UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re: KIDDE-FENWAL, Inc., Debtor.	Chapter 11 Case No. 23-10638 (LSS) Re: Doc. No. 483

BENCH RULING[1]

This is my decision on Kidde-Fenwal's motion to enter into and perform a reimbursement agreement with the professionals retained by the Ad Hoc Committee of Governmental Claimants.[2] The motion is supported by the Official Committee of Unsecured Creditors and the Ad Hoc Committee. It is opposed by the Office of the United States Trustee. I took evidence and heard argument on October 26 and took the matter under advisement.

The evidence is undisputed and is in the form of the Declaration of James Mesterharm, Debtor's chief transformation officer. Mr. Mesterharm was present in the courtroom and no one chose to cross-examine him.

Mr. Mesterharm testified that the Ad Hoc Committee of Creditors was formed shortly after Kidde-Fenwal filed bankruptcy. It consisted of 20 governmental entities, which counsel represents has now increased to 23 and may grow further. Debtor considers the Ad Hoc Committee to be a key participant in its restructuring process and plan negotiations and

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[1] This Bench Ruling was read in court on November 7, 2023. Minimal, minor, non-substantive corrections were made and citations were added.

[2] Motion of Debtor to Enter Into, and Perform its Obligations Under, the Reimbursement Agreement with the Professional Retained by the Ad Hoc Committee of Governmental Claimants, *Nunc Pro Tunc* to May 14, 2023, Dkt No. 483.

believes its involvement in the case to be both important and necessary. Debtor believes without the Ad Hoc Committee providing a single point for negotiation of the distinct issues facing governmental entities, Debtor will wind up in seriatim negotiations with each governmental unit, resulting in unduly burdensome, protracted and costly proceedings. Debtor believes that an ad hoc committee structure is the most efficient path forward in the case, which has already resulted in streamlining a negotiated, voluntary extension of the automatic stay to governmental entities. A streamlined, consensus-building process with the ad hoc committee is integral to Debtor's path in confirming a plan and, Debtor believes, is in the best interest of the estate and will benefit the estates as a whole.

The negotiated fee arrangement with the Ad Hoc Committee's professionals is documented in a letter agreement filed with the motion. The letter agreement provides for the payment of the Committee's attorneys, Kelley Drye & Warren and A.M. Saccullo Legal, as well as its financial advisor, Berkeley Research Group. Debtor agrees to pay these professionals "reasonable and documented" fees and out-of-pocket expenses for services rendered to the Ad Hoc Committee at their normal hourly rates up to a cap of $600,000 per month beginning May 14, 2023. The monthly cap can be rolled forward or backwards to cover fees and expenses exceeding $600,000 in a given month. Debtor may terminate the agreement at any time and for any reason effective 30 days after notice.

After this arrangement was reached, the Official Committee of Creditors negotiated additional conditions on payment. The Ad Hoc Committee's professionals now must comply with the Interim Compensation Procedures Order that applies to estate professionals, including the review process, a 20% hold back and review by the fee examiner appointed in this case. Further, the fees and expenses incurred in connection with or

relating to the allocation by and among creditor constituencies, the estate, or any proposed settlement inuring to the benefit of Debtor's creditors shall be segregated and recorded in separate matters. These fees related to allocation of value are payable only upon the earlier of (i) Debtor's and the Official Committee's consent to the payment, (ii) a Court Order (presumably upon application by the Ad Hoc Committee's professionals), (iii) the approval by the Court of a restructuring support agreement that includes support from the Ad Hoc Committee , (iv) confirmation of a chapter 11 plan or (v) the approval of a sale of substantially all of Debtor's assets and a motion that otherwise effectuates Debtor's exit from the case, such as conversion or dismissal.

This further negotiated arrangement is encapsulated in a revised form of order that was filed in advance of the hearing. The revised form of order also provides that entry of an Order approving this arrangement is without prejudice to fees incurred, but not authorized to be paid under the arrangement, which presumably means that the Ad Hoc Committee could seek to have those fees paid as conferring a substantial contribution.

The sole objection was brought by the Office of the United States Trustee ("UST"). The UST's primary argument is that a request to pay a non-estate professional's fees may only be brought by way of a substantial contribution motion pursuant to sections 503(b)(3)(D) and (b)(4). The UST argues that section 363 may not be used to circumvent the plain language of section 503, which specifically addresses payment of fees and expenses incurred by ad hoc committees in a bankruptcy case. The UST further invokes the "specific governs the general" canon of statutory construction, with section 503 being the specific and section 363 being the general. Secondarily, the UST argues that the motion fails even if analyzed under section 363 for a lack of evidence that the governmental entities would

abandon negotiations or otherwise not participate in the case in the absence of the requested payment of fees. The UST also points out that unlike in some of the few other cases in which relief has been granted under section 363, the ad hoc committee has not signed a restructuring support agreement and a portion of the relief is backwards looking. Further, the UST points out that the ad hoc committee cannot bind any governmental entities beyond its direct members and over 30 States or Commonwealths are not members of the committee.

Having reviewed the case law and considered the evidence and arguments of counsel, I will, in the unique facts and circumstances of this case, approve the motion as I am about to discuss.

The statutory issue presented is at once both simple and complex. The Code permits a debtor to bring a motion for permission to use property of the estate, including cash, outside of the ordinary course of business. This is embodied in section 363 and a debtor, therefore, brings a request under section 363 to seek permission from the court of any action it seeks to take that is outside of the ordinary course. The instant request falls into this category.

Section 503, entitled Allowance of Administrative Expenses, provides, in the first instance, that an "entity" may make a request for payment of an administrative expense. Section 503 then provides a non-exclusive list of expenses that may be allowed administrative priority, meaning the expense is paid ahead of general unsecured claims. The subsections at issue here—(b)(3)(D) and (b)(4)—allow as administrative expenses the actual and necessary expenses of an ad hoc committee that makes a "substantial

contribution" in a chapter 11 case as well as reasonable compensation for the services of the ad hoc committee's attorneys or accountants.

I agree with the cases that have concluded that section 363 and section 503 are not mutually exclusive when it comes to seeking payment of an ad hoc committee's expenses and professional fees. I am persuaded by the analysis in both *Bethlehem Steel*, 2003 WL 21738964 out of the District Court for the SDNY (Judge Mukasey)[3] and *Mallinckrodt*, 2022 WL 906458 from Judge Stark out of our District[4] that a request under section 363 is not prohibited because the Code permits creditors to seek the same type of payment under section 503. As those courts recognize, in most circumstances, debtors do not seek to pay these fees, or oppose payment. I am also persuaded by Judge Stark's analysis that sections 363 and 503 are not contradictory such that there is no need to apply the general/specific canon and, similarly, that there is no superfluity issue. As Judge Stark points out, section 363 and section 503 are "directed at different parties, operate at different times, and serve different purposes."[5]

In my view, the more difficult question is whether to approve the request under section 363. The court may approve a request under section 363 if it is a proper exercise of the debtor's business judgment. As I stated during argument, given that section 363 requires notice and a hearing as well as court approval, I agree with those judges who carefully weigh all supporting and opposing views and determine in the court's judgment, whether

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[3] *In re Bethlehem Steel Corp.*, No. 02-2854, 2003 WL 21738964 (S.D.N.Y. July 28, 2003).

[4] *In re Mallinckrodt PLC*, No. 21-167, 2022 WL 906458 (D. Del. Mar. 28, 2022).

[5] *Mallinckrodt*, at * 9.

the debtor's decision makes good business sense. Here, as the UST points out, Debtor's decision is not an operational one to which greater deference may be owed. Rather, as Mr. Mesterharm articulates it—the decision is a strategic one about what Debtor believes may pave a more efficient path to an exit.

In considering Debtor's decision, then, I have to evaluate Debtor's judgment in this case. In doing so, it is appropriate to consider the existence of section 503 as an alternative for a creditor to pursue. That this consideration is appropriate is evident from the decisions made in other cases, including the bankruptcy courts' respective decisions in *Purdue* and in *Mallinckrodt* (at least as I glean from a reading of the transcripts[6]). In each of those cases, the court did not accept the fee payment arrangement as originally proposed by the debtor. Rather, the courts recognized the challenging situation of determining, in the circumstances of the case before them, whether the expenditure of a debtor's funds to pay these expenses, which diminishes—or could diminish—funds available to pay creditors, is a best use. Therefore, in both *Purdue* and *Mallinckrodt*, which are most analogous, after hearing concerns raised by objectors, the court added additional conditions on payment. Those additional conditions permitted a backwards looking view at the time of payment to see if the ad hoc committee's actions, as anticipated when the section 363 motion was approved, benefited all of the parties in the case and/or whether the ad hoc committee was constructive, generally. For example, in *Mallinckrodt*, Judge Dorsey imposed two additional requirements. One: if mediation fails and there are no further prospects for a mediated resolution, all reimbursement of fees and costs would cease. Two: if the mediator advised

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[6] *See In the Matter of Purdue Pharma L.P.*, Case No. 12-23649 (Drain, J.), 11/19/2019 Transcript of Oral Argument, Dkt. No. 550; *see also In re Mallinckrodt PLC*, Case No. 20-50850 (Dorsey, J.), 1/19/2021 Transcript of Court Decision, Dkt. No. 1189.

the court that an ad hoc group was not participating in the mediation in good faith, all reimbursements would cease and any fees and expenses previously paid would be subject to disgorgement following notice and an opportunity for a hearing.[7] Those conditions bring the standard of review on fees requested by ad hoc committee professionals closer to a general administrative claim or substantial contribution standard then to a review of professional fees under section 330. As noted in *Perdue,* additional safeguards put the ad hoc committee at some risk.[8]

As applied here: the conditions that Debtor originally put in place together with the additional restrictions placed on payment agreed to with the Official Committee also reflect a heightened standard and a backwards looking view on fees. In fact, the payment of fees related to the allocation issue (as it is called) are conditioned on the approval of an RSA, confirmation or other exit strategy supported by the ad hoc committee. To the extent it is not clear, I will impose the additional condition that all fees and expenses ultimately be subject to notice and a hearing and review by the court even if one of the events for payment occurs. Further, in my determination of what is an appropriate/reasonable level of fees, I will take into consideration the ad hoc committee's positive contribution to the case and its good faith participation to a resolution. While that, admittedly, injects some risk into the ultimate receipt of payment, this is an appropriate level of risk for a motion brought under section 363.

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[7] *Mallinkrodt*, Transcript of Court Decision at 11:21-12:9.

[8] *Purdue Pharma*, Transcript of Oral Argument at 167:7-19.

Here, I do place some significance in approving the arrangement that the governmental entities cannot sit on the Official Committee. I also credit the agreed-to restrictions and the ability to review the fees to determine appropriateness at the time of payment. I also place some significance on the fact that the ad hoc committee has twice agreed to a voluntary stay of AFFF-related claims against non-debtor parties to provide an opportunity to bring consensus to the case. I expect continued similar positive actions in the case. And, if, for whatever reason, Debtor feels the arrangement is no longer beneficial, Debtor may terminate the agreement. While I am not sure why there is a notice period, I will accept this negotiated term in light of the other conditions and can address any fees sought in that 30-day period at the time they are requested.

So – I will approve Debtor's motion as the relief has been modified. Based on the unopposed evidence and the conditions to payment, I conclude, for purposes of this motion, that Debtor has properly exercised its business judgment in determining that it will be beneficial to the estate to have the Ad Hoc Committee participate in these cases as a committee and to serve as a focal point for negotiations with governmental entities.

In doing so, however, let me make clear that I consider the granting of such relief to be a rare occurrence. While, as evidenced by the *Bethlehem Steel* decision, the use of section 363 in this fashion is not new, but it does seem to be picking up steam. Each case will have to be evaluated on its own terms and I do not expect to be regularly approving the payment of fees for a prepetition creditor or group of creditors on a section 363 motion. I can envisage that to the extent such a request becomes commonplace, I would become more hesitant, not less hesitant, to grant the request.