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10 UNITED STATES BANKRUPTCY COURT
11 NORTHERN DISTRICT OF CALIFORNIA
12 OAKLAND DIVISION

13 In re
14 FOX ORTEGA ENTERPRISES, INC., dba
PREMIER CRU
15 Debtor.

Case No. 16-40050-WJL

Chapter 7

**APPLICATION FOR ORDER
AUTHORIZING EMPLOYMENT OF
DIAMOND McCARTHY LLP AS
SPECIAL LITIGATION COUNSEL FOR
CHAPTER 7 TRUSTEE**

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21 **TO THE HONORABLE WILLIAM J. LAFFERTY, III, UNITED STATES**
22 **BANKRUPTCY JUDGE, AND THE OFFICE OF THE UNITED STATES TRUSTEE:**

23 Michael G. Kasolas, the Chapter 7 Trustee herein (the "Trustee") in the above-captioned
24 chapter 7 case of Fox Ortega Enterprises, Inc. dba Premier Cru (the "Debtor"), hereby applies to
25 this Court for entry of an order authorizing the employment of Diamond McCarthy LLP
26 ("Diamond McCarthy") as Special Litigation Counsel to the Trustee effective as of September 1,
27 2017, on a contingent fee basis pursuant to 11 U.S.C. §328(a).
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1 This application (the "Application") is made pursuant to Bankruptcy Code section 328, and
2 Federal Rule of Bankruptcy Procedure 2014. This Application is based on the Declaration of
3 Kathy Bazoian Phelps (the "Phelps Declaration") filed concurrently herewith, other papers of
4 record, and upon such further pleadings and evidence as may be filed in connection herewith.

5 In connection with this Application, the Trustee respectfully represents as follows:

6 I. BACKGROUND

7 1. The Debtor, a wine merchant, filed its voluntary petition under chapter 7 on
8 January 8, 2016. The Trustee is the duly appointed trustee in the case.

9 2. On August 11, 2016, John Fox, the Debtor's former chief executive officer,
10 executed a Plea Agreement filed in the criminal matter of United States of America v. John Fox,
11 then pending in the United States District Court for the Northern District of California, Case No.
12 CR 16-281 JD, in which he admitted to his running the Debtor as a fraudulent scheme wherein he
13 would cause the Debtor to accept payments on orders for the purchase of "pre-arrival" wine that
14 were never fulfilled and would use funds received from current sales to cover on certain prior sales
15 in order to keep the fraudulent enterprise operating.

16 3. The Trustee wishes to employ special litigation counsel to investigate potential
17 Ponzi scheme "net winner" claims; advise it regarding the results of its investigation; agree to
18 consider prosecuting potential claims on behalf of the Estate if counsel concludes there are viable
19 claims that can be brought and are economically viable for the firm; and to advise the Trustee with
20 respect to the various legal considerations and decisions that will arise in connection with the
21 investigation and prosecution of such claims. Diamond McCarthy has already expended time in
22 reviewing this matter, the Debtors' background as reflected in the Court's docket; reviewing
23 available material; and investigating the claims in connection with a possible engagement.

24 II. RELIEF REQUESTED

25 4. As permitted by Bankruptcy Code section 328 and Federal Rule of Bankruptcy
26 Procedure 2014(a), the Trustee wishes to employ Diamond McCarthy as his special litigation
27 counsel to conduct further investigation into the claims described above, as well as any related
28 claims, and to potentially prosecute such claims on behalf of the Estate on a contingent fee basis as

1 described further below and in such amounts as this Court may allow in accordance with 11
2 U.S.C. §328(a).

3 **III. QUALIFICATIONS AND SCOPE OF PROPOSED EMPLOYMENT**

4 5. Diamond McCarthy possesses the requisite resources and is highly qualified to
5 serve as the special litigation counsel in investigating potential litigation claims and prosecuting
6 litigation claims.

7 6. Diamond McCarthy's professionals specialize in representing fiduciaries, including
8 receivers and bankruptcy trustees, in large and complex bankruptcy and litigation cases around the
9 country. Diamond McCarthy served as lead trial counsel for various parties having significant
10 roles in the Enron/LJM2, Parmalat, Livent, Bayou Funds, Dreier, LLP, USA Commercial
11 Mortgage, Diversified Lending Group, Inc., Equipment Acquisition Resources, Inc., Bank United,
12 and the Syntax-Brilliant cases, among many others, involving complex fraud, Ponzi schemes,
13 accounting, legal and other malpractice and bankruptcy related claims for which Diamond
14 McCarthy recovered millions and millions of dollars for its clients.

