

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

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DISTRICT COURT
ALBUQUERQUE, N.M.

In Re:

FURR'S SUPERMARKETS, INC.,

Chapter 11
Case Nos. 01-10779-SA

Debtor.

No Hearing Date Set

**RESPONSE OF PEPPER HAMILTON LLP TO THE OBJECTIONS OF FURR'S
SUPERMARKET, INC., HELLER FINANCIAL, INC. AND THE UNITED STATES
TRUSTEE TO ITS FIRST INTERIM APPLICATION FOR THE ALLOWANCE AND
PAYMENT OF COMPENSATION FOR SERVICES RENDERED IN THE PERIOD
FEBRUARY 14, 2001 TO JUNE 30, 2001 AND THE APPLICATION FOR
REIMBURSEMENT OF EXPENSES OF MEMBERS OF OFFICIAL UNSECURED
CREDITORS' COMMITTEE**

PEPPER HAMILTON LLP, on behalf of itself and the Official Committee of Unsecured Creditors ("Committee"), responds to the objections of Furr's Supermarket, Inc. ("Furr's"), Heller Financial, Inc., as agent for itself, Bank of America, N.A., Fleet Capital Corporation and Metropolitan Life Insurance Company (collectively "Heller") and the United States Trustee ("US Trustee") to its First Interim Application for the Allowance and Payment of Compensation for Services Rendered in the Period February 14, 2001 to June 30, 2001 (the Fee Application") and the Objections of Furr's and Heller to the Application for the Reimbursement of Expenses of Members of the Official Unsecured Creditors' Committee (the "Expense Application"), as follows:

1. On February 8, 2001, the Debtor filed a voluntary petition under Chapter 11 of the Bankruptcy Code (the "Code").

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2. On or about February 13, 2001, the United States Trustee appointed the Committee under Section 1102 of the Code.

3. On February 14, 2001, at a scheduled telephonic conference call of the Committee, at which all of its members were present, and pursuant to the provisions of Section 1103 of the Code, the Committee selected and authorized the employment of Pepper Hamilton LLP to serve as its general counsel.

4. On February 20, 2001, the Committee filed its Application for Order Pursuant to 11 U.S.C. § 327(a) Authorizing the Retention and Employment of Pepper Hamilton (the "Retention Application").

INTRODUCTION

5. In support of its "First Day Motions and Applications," the Debtor submitted the 43 page, 116 paragraph Declaration of Steven L. Mortensen, the Debtor's then Vice-President and Chief Financial Officer. Mr. Mortensen averred that the Company (i) has "generated annual revenues of \$700-\$800 million," (ii) is "one of New Mexico's largest private employers, with almost 5,000 employees, the majority of which are unionized," (iii) has over "13,000 creditors in this case, and total claims [exceeding] \$280 million," and (iv) has "secured creditors, including the lenders under the proposed debtor-in-possession credit facility, [that] are among the nation's largest and most sophisticated financial institutions." Mortensen Declaration, ¶23, p. 6.

6. For these reasons, among others, Mr. Mortensen declared that the Company required "the services of a large, national, full-service law firm . . . with the expertise and

experience, not only in large and complicated chapter 11 cases, but also in transactional, labor, tax, and other legal [sic] issues likely to arise in this case.” Mortensen Declaration, ¶24, p. 7.

7. Like the secured lenders in this case, the Committee members also are among the nation’s largest and most sophisticated companies, including Kraft Foods, Conagra Foods, Inc., Nestlé USA, Pepsi Bottling Group, among others. Their designated representatives are senior executives, many of whom have been members of unsecured creditors’ committees in some of the largest chapter 11 cases ever filed in the United States. The Committee members are also a geographically diverse group, with representatives from Cincinnati, Omaha, Colorado Springs, Chicago, Winston-Salem, Los Angeles, Grapevine (Texas), as well as Albuquerque.

8. For reasons similar to those stated by Mr. Mortensen, the Committee too concluded that it required the services of a large, national, full-service law firm with the expertise and experience, not only in large and complicated chapter 11 cases, but also in transactional, labor, tax, and other legal issues likely to arise in this case.

9. As is customary of committees generally, in-person committee meetings with the debtor are held regularly. The scheduling of the meetings is a function of time and location, as well as the speed at which the case is moving. In the early stages of this case covering the time period of the Applications, in-person Committee meetings were held on February 21, 2001 in Chicago, April 18, 2001 in New York, May 9, 2001 in Dallas. In addition to these Committee meetings, meetings between representatives of the Debtor and certain sub-committees were held on two occasions in Denver, Colorado. As the Debtor’s objection notes, the locations of the Dallas and Chicago meetings were determined by a number of factors, including availability of flights and the convenience and centrality of the location. With respect to the April

meeting, the New York location was suggested *by the Debtor* in order to accommodate meetings between the Debtor and certain of the lenders in the case which were to be held immediately prior to and after the Committee meeting. Similarly, two sub-committee meetings were held in Denver at the suggestion and request of the Debtor, in one instance to accommodate the schedule of Debtor's counsel and, in the other instance, to accommodate the schedule and needs of the Debtor's officers.

10. As is the case with any geographically diverse group, it was impossible for certain Committee members to fly in and out of the meeting location on the same day and, therefore, in limited instances, an overnight stay was required. These overnight stays, however, were put to good use, with at least a portion of the evening spent in additional meetings of the Committee or the applicable sub-committee. Between in-person meetings, numerous Committee and sub-committee meetings were held by conference call.

11. Committee meetings generally begin very early in the morning and last all or most of the day. The agenda is typically divided among a report by Committee counsel and a discussion of the significant legal issues confronting the Debtor and the Committee, a report by the Committee's financial advisors regarding the Debtor's current financial condition, the financial impact of the Debtor's proposals and the Debtor's longer term outlook, and, ultimately, a report by the Debtor's senior management and its professionals.

12. At the conclusion of the meeting, it is the practice of the Committee to schedule the next in-person meeting, thereby insuring that Committee members will have at least one month within which to make appropriate travel arrangements. In this case, however, the Committee's ability to schedule meetings well in advance (and thereby reap the benefit of reduced

costs for airfare) was hampered by the Debtor's senior managements' inability to commit to a pre-determined date and time. As a result, in-person Committee meetings with the Debtor were scheduled on substantially shorter notice, with a concomitant increase in airfare and related costs. Nevertheless, Committee members seek reimbursement for coach fares only, and any Committee member who traveled first-class was able to do so only because they were able to upgrade at no additional expense to the estate.

13. From the inception of this case, and throughout most of the period covered by the Applications at issue, the Debtor repeatedly and consistently emphasized the fundamental viability of the Company and exuded a confidence in the Company's ability to successfully reorganize. In his affidavit, for example, Mr. Mortensen averred that "[T]he Company does not anticipate a prolonged chapter 11 case. With the support of the Company's employees, vendors, customers, and other constituents, the Company believes that the implementation of this plan will resolve its operational and financial difficulties, enhance the Company's viability and profitability, and permit the Company to successfully reorganize and exit from chapter 11 at the earliest possible and appropriate time." Mortensen Declaration, ¶116, p. 43.

14. The Company's sanguine predictions were consistently echoed at every opportunity, including at all meetings with the Committee and its advisors. Through its actions, the Company also evidenced its firm belief in its fundamental ability to successfully reorganize. For example, the Company withdrew its initial severance and retention bonus program proposal on the grounds that it was no longer necessary in light of the Company's overall prospects. Similarly, the Company demurred to the Committee's recommendation on the implementation of a "trade lien," a mechanism to reestablish the availability of trade credit and enhance trade

creditor confidence, on the ground that the implementation of a trade lien was no longer necessary to effectuate these goals.

15. Extensive requests for financial information regarding the liquidity and solvency of the Debtor were made by the Committee's financial advisors in an effort to obtain an accurate picture of the Debtor's current financial condition. The Committee's efforts to validate the Debtor's optimistic assessment of its prospects for a successful restructuring, however, were hampered by the Debtor's delay in providing critical financial information to the Committee and in filing its monthly operating reports.

16. Moreover, when the Company did discuss pursuing parallel paths of a stand alone restructuring and the prospect of a going concern sale, it always emphasized that the implementation of operational changes would significantly enhance the sale value of the company sufficient to result in a distribution to unsecured creditors. Indeed, it was not until the very end of this Application period that the Debtor announced that it was abandoning its efforts toward a stand-alone plan of reorganization in favor a quick asset sale to Fleming, and that the sale proceeds alone would likely be insufficient to result in a distribution to unsecured creditors. Nevertheless, even at this juncture, the Debtor continued to assert that Fleming would likely "put back" dozens of unencumbered and extremely valuable store leases, and that the disposition of these valuable leases would result in a significant distribution to unsecured creditors.

17. Although the disposition of these leases and the sale of the Company occurred after the conclusion of this Application period, it is relevant to note that, upon learning of the possibility of an administrative insolvency in this case, the Committee took immediate steps to reduce its efforts and contain expenses. By way of example, although in-person meetings are

the preferred method of efficiently conducting Committee business, no in-person Committee meetings were held after the May 9, 2001; all future business of the Committee (and all sub-committees) was conducted *exclusively* by telephone conference calls. See, In re Auto Parts Club, Inc., 211 B.R. 29, 35 (B.A.P. 9th Cir. 1997) (services by committee counsel should be scaled back once it becomes obvious that there will be no distribution to unsecured creditors).

ARGUMENT

I. RESPONSE TO OBJECTIONS REGARDING PEPPER HAMILTON LLP

18. The Objections of Furr's, Heller and the US Trustee can be divided into four categories. The first category involves challenges to work performed after it was determined that a distribution to unsecured creditors was unlikely. In a scant four paragraphs, Heller, joined by Furr's, objects that work performed by Committee counsel (or expenses incurred by Committee members) could not benefit the estate since there was little likelihood of a distribution to unsecured creditors. The second category involves non-specific allegations of duplication. The third category relates to so-called staffing concerns. The final category contains miscellaneous objections to fees and expenses.

Benefit of Services

19. Turning to the first category, Heller's and Furr's objections are premised entirely on an inaccurate recitation of the operative facts and the application of an erroneous legal standard. The issue is not, as Heller and Furr's contend, whether an ultimate distribution to unsecured creditors occurs in this case. Rather, "the standard is an objective one as to whether the fees were reasonable and necessary *at the time they were incurred.*" In re Auto Parts Club, Inc., 211 B.R. 29, 35 (B.A.P. 9th Cir. 1997) (emphasis added). As recognized by the Bankruptcy

Appellate Panel for the Tenth Circuit, "Courts cannot limit their inquiry to an evaluation of whether the services actually benefitted the estate. Instead, the court must make a determination whether or not it was probable or likely that the services would benefit the estate." In re Double J Cattle Co., 226 B.R. 284 (Table); 1997 WL 837762, **5 (B.A.P. 10th Cir. 1997).

20. In Double J Cattle, the 10th Circuit Bankruptcy Appellate Panel reversed a fee order premised upon a *per se* rule that, because there was no return to pre-petition unsecured creditors, there could be no corresponding benefit to the estate. Rather, relying on Auto Parts Club, *supra*, the Double J Cattle Panel held that "[t]he concept of 'benefit to the estate' is not necessarily limited to an economic approach along the line that a dollar's worth of services must directly benefit the estate and bring a cash dollar into the estate in order to justify allowance of such dollar in cash compensation . . . [O]ther factors besides the economic impact on the estate of actions taken should be considered in the 'benefit to the estate' analysis." In re Double J Cattle, *supra* at **6, quoting In re Spanjer Brothers, Inc., 203 B.R. 85, 90 (Bankr. N.D. Ill. 1996).

21. First and foremost, such other factors include an analysis of whether, at the time such services were rendered and without the benefit of hindsight, counsel's services were *reasonably likely* to benefit the debtor's estate, not whether counsel is able to show *actual benefit* to the estate. In re Mednet, 251 B.R. 103, 107 (B.A.P. 9th Cir. 2000) (italics in original). Accord, In re Ames Department Stores, Inc., 76 F.3d 66, 71-72 (2d Cir. 1996) (remanding to bankruptcy court for a determination of the fees of Skadden, Arps, *et. al.*, Debtor's counsel in the instant case, on the grounds that Skadden's fee entitlement should not be "made contingent upon a showing of actual benefit to the estate." Rather, the test to apply is based upon whether such

services were reasonably likely to benefit the estate and what services a reasonable lawyer or legal firm would have performed in the same circumstances.)

22. As succinctly stated by Judge Yacos in connection with the fee request of Furr's bankruptcy counsel, Richard Levin, while a member of the law firm Stutman, Treister, *et al.*,

The court is well aware of the uncertain world of fact and law in which the reorganization lawyer must dwell under the pressures of time and expense in moving forward with a reorganization plan. It is a shadowy realm of incomplete facts and unformed legal issues that must be mastered quickly under manifold time pressures. What seems crystal clear and simple in hindsight when the reorganization is accomplished is seldom presented as such in the heat of battle. However, in the last analysis, final fee awards necessarily must take into account all the circumstances of a particular case, and the results of services provided as can only be evaluated at the conclusion of the proceeding. Billed hours are an important factor in that determination but are not by themselves controlling in the ultimate determination of "reasonable" compensation pursuant to the statute.

In re Public Service Co. of New Hampshire, 86 B.R. 7, 12 (Bankr. D.N.H. 1988). See also, In re Public Service Co. of New Hampshire, 102 B.R. 276, 278 (Bankr. D.N.H. 1989) ("Reorganization counsel are not required to guarantee the success of a reorganization effort."). Accord, In re Garrison Liquors, Inc., 108 B.R. 561, 564 (Bankr. D. Md. 1989). These standards, while often enunciated in connection with debtor's counsel, are equally applicable to counsel for the unsecured creditors' committee. In re Smith Technologies Corp., 1999 WL 1427681 at *6 (D. Del. 1999).

23. Only through the application of biased hindsight are either Heller or Furr's able to complain that the work performed during the Application period by counsel on behalf of

and at the direction of the Committee was of inadequate benefit to the estate in light of the anticipated distribution to unsecured creditors. As detailed above, *throughout most of this Application period*, the Debtor repeatedly and consistently emphasized the fundamental viability of the Company and exuded a confidence in the Company's ability to either successfully reorganize as a stand alone company or, alternatively, maximize value for an ultimate sale which would result in a significant distribution to unsecured creditors. Having represented the financial viability of the Debtor and solicited the involvement of its unsecured creditors through the instigation of this case, the Debtor and Heller cannot now be heard to complain that such work was not beneficial in light of the Debtor's failed reorganization.

24. As a corollary to this objection, Furr's specifically objects to all time billed in connection with the Committee's Motion to Appoint a Chapter 11 Trustee which, according to Furr's, "was never pursued, had no merit, did not benefit the estate, and was a waste of time and money." Furr's Objection, ¶13, p. 5. The Committee respectfully disagrees with Furr's opinion of the underlying merits of this Motion. A fundamental premise of the Committee's request for the appointment of an operating Trustee was the Debtor's refusal to undertake the promised operational restructuring necessary to accomplish the Company's self-proclaimed parallel tracks. The Committee correctly determined that, without these changes, the Company would not be in a position to propose either a feasible stand alone plan or maximize the Company's value, as was borne out by the results of the quick sale to Fleming. The Court's reluctance to hear the Trustee motion until after the hearing on the approval of the Fleming sale mooted much of the requested relief, since approval of the sale eliminated the opportunity to effectuate additional operational restructuring. After it became apparent that the Trustee motion

should not be heard prior to the sale hearing, the Committee and the Debtor agreed to postpone discovery or any other legal work on the Trustee motion to determine whether the sale hearing would moot the requested relief. Once this determination was made, the motion was held in abeyance. Fortuity in scheduling, however, does not translate into a lack of merit. Moreover, despite Furr's "scorecard," most of the work of a properly functioning committee takes place outside of the courtroom, and the number of pleadings filed by committee counsel is *not* an accurate barometer of a committee's value to the reorganization process.

Duplication

25. For their next objection, Furr's and Heller, and joined by the US Trustee allege without detail that Pepper Hamilton professionals duplicated each other's efforts (or the efforts of local counsel) in connection with the review of pleadings, attendance at meetings and inter-office conferences, among others events. However, as the Debtor averred under oath, the size and complexity of this case required "the services of a large, national, full-service law firm . . . with the expertise and experience, not only in large and complicated chapter 11 cases, but also in transactional, labor, tax, and other legal[sic] issues likely to arise in this case." Mortensen Declaration, ¶24, p. 7. As is the case with the Debtor's and lender's selection of counsel, the use of a full service firm necessitates the use of local counsel as well. With respect to the Committee, however, the involvement of local counsel at court hearings, meetings and the like, have resulted in significant savings to the estate in fees and expenses that would otherwise have been incurred by Applicant. The proper utilization of local counsel obviously requires that local counsel be fully prepared to advocate the Committee's position accordingly. Thus, inter-office conferences

and/or participation of local counsel at meetings is to be expected and encouraged if the benefits associated with the meaningful use of local counsel are to be realized.

26. Moreover, in a case of this complexity, it is not unusual to have more than one attorney present at meetings or conferences to be responsible for and lead discussions on discrete assigned issues that required reporting and discussion. Certainly, the Debtor's counsel had more than one attendee at significant meetings and conferences and, although Heller's lawyers are not required to file fee applications, Applicant assumes that a national law firm such as Latham & Watkins is equally familiar with this practice. The issues discussed at Committee meetings and on Committee conference calls were of a developing and on-going nature and required a comprehensive understanding of the issues and the positions taken by other professionals on those issues in order to effectively represent the Committee relative to the interests of other constituencies. It is not unreasonable that more than one professional would be called upon to have both the experience and issue-specific knowledge in discrete aspects of the case. In this manner, Committee counsel was able to present and discuss reports on numerous agenda items in both an efficient and expedient fashion, communicating to the Committee the complexities and nuances on the issues, as well as participating in substantive discussions with the Debtor's attorneys on matters which they brought to Committee meetings.

27. Conference calls are even less problematic. With the exception of a legal assistant who acted as the Committee Secretary, other professionals who addressed specific issues on which they had done analysis or research seldom stayed for the entire meeting. The legal assistant participated in meetings and conference calls for the purpose of taking notes, which were rewritten as minutes and then distributed to the full Committee. In addition, Committee and sub-

committee conference calls rarely lasted over two hours rather than the in-person meetings during the early stages of this case which frequently lasted all day.

28. Similarly, with regard to the intra-office conferences specifically and staffing in general, associates were assigned to review and analyze, if appropriate, all pleadings filed in this case, perform research on miscellaneous matters, analyze certain security documents, and the preparation of memoranda and reports for the Committee. In this way, the senior partners and the Committee members were kept informed of significant legal issues without the additional expense of several attorneys reviewing the same pleading. A legal assistant was assigned to perform services relative to the preparation of monthly fee statements and fee applications, to interface with the records department to organize all correspondence and documents for expedient reference and retrieval, to disseminate information to Committee members, attend Committee meetings as Committee Secretary and take notes, prepare minutes, and to attend to other matters that can be properly performed by a legal assistant. These services were performed at a fraction of the cost that would have been incurred had an attorney performed these same services.

29. It is Applicant's experience that this delegation of responsibility is an effective and highly cost-efficient method for managing a case of this size. This method, however, requires brief intra-office conferences among the professionals involved in order to coordinate efforts and permit the senior partners on this engagement to remain informed, manage the case effectively and to communicate appropriately with the other professionals and members of the Committee.