 from the Debtor on February 2, 2001. Initially, in the letter agreement attached to the original employment application filed herein on February 8, 2001, PWC stated, "Our customary practicing engagements such as this is to receive an initial retainer of $200,000. The retainer, which is payable upon the execution of this letter, will be held and applied to the final bill for the services, with any excess refunded to you. *See* letter dated February 2, 2001, from Loretta R. Cross to Tom Dahlen attached to Application for Order under

11 U.S.C. 327(a) and Federal Rule of Bankruptcy Procedure 2014 Authorizing the Employment of PricewaterhouseCoopers LLP, s the Debtor's Financial Consultants, Docket No.15.

Subsequently, Loretta Cross stated as follows:

> PWC received a retainer of $200,000 on February 2, 2001. On February 2, 2001, the retainer was received, deposited in PWC's operating cash management system as pre-paid fees, and applied as a credit balance to the Debtor's account for services rendered or to be rendered on or after February 1, 2001. For the period from February 1, 2001, through the date of the filing of the Bankruptcy Case, the fees and expenses that PWC earned and incurred assisting the Debtor with its pre-bankruptcy planning and negotiations amount to $128,541 and $9,676.75, respectively, for total of $138,217.75. The remaining credit balance of $60,782.25 has been set aside as a post-petition retainer with other bankruptcy retainers paid to PWC, and will be available to apply to compensation charge for post-petition services.

Amended and Restated Declaration of Loretta Cross in Support of Application for Order under 11 U.S.C.§§327 (A) and Federal Rule of Bankruptcy Procedure 2014 Approving Retention of PricewaterhouseCoopers, LLP as Debtor's Financial Consultants, at ¶ 20. Docket No. ?

II. The Burden Is on PWC to Establish the Reasonableness of Its Employment Application

As an initial matter, the Court authorizes the employment of professional persons under §327 or §1103, "on any reasonable terms and conditions of employment, including on a retainer..." 11 U.S.C.§328(a). Further, the burden of proof to establish that proposed terms and conditions of employment are reasonable falls on the professional. *In re Gillett Holdings, Inc.*, 137 B.R. 452, 455 (Bankr.D.Col.1991); *In re C & P Auto Transport, Inc.*, 94 B.R. 682,686 (Bankr.E.D.Cal.1988). In this case therefore, the burden of showing that the retainers and hourly rates are reasonable, is on PWC.

III. The Terms of the Retainer Required by PWC All Are Not Reasonable under the Terms of the Bankruptcy Code.

In determining the reasonableness of retainers, bankruptcy law is the primary source of standards. As stated by one court,

> The Court must be persuaded that the terms and conditions of employment are in the interest in the estate. The decision is a matter of discretion and is made against the background of the statutory compensation scheme of Sections 330 and 331, which scheme is, as a matter of law, reasonable. . 129 B.R. 212,220 (Bankr.D.Col.1991).

Therefore, reasonableness is not only measured by the quantitative amounts but also qualitative factors such as whether the terms of the retainer comply with the statutory scheme set forth in 11 U.S.C.§§327-331. *In re NBI, Inc*., 129 B.R. at 222.

In addressing the former, there are three different types of retainers, including: (1)classic retainers, (2) advance payment retainers, and (3) security retainers. See *In re Sheridan,* 215 B.R. 144 (Bankr.N.D. Ill.1996). Under the initial terms of the letter agreement dated February 2, 2001, and executed by both PWC and Mr. Dahlen, on behalf of Furr's, the retainer of $200,000 is clearly a security retainer. As stated in the agreement, that amount was to be held and applied to PWC's final bill for services. The second explanation given by PWC for the retainer, clearly classifies it as an advance payment retainer, since it was deposited in PWC's accounts as "pre-paid fees."

In attempting to determine the true character of the retainer, the documents clearly show that the intent of the parties was to have a security retainer arrangement in place. The terms of the letter agreement dated February 2, 2001, unequivocally state that the $200,000 was to be applied to the PWC's final bill in this matter. The terms were dictated by PWC, and agreement thereto by Furr's is shown by the signature of its president, Tom Dahlen. Only after the U.S. Trustee objected to PWC's employment application (in part on the terms of the retainer), did PWC file the Amended Declaration instead, stating that the retainer had largely been applied to pre-paid fees. Nowhere in the Amended Declaration is Furr's agreement to the change in terms

indicated. As such, the Amended Declaration appears to be an attempt to unilaterally and retroactively, alter the terms. This, PWC cannot do. Once this case was filed, the retainer given to PWC became property of the estate. 11 U.S.C.§541; *In re Amdura Corp.,* 139 B.R. 963,987 (Bankr.D.Col.1992). See also *In re Hathaway Ranch Partnership,* 116 B.R. 208, 217 (Bankr.C.D.Cal.1990).