15 7. It is anticipated that Kathy Bazoian Phelps, a partner of Diamond McCarthy, will
16 serve as lead counsel in this matter. Ms. Phelps has more than 25 years of experience as a lawyer
17 in bankruptcy law, fiduciary representation and fraud litigation, as well as serving as a fiduciary
18 herself. Kathy's practice includes representing trustees and receivers, serving as a Chapter 11
19 trustee, representation of litigants and parties in interest in bankruptcy and receivership cases and
20 other insolvency proceedings. She is particularly knowledgeable about the administration of Ponzi
21 scheme cases and has extensive litigation experience in a claims arising in these types of cases,
22 including fraudulent transfer litigation. Ms. Phelps has lectured widely and written on bankruptcy
23 and receivership matters, with a focus on Ponzi schemes. She is the co-author of *The Ponzi Book:*
24 *A Legal Resource for Unraveling Ponzi Schemes.*

25 8. Diamond McCarthy is well-qualified and uniquely able to serve as special litigation
26 counsel in the Contingency Litigation. Diamond McCarthy's extensive litigation background with
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1 the specific types of claims likely to be at issue in this case will be invaluable in assessing the
2 options for maximizing the return to creditors in this case.

3
4 9. The duties to be performed by Diamond McCarthy in this matter include:

- 5 a. Investigation of the Estate's potential litigation claims against transferees of
6 net winner fraudulent transfer claims;
7 b. Negotiating a resolution of, or filing and prosecuting net winner potential
8 claims ("Contingent Litigation Claims"), if any such claims are filed;
9 c. Making court appearances on behalf of the Trustee if required or warranted
10 as part of its special litigation counsel role; and

11 **IV. COMPENSATION**

12 10. Subject to this Court's approval, Diamond McCarthy will be employed on a
13 contingency basis under 11 U.S.C. §328(a), subject to the terms and conditions specified below
14 and approval by the Court.

15 11. Except for the potential reimbursement of out of pocket expenses as described
16 below, Diamond McCarthy will be compensated for its services only when the Trustee obtains a
17 Recovery,¹ either through settlement, judgment, reduction or elimination of claims against the
18 Estate, or otherwise.

19 12. The Contingency Fee shall be paid as follows:
20

21 ¹ "Recoveries" or "Recovery," means any and all monetary payments or other valuable property
22 received by the Estate arising, pertaining to or resulting from the pursuit of the Contingency
23 Litigation Claims. For the purposes of calculating the appropriate contingency fee, a Recovery is
24 "received" when the Estate takes possession or control of any Recovery. Recoveries, or Recovery
25 shall include the value received by the Estate from the disallowance of any claims resulting from
26 resolution of Contingency Litigation Claims. For the purposes of determining the value received
27 by the Estate from the disallowance of any claims resulting from resolution of Contingency
28 Litigation Claims, the value shall be equal to the percentage of the pro rata distribution to
unsecured creditors by the Estate applied to the amount of the disallowed claim at the time of any
interim and/or final distributions to unsecured creditors, and the Firm shall be paid that amount of
the Firm's contingency fee due to the disallowance of any claims at the time of any interim and/or
final distribution to unsecured creditors.

