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Who Knew Bankruptcy Paid So Well?

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MORE than \$263,000 for photocopies in four months. Over \$2,100 in limousine rides by one partner in one month. And \$48 just to leave a message. Explanations for these charges? Priceless.

The lawyers, accountants and restructuring experts overseeing the remains of [Lehman Brothers](#) have already racked up more than \$730 million in fees and expenses, with no end in sight. Anyone wondering why total fees doled out in the Lehman bankruptcy alone could easily touch the \$1 billion mark merely has to look at the bills buried among the blizzard of court documents filed in the case.

They're a Baedeker to the continuing bankruptcy bonanza, a world where the meter is always running — sometimes literally: in the months after Lehman's collapse in September 2008, the New York law firm [Weil, Gotshal & Manges](#) paid one car-service company alone more than \$500 a day as limo drivers cooled their heels waiting for meetings to break (and this in a city overflowing with taxis).

While most of corporate America may be just emerging from the Great Recession, bankruptcy specialists have spent the last two years enjoying an unprecedented boom. [Ten of the 20](#) largest corporate bankruptcies in recent decades have occurred over the last three years, according to [BankruptcyData.com](#), with Lehman snaring honors as the biggest corporate belly-flop in American history.

These megacases — Lehman, [General Motors](#), [Chrysler](#) and [Washington Mutual](#), to name a few — are orders of magnitude larger than most bankruptcies in the past, and their size and

complexity have created a feeding frenzy of sorts for those asked to sort them out. To date, Weil, the lead law firm representing Lehman, has billed the Lehman estate for more than \$164 million.

Analysts, lawyers and others involved in the larger bankruptcy boom say that some fees are legitimate — and that others are, at a minimum, highly questionable.

“There’s clearly pressure on people to create more revenue,” says Robert White, a former bankruptcy partner at O’Melveny & Myers who retired in 2006 after practicing for 35 years. At one deposition he attended last year, each law firm sent two or three lawyers when one would have sufficed. “They were just sitting there on their BlackBerrys and talking to other people,” he said.

With first- and second-year associates charging more than \$500 an hour in some of these bankruptcy cases, according to court records, that can amount to some pretty expensive downtime. At several firms, including Weil and [Milbank, Tweed, Hadley & McCloy](#), partners now charge \$1,000 an hour or more for their bankruptcy services.

But billable hours explain only part of the run-up in costs. In the seven months after the bankruptcy filing of G.M., which taxpayer dollars helped keep afloat, various law firms and other advisers received nearly \$90 million. Lawyers from Weil, which has accounted for nearly \$16 million of fees in that case, put in for \$364.14 in dry cleaning as well as more than a week at the Sherry-Netherland hotel in Manhattan last summer, where one lawyer’s room cost \$685 a night.

In court documents, the firm responded that it could be tough to find hotel rooms in New York City for \$400 or less and that dry-cleaning or laundry bills were appropriate for out-of-town lawyers required to stay in New York for 9 or 10 days.

THINK the lawyers are expensive? Meet the consultants. [Alvarez & Marsal](#), a turnaround firm that is essentially running what remains of Lehman, has billed more than \$262.1 million.

No charges have been too big, or too small. The [Huron Consulting Group](#), a management consultancy involved in Lehman, charged \$2.54 for “gum in airport.” In the G.M. case, [Brownfield Partners](#) has billed \$230,209.55, including an \$18 fitness-club charge at a hotel.

A Brownfield partner said an employee didn’t realize that there was a separate charge to use the fitness club and didn’t notice it on the hotel bill. The firm agreed to remove the charge

after the examiner brought it to the firm's attention.

Analysts say that nickel-and-diming might be worth a laugh or two — if some of the larger fees weren't snowballing so quickly as well. They say these bounteous fees reduce the money left for creditors in the bankruptcy cases. In the Lehman case, some unsecured creditors, including bondholders, banks and vendors, are likely to get just 14.7 cents on the dollar for their claims, according to Lehman's proposed reorganization plan. Nor will they get their money quickly — some experts say they believe that the Lehman case could drag on for three to five more years.

Lawyers and restructuring pros who are picking up the pieces of companies swamped by the bankruptcy wave say that their fees are well deserved and that their services help make the bankruptcy process more efficient. And they say the pay is more than made up for by a tidier resolution of a financial debacle — or, as in G.M.'s case, the revivification of a wounded company.

“The legal skill we used to sell Lehman's North American capital markets business to [Barclays](#) saved 10,000 jobs and preserved the business itself, capturing value that otherwise would have been lost,” said Harvey Miller, 77, a Weil partner who is considered the dean of the bankruptcy bar.

Many people in the industry agree that Lehman, in particular, is a huge case that tests even the most experienced lawyers. “Lehman is a sufficiently complicated company that it would be safe to assume that if it weren't for equally sophisticated professionals running the Chapter 11 case, that the creditors would essentially receive nothing,” says Stephen J. Lubben, a professor at the [Seton Hall University](#) School of Law. “In those situations, it makes sense for sophisticated professionals to handle the case.”

Others, however, have a distinctly different perception about the fees that advisers are harvesting in bankruptcies.

“It violates any sense of proportion,” says [Kenneth Feinberg](#), the Washington lawyer who serves as the “pay czar” for banks bailed out by the government and whom the court appointed last June to monitor fees associated with the Lehman bankruptcy. The court asked him to participate after concerns were raised in the news media about the soaring fees in the Lehman case.

“Unemployment is over 9 percent, and to be paying first-year associates \$500 an hour

angers the public," he observes. "People read about all of this and say that lawyers and the legal system are one more example of Wall Street out of control."

Despite the rise in bankruptcy fees over the years, there was little or no public criticism or pushback until recently. Lawyers were reluctant to challenge their peers, fearing retaliation. Analysts say watchdogs from the [United States Trustee's office](#), a part of the Justice Department that oversees bankruptcy cases and monitors billing practices and possible conflicts, were overworked and outgunned. Even as its workload has increased, the Trustee's office has seen its staffing fall to 1,323 in 2010 from 1,468 in 2007.

Meanwhile, judges, many of whom used to work at the firms now benefiting from the bankruptcy boom, were also reluctant to challenge the status quo. All of this, analysts say, has fed a legal culture with few restraints on billing for bankruptcies.

"I don't think professionals cheat the client, but in a number of ways they can talk themselves into doing things that they wouldn't do for clients outside of bankruptcy," says Nancy B. Rapoport, a former bankruptcy lawyer at Morrison & Foerster who teaches law at the [University of Nevada](#), Las Vegas. "If you send eight people to a hearing because there is an outside chance they might have to speak at that hearing and you try that outside of bankruptcy the client will go ballistic."

Now, however, a handful of fee examiners in several high-profile bankruptcies are taking a harder line on such charges, setting the stage for a confrontation with lawyers and consultants opposed to the moves. Both Mr. Feinberg and the examiner in the G.M. case, Brady C. Williamson, for instance, have suggested reductions in hourly fees charged by some firms.

That's the kind of precedent that sets some of the bankruptcy industry leaders' teeth on edge. "Mr. Feinberg doesn't know what he's talking about," says Mr. Miller. "We don't generally give discounts. Just because bankruptcy has been the hot legal area for the last 19 months doesn't demand you cut fees."

If Mr. Feinberg and others succeed in reining in certain fees and expenses, the outcome could reverberate through the bankruptcy universe.

"This is a very important test case; it's bigger than just Lehman," observes Mr. Feinberg. "The culture of bankruptcy is unique."

So what, asks Bryan Marsal, co-founder of the restructuring firm Alvarez & Marsal. "I don't

care whether Feinberg or Moses comes into this case, you're not going to get me to apologize," he says. "If you look at this case in the context of the billions of dollars that has been recovered and the billions of dollars in claims that have been managed, just because the case was big doesn't mean it was operated inefficiently."

ON the evening of Sunday, Sept. 14, 2008, Mr. Marsal was sitting in his study in Westchester County, N.Y., when the phone rang.

Calling was Mark Shapiro, who ran Lehman's restructuring practice. He told him that Lehman's lawyers were preparing a bankruptcy filing and that the board wanted Mr. Marsal's firm to oversee the bankruptcy and eventual liquidation after Barclays and others bought pieces of the firm.

Since receiving that call, Mr. Marsal's firm has been billing \$13 million to \$18 million a month in fees and expenses for its work on Lehman, a 160-year-old name on Wall Street.

Mr. Marsal says the firm will most likely bill at \$13 million a month through October, just after the second anniversary of Lehman's collapse. After that, rates will begin to decrease, although Alvarez & Marsal will also earn an incentive fee at the end of the case, which could total more than \$50 million.

A jovial, self-deprecating man who points out a coffee stain on his shirt and, later, jokes that he wants to put on a blazer to hide a rotund midsection, Mr. Marsal is unapologetic about the fees that he and his staff are earning. Those fees pay for the salaries of the 150 people from Alvarez & Marsal now working inside Lehman (down from a peak of 185), including Mr. Marsal himself. He serves as Lehman's C.E.O., while John Suckow, an Alvarez & Marsal managing director, is Lehman's president and chief operating officer.

"The size of this case justifies the size of the fees," says Mr. Marsal, shrugging as he sits in a conference room at Lehman's headquarters in Midtown Manhattan. Mr. Marsal and Mr. Suckow estimate that they have increased the potential recovery value for Lehman creditors by \$4 billion to \$5 billion in the last year.

Indeed, deciding whether these firms and their sky-high fees are justified is difficult because the bankruptcy trade is in uncharted territory. Several of the companies that went bankrupt in the last two years were significantly bigger than [Enron](#), in terms of assets, when it collapsed in late 2001.

As if the magnitude of the bankruptcies weren't enough, there's also the matter of the

complex financial instruments that some of the companies held.

“There was commercial real estate, bank loans — all of that stuff is pretty well known to our team, but derivatives? We hadn’t had much experience in derivatives,” acknowledges Mr. Marsal, who added that his firm hired two subcontractors to work through Lehman’s derivatives book.

Mr. Miller adds that those derivatives, even today, are taking up a lot of time and energy. “We’re still in the process of unwinding them,” he says, “which raises all sorts of difficult and novel legal issues.”

In April, Lehman filed a plan with the court that would create an asset-management business, called Lamco, that would manage Lehman’s real estate and private-equity assets for five years.

By not selling some assets at fire-sale prices, the estate will be able to recoup much more money for creditors, notes Mr. Marsal.

“The money that’s going to the creditors is my money,” he says, pointing out that he’s aligned with the creditors’ goals. That’s because, at the end of the case, Mr. Marsal’s firm will receive an incentive fee that is based on a percentage of the money returned to creditors.

Mr. Marsal says critics should be careful about identifying where problems lurk in bankruptcy fees. He says the savings that result from making sure that no one is flying first class to Europe are “peanuts.”

“You should be much more worried about the two or three lawyers who are overbilling and whether they should even be in attendance at a meeting,” he says. “I think the fee committee and the fee examiner is a lot of hooey.”

IF anyone is a master of getting to yes, it’s Kenneth Feinberg. As a mediator, he brokered settlements in long-running product liability suits brought by those who said they were victimized by Agent Orange, asbestos and the Dalkon Shield. More recently, he managed to win praise on delicate assignments like determining how much the Sept. 11 Victim Compensation Fund should pay out — or what is an appropriate salary for an executive at a financial institution that the government propped up with taxpayer funds.

But he says that challenging bankruptcy lawyers is tougher in some ways. “In the 9/11 case, the country was behind me; as pay czar, there was a lot of support for what I was doing,” he

says. "This is more problematic."

In particular, Mr. Feinberg is perplexed by why fees keep rising in the Lehman case, even though it's no longer the chaotic affair it was in the weeks and months after the bankruptcy filing. "Now the emergency is over; it is more like a traditional bankruptcy," he says. "Yet the fees are higher than ever."

Mr. Feinberg has managed to get under the skin of the lawyers in the case. And he is equally frustrated. His voice rising and Boston accent thickening (think "debt-ah" and "credit-ah"), he says that bankruptcy professionals "still haven't gotten the message."

The four-member Lehman fee committee, of which Mr. Feinberg is chairman, has disagreed about how to rein in fees, he says. But he declines to elaborate. Mr. Miller says it's because creditors and debtors are willing to pay well so they can get "the best representation possible."

On a rainy summer day last year, Mr. Feinberg journeyed to the plush offices of Mr. Miller in the General Motors building in Manhattan. His pitch was simple: Cut 10 percent to 15 percent right off the top of the fees being billed.

Mr. Miller and Dennis Dunne, a partner at Milbank who represents creditors, told him, "You don't know how complicated this is; you don't know how difficult it is," Mr. Feinberg recalls.

Mr. Miller doesn't dispute Mr. Feinberg's account, and Mr. Dunne declined to comment for this article.

Despite these frictions, a deal was eventually struck.

Among the new fee rules being enforced are these: Air travel must be in coach class only. Ground transportation is limited to \$100 a day, and only after 8 p.m. Hotel rooms are capped at \$500 a night. Photocopy charges are limited to 10 cents a page. Late meals can't be more than \$20 each.

"If you continue to violate the very guidelines that are in place, 50 percent of the disputed amounts will be deducted," says Mr. Feinberg. After that, the full amount will automatically be deducted, he added.

The lawyers reserve the right to challenge the fee committee's decisions at the end of the case, but the ultimate call will be up to the bankruptcy judge, James Peck. He declined to

comment.

Mr. Feinberg has so far challenged a very small percentage of the fees and expenses in the case. But he is intensifying his efforts. In March, the court increased his monthly budget to \$250,000 from \$75,000, giving Mr. Feinberg more accountants, examiners and others to pore over records and to zap overcharges. His firm and the fee committee have billed the Lehman estate \$645,000 in fees for services through March.

Already, he's called out Jones, Day, saying it charged \$70,800 extra for photocopying and spent \$2,856 too much on taxi rides last summer. According to court filings, a Jones, Day partner, William Hine, claimed more than \$2,100 for late-night rides home in one month. Milbank, according to court filings, charged \$148,426 just to compile its bills and time records — a move akin to a doctor charging a patient to prepare a bill after expensive, complex surgery.

"Lawyers don't charge for invoice preparation except in bankruptcy," Mr. Feinberg says. "I've prepared bills my entire professional life. You don't charge a fee. Most people would argue that charging anything is inappropriate."

Jones, Day and Milbank both declined to comment.

Like the restructuring executives, bankruptcy lawyers seem defiant and want to make sure precedents aren't set that would make it easier to curb fees in the future.

"When people work late and they want to go home, we don't like to send people in the subway at midnight or thereafter," Mr. Miller says. "I don't believe it's appropriate to require people to fly coach for 15 hours and then go to a meeting."

Nevertheless, Mr. Miller is going along with Mr. Feinberg's guidelines.

"Those are the rules; we're going to abide by the rules and pick up the difference," Mr. Miller says.

FOR all his annoyance at Mr. Feinberg's role in the Lehman case, Mr. Miller saves his real vitriol for Mr. Williamson, the fee examiner in the G.M. bankruptcy, which Weil also worked on. In the case's first seven months, Weil accounted for \$16.5 million of the \$90 million in fees paid. Mr. Williamson objected to a small portion of the expenses. Weil, according to court documents, agreed to deduct \$500 in expenses relating to the cancellation of a vacation, and said that any first-class travel charges were included "inadvertently" and

reduced. It also agreed to pay for any meals in excess of \$20.

Mr. Williamson also recommended that a 5 percent cut in Weil's overall rates would be "appropriate," especially given that several other large firms in the case already provided discounts.

"Williamson is way off base," says Mr. Miller. "He perceives himself to be a sage, giving advice to the world, and that is not his role."

Mr. Williamson wrote in an e-mail message: "Courts appoint independent examiners to help ensure transparency and accountability, most recently where tax dollars and significant economic issues are at stake. Not everyone, unfortunately, always appreciates either the role or the rules the examiner is bound to apply."

Mr. Miller sees his own work as a battle between corporate life and death, with the money spent on photocopies and dry cleaning an insignificant detail.

"If you had cancer and you were going into an operation, while you were lying on the table, would you look at the surgeon and say, 'I'd like a 10 percent discount,' " he explains. "This is not a public, charitable event."