In the case of a normal security retainer, in which a professional after notice and hearing first exhaust the amounts held in the retainer before billing the Debtor, the Code recognizes and accepts this arrangement. See *In re NBI, Inc*., 129 B.R. at 224; *In re Martin,* 817 F.2d 175 (1st Cir. 1987). However, the provision reserving the retainer for application to a final billing in this proceeding in effect gives PWC a security interest, and therefore a priority to other administrative claimants at the conclusion of this proceeding. As such, it is not in keeping with the underlying purposes of §§ 328 and 503(b) and is therefore unreasonable. In addition, it may well create a disqualifying preference to PWC, since it is not a contemporaneous exchange of value for services. 11 U.S.C. §547. Therefore if the retainer is interpreted as one for security, Court approved fees should be paid from the retainer until exhausted, prior to billing the Debtor.

If the retainer is found to be an advance fee retainer as characterized in the Amended and Restated Declaration of Loretta Cross, it is nonetheless objectionable since it runs counter to the underlying purposes of the Code. As simply stated by one Court, "Parties in interest and the Court have the right, if not the duty, to monitor the conduct of a case and related expenditures which have a potential impact on the assets of the estate." *In re NBI, Inc*., 129 B.R. at 223 (Bankr.D.Col 199). Where "pre-paid" fees are deposited in a professional's general account, this can be difficult since:

> The debtor-in-possession, as fiduciary to the bankruptcy estate, must maintain and account for all property of the estate to its creditors and to this court. It is impossible for the debtor-in-possession to do so if its attorney has deposited an advance fee payment in its operating account and treats the funds as the professional's own money. *In re Hathaway Ranch Partnership,* 116 B.R. at 217-218.

The advanced fee payment (if indeed it is characterized as such) to PWC is therefore unreasonable insofar is as it was deposited into PWC's operating account.

Finally, although PWC stated that it rendered services and incurred expenses of over $138,000 in the week before the filing of this proceeding, it has refused to disclose when a billing was made or when amounts from the retainer were credited in payment of the fees. To the extent that there was a post-petition allocation of a portion of the retainer to payment of pre-petition fees and expenses, it was improper. *In re Amdura Corp*., 139 B.R. at 987, *In re Independent Engineering Co., Inc.*, 197 F.3d 13 (1st Cir.1999). If in fact this is the case, PWC must also deal with its status as a pre-petition creditor, and its compliance with the disinterestedness standard. Further, the U.S. Trustee respectfully request that PWC be required to disclose the date on which it billed and paid its pre-petition claims from the retainer.

IV. The Hourly Rates Requested by PWC Are Excessive and Therefore Unreasonable

PWC, in the Amended and Restated Declaration of Loretta Cross (Declaration), has set forth the hourly rates for its professionals at paragraph 16. The rates range from $100 for associates and analysts up to $595 for partners. As regard to "core team members" who are or will be assigned to provide services to the Debtor, the hourly rates range from $220 to $570 an hour. Declaration at ¶17. The U.S. Trustee respectfully submits that the hourly rates are excessive in the circumstances of this case.

As a starting point, the Tenth Circuit has stated that, absent unusual circumstances, "[T]he fee rates of the local area should be applied even when the lawyers seeking fees are from another area." Ramos v. Lamm, 713 F.2d 546, 555 (10th Cir.1983) (civil rights case often cited as authority in bankruptcy fee matters). In this case, as regards accounting firms, the U.S. Trustee was unable to obtain evidence of rates for financial consulting in the local area similar to those described for PWC in this case. However, certain case law has used as a factor the magnitude of the case at issue in determining the appropriateness of the rates. See *In re Zolfo, Cooper & Co.,* 50 F.3d 253 (3rd Cir. 1995*); In re Frontier Airlines,* 74 B.R. 973, 977 (Bankr.D.Col 1987).

In this case, United States Trustee has obtained a copy of an employment application for PWC which was filed in September 2000 in *In re Edwards Theater Circuit,* Case No. SA 00-16475-LR (Bankr.C.D.Cal 2000) . See UST Exhibit No.14. In that matter, PWC requested fees ranging from $90 for assistants to $450 for partners/directors. As is evident from the caption of the case, seven different entities and proceedings have been administratively consolidated. Additionally, as is evident from the summary of schedules attached to the exhibit, both the assets and liabilities substantially exceed the amounts at issue in this case. On its face, the *Edwards Theater Circuit* case appears to be more complex, if only from the multiple entities involved. It is indeed difficult to understand how the hourly rates proposed by PWC in this case should be substantially higher than in the California case, in which PWC filed its employment application approximately five months before the above referenced matter.

As stated above, it is the burden of PWC to establish that the terms of its employment application are reasonable. Without having had the opportunity to view the evidence which PWC intends to introduce that the final hearing on this matter, it is difficult to anticipate the matters to

be presented. However, the U.S. Trustee respectfully submits that PWC's burden is extremely heavy in light of the above.

In light of the above, United States Trustee respectfully requests that the PWC's employment application be denied. Alternatively, the U.S. Trustee requests that (1) deficiencies with the retainer be corrected and (2) that hourly rates be reduced to reasonable levels as conditions to its employment.

Respectfully submitted,

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United States Trustee

Filed electronically 4/16/01
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The undersigned certifies that a true and accurate copy of the foregoing was mailed and sent by telefacsimile to the below listed counsel this 16th day of April, 2001.

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