- 1 a. In the event the Trustee receives a Recovery pursuant to a settlement,
2 judgment or otherwise at any time before Commencement of Trial,²
3 Diamond McCarthy shall be entitled to (1) forty percent (40%) of all Gross
4 Recoveries of the amounts received by the Trustee until a total of \$1.5
5 million is received; (2) thirty-three and one-third percent (33⅓) of all Gross
6 Recoveries received after the first \$1.5 million are received until Gross
7 Recoveries in the amount of \$3 million (\$3,000,000) are received; and (3)
8 twenty-five percent (25%) of all Gross Recoveries of amounts received that
9 total more than \$3 million.
- 10 b. After the Commencement of Trial, Diamond McCarthy shall be entitled to a
11 contingency fee in the amount of (1) forty percent (40%) of all Gross
12 Recoveries of the amounts received by the Receiver or Receivership until a
13 total of \$3 million (\$3,000,000.00) is received and (2) thirty-three and one-
14 third percent (33⅓ %) of all Gross Recoveries received after the first \$3
15 million are received.
- 16 c. The Trustee will pay from the Estate all necessary out of pocket expenses
17 incurred in connection with the Contingency Fee Claims and Contingency
18 Litigation, which expenses can be paid on an interim basis by the Trustee so
19 long as there are sufficient funds available in the Estate, but with such
20 expenses ultimately subject to Bankruptcy Court approval and allowance or
21 disallowance pursuant to 11 U.S.C. §§ 330(a)(1)(B) and 331, the local rules
22 for the Bankruptcy Court and United States Trustee Guidelines. Diamond
23 McCarthy will maintain records of the costs and expenses incurred in
24 connection with its legal services and shall comply with the United States
25 Bankruptcy Court for the Northern District of California Guidelines for
26 Compensation of Reimbursement of Professional and Trustees. The Firm
27 will request the Trustee's approval prior to incurring any individual expense
28 greater than \$5,000 (including pre-suit expenses and post-suit expenses for,
inter alia, expert witnesses, jury consultants, demonstrative evidence
consultants, photocopying, scanning, digitizing and document
imaging/coding, postage, facsimiles, long-distance telephone calls, travel,
delivery, computerized research, deposition and court reporting transcript
and other fees, videography fees and costs) (the "Expenses") with the
understanding that all Expenses ultimately must be approved by the
Bankruptcy Court on an interim or final basis..

13. Diamond McCarthy is not obligated to file or prosecute any Contingent Litigation
Claim unless in its discretion it concludes that any such Contingent Litigation Claim is factually

² "Commencement of Trial" shall mean the first scheduled day of any bench trial, jury trial or arbitration set by the court or arbitrator(s) in any lawsuit, legal action, contested proceeding or arbitration filed by the Firm on the Trustee's or Estate's behalf, even if that first scheduled trial or arbitration date is continued or rescheduled to a later date.

1 and legally supportable and is economically viable for the firm to pursue. Diamond McCarthy has
2 the option to seek Court approval to terminate this agreement if the firm in good faith concludes
3 that there are no viable claims for the Trustee to pursue on behalf of the Estate.

4 14. The contingency fee terms outlined above are the result of arm's length
5 negotiations between the Trustee and Diamond McCarthy. The provisions reducing Diamond
6 McCarthy's contingency fee percentage for pre-trial settlements and recoveries are all designed to
7 provide the highest recovery possible to the Estate and its creditors and ensure the contingency fee
8 paid is commensurate with the risk and costs borne by Diamond McCarthy and the results
9 obtained. The Trustee submits that the proposed contingency fee terms set forth above are fair,
10 reasonable and in the best interest of the Estate and its creditors.

11 15. The following schedule sets forth the current normal and customary hourly rates of
12 the Diamond McCarthy attorneys most likely to render services in this case, which rates are
13 subject to periodic increase:

14	Kathy Bazoian Phelps	Partner	\$625
15	Jon Maxwell Beatty	Partner	\$495
16	Michael Yoder	Partner	\$495
17		Associate	\$270 - \$320

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19 16. In addition to Diamond McCarthy's professional fees, its billing statements will
20 include expenses for reasonable and necessary third party and staff services employed in the
21 course of its representation of the Trustee, as well as expenses incurred with respect to long-
22 distance telephone calls, postage, messenger services, photocopying, filing fees, computerized
23 legal research, and facsimile transmission. These expenses are separately itemized on Diamond
24 McCarthy's statements at scheduled rates based on the service involved and out-of-pocket
25 disbursements incurred. Diamond McCarthy will record these expenses in a manner and at a rate
26 that is consistent with charges generally made to Diamond McCarthy's other clients. No expense
27 charges will be assessed for word processing or secretarial overtime in Diamond McCarthy's
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1 representation of the Trustee. Diamond McCarthy will seek approval for reimbursement of such
2 expenses in accordance with the contingent fee terms outlined above.

3 17. Diamond McCarthy understands and agrees that it must keep accurate records of its
4 time and the hourly legal fees incurred, but does not intend for the purposes of this contingent fee
5 agreement to keep those records in the detail required for professionals whose employment and
6 compensation is governed by 11 U.S.C. §330. Diamond McCarthy will comply with the United
7 States Bankruptcy Court for the Northern District of California Guidelines for Compensation of
8 Reimbursement of Professional and Trustees.

9 18. In conformity with Bankruptcy Code sections 330 and 331, if there are sufficient
10 fund available to the Estate, Diamond McCarthy intends to file interim applications for allowance
11 of fees and reimbursement of costs advanced as and when appropriate under the Bankruptcy
12 Rules, the Local Rules and this Court's orders.

13 19. At the conclusion of the Bankruptcy Case, Diamond McCarthy will file an
14 appropriate application seeking final allowance of all fees and costs, regardless of whether interim
15 compensation has been paid. Upon allowance of such fees and costs, the Estate will cause to be
16 paid to Diamond McCarthy the difference between the amounts allowed and any interim
17 compensation paid.

18 20. Diamond McCarthy has not shared or agreed to share any compensation related to
19 the services to be rendered as special litigation counsel for the Trustee with any other person,
20 except as among Diamond McCarthy firm members and/or employees.

21 **V. CONNECTIONS WITH THE DEBTOR AND OTHER PARTIES**

22 21. Diamond McCarthy maintains a computerized database of its client matters. In
23 connection with the proposed retention of Diamond McCarthy by the Trustee, Diamond McCarthy
24 performed an internal conflicts search to ensure that Diamond McCarthy does not have a conflict
25 of interest that would prohibit it from representing the Trustee in this matter. Specifically,
26 Diamond McCarthy has researched its client database to determine whether it had any relationship
27 with the following:

28 a. The Debtor;

- b. Parties identified by the Trustee has having received transfers from the Debtor within 7 years prior to the Petition Date;
- c. The officers, directors and interest holders of the Debtors listed on the Debtors' SOFAs.

22. As Diamond McCarthy becomes aware of new parties-in-interest being involved in the Bankruptcy Case, Diamond McCarthy will file supplemental declarations as needed to update the disclosures made herein.

23. To the best of Diamond McCarthy's knowledge, information and belief, and other than as set forth in the Phelps Declaration and below, Diamond McCarthy has no interest materially adverse to (a) the Debtor's estate, (b) the target defendants, or (c) of any class of the Debtor's creditors, either by reason of any direct or indirect relationship to, or connection with, the Debtor or for any other reason. Pursuant to Bankruptcy Rule 2014(a), the Phelps Declaration sets forth Diamond McCarthy's known connections, if any, with the Debtor, the Debtor's creditors, and other known parties-in-interest. The Phelps Declaration also discloses the method in which Diamond McCarthy has reviewed its own records and files and has obtained information in connection with matters set forth herein. The Phelps Declaration also sets forth the manner in which Diamond McCarthy will continue to review its files in connection with this Application to make further disclosures as warranted. Diamond McCarthy believes it is a disinterested person within the meaning of Bankruptcy Code section 101(14), other than as to those matters disclosed herein or in the Phelps Declaration.

24. To the best of Diamond McCarthy's knowledge, none of the attorneys comprising or employed by Diamond McCarthy are related to any judge of the United States Bankruptcy Court for the Northern District of California, the United States Trustee or any person employed in the Office of the United States Trustee.

VI. NOTICE OF THE APPLICATION

25. Notice of this Application has been given to the interested parties by serving this Application and the Phelps Declaration on (i) the Office of the U.S. Trustee; (ii) the Debtor, and the Debtor's counsel, and (iii) parties who have filed with the Court a request for special notice.

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VII. DISCUSSION

A. The Agreement Meets the Requirements of Section 328

26. Bankruptcy Code section 328 permits the employment of a professional to assist a committee “on any reasonable terms and conditions of employment, including on a retainer, on an hourly basis, on a fixed or percentage fee basis, or on a contingent fee basis.” 11 U.S.C. §328(a). Diamond McCarthy is specifically requesting that the contingency fee set forth above and in this Application be awarded under Bankruptcy Code section 328. *Circle K Corp. v. Houlihan, Lokey Howard & Zuken, Inc. (In re Circle K Corp.)*, 279 F.3d 669, 671 (9th Cir. 2001) (holding that unless the retention application of a professional unambiguously specifies that approval is sought under Bankruptcy Code section 328, any fee award is subject to review under Bankruptcy Code section 330).

27. The Court must determine the reasonableness of the terms and conditions of the proposed employment at this time because once a bankruptcy court approves a fee agreement under section 328, “when the professional ultimately applies for payment, