

# **Fiduciary Duties in Chapter 11**

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# Fiduciary Duties in Chapter 11

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## **Board of Directors is fiduciary for all stakeholders**

- Responsible for maximizing value of estate
- Must navigate potentially competing interests of:
  - △ secured creditors
  - △ unsecured creditors
  - △ equity holders
  - △ other interested parties (e.g., unions, customers, regulators)

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**Board decisions are reviewed under same standards as outside Chapter 11**

- Business judgment
- Entire fairness

**But in Chapter 11 the Board's decisions might be subject to oversight in areas in which, outside of bankruptcy, no court is involved**

- Compensation (severance and retention)
- Settlements (9019 review)
- Releases

**And the scrutiny can be far more intense and less deferential**

- Bankruptcy Court is forum for “real-time” review
- Decisions can be challenged by:
  - △ economic stakeholders (ad hoc committees)
  - △ official committees (co-fiduciaries)
  - △ government officials (United States Trustee)

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## **Potential liability for directors is usually low**

- Bankruptcy Court reviews and approves/disapproves non-ordinary course action before it is taken
- Directors usually released/exculpated in plan of reorganization for post-petition conduct

## **But directors must nevertheless be diligent in overseeing the debtor**

- Reputation
- Minimize or avoid public second-guessing of decisions
- Potential litigation if debtor collapses (Chapter 7 trustee)

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## Three areas in which fiduciary issues can arise

- Appointment of equity committee
- Restructuring Support Agreement
- Conflicts between or among subsidiary-debtors and debtor-parent

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## Appointment of equity committee

- Not warranted if Debtor is “hopelessly insolvent.”
  - △ How and when measured?
  - △ Does this mean Board no longer has fiduciary duty to shareholders?
- Board can “adequately represent” shareholders.
  - △ True in every case?
  - △ Does this put Board in conflict with creditors?

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## Restructuring Support Agreement (RSA)

- Binds creditors but not Debtor (fiduciary-out)
- Creditors often require Debtor to assume RSA
- Forces a mini-trial on plan of reorganization (Plan)
- What is the standard for scrutinizing Board decision to enter into RSA? Good faith? Business judgment? Entire fairness?

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## What if estates have claims against each other?

- Examples: tax claims; allocation of corporate overhead; intercompany loans/advances
- Who analyzes claims and determines whether to bring or settle them? Disinterested directors?
- What about Plan/strategy that affects subsidiaries differently?