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Creditor's Self-Interest Precludes Fee Reimbursement From The Estate

OVERVIEW

In *In re Tropicana Entertainment LLC, et al.*, 2012 WL 3776531, No. 10-3970 (3d Cir. Aug. 31, 2012), the United States Court of Appeals for the Third Circuit ("the Third Circuit") recently held that the fees of an ad hoc noteholder committee ("the Noteholder Committee") were not reimbursable as an administrative expense. The fee request was denied because there was no evidence showing the committee's actions were not self-interested. Notably, the fees were not reimbursable despite the debtor's willingness to compensate the Noteholder Committee for its fees.

BACKGROUND

New Jersey's gaming commission revoked Tropicana's gaming license in the wake of a board member's gross mismanagement. Thereafter, the gaming commissions of other states threatened to revoke Tropicana's licenses to operate in those states, and the pre-bankruptcy Noteholder Committee urged the board member to step down. The board member refused, and the company eventually filed for chapter 11. The Noteholder Committee filed a motion to appoint a trustee because the company was still subject to adverse regulatory actions related to the board member's involvement with the business postpetition. As part of a settlement that avoided the appointment of a chapter 11 trustee, the company and the other major constituencies agreed that the board member would resign if the Noteholder Committee withdrew its trustee motion. As part of the deal, Tropicana also agreed that the Noteholder Committee's fees incurred in prosecuting the motion would be allowed as an administrative expense on the basis that its actions provided a "substantial contribution" to the bankruptcy estate.

SUBSTANTIAL CONTRIBUTION STANDARD

Like many terms in the Bankruptcy Code, "substantial contribution" is not defined nor does it provide criteria to be used. Nevertheless, courts have developed a narrow standard for the approval of administrative expense claims based on a creditor's "substantial contribution." Factors courts consider when determining whether a creditor's actions provided a substantial contribution include (i) whether the actions were solely for the benefit of the creditor itself or all parties in interest, (ii) whether the creditor would have performed the actions for its own interest without an expectation of reimbursement from the estate, (iii) whether the creditor's actions conferred a tangible, demonstrable benefit to the estate, and not one that is incidental to the creditor's action, (iv) weighing the benefits against the cost, and (v) whether the creditor's actions were duplicative of actions taken by other parties in interest.

THE COMMITTEE'S SELF-INTEREST PRECLUDED REIMBURSEMENT

In *Tropicana*, the motives of the Noteholder Committee were poorly documented in the fee request presented to the bankruptcy court. This prevented the bankruptcy court and the Third Circuit from finding that its actions were not wholly self-interested. Because there is a presumption that creditors act only in their self-interest, the Noteholder Committee was required to rebut the presumption with evidence showing that its actions "transcended self-protection." Here, the courts found that the Noteholder Committee would have prosecuted the trustee motion even if its fees would not have been reimbursed. This, the Third Circuit reasoned, showed that its actions were driven by self-interest. The *Tropicana* decision was not published in the Federal Reporter, which means that it has no precedential effect. Still, the decision serves as a reminder of the Third Circuit's very narrow view on this topic. A debtor's willingness to pay the fees will not change the standard. The creditor's intentions must be well-documented. Further, the creditor must demonstrate that the consequences of its actions conferred a tangible, substantial, and demonstrative benefit to the estate that was intended to benefit all constituencies in the case.

Please contact John Fiero or John Lucas with any questions regarding *Tropicana*.

Los Angeles:	310.277.6910
San Francisco:	415.263.7000
New York:	212.561.7700
Delaware:	302.652.4100
Web:	www.pszjlaw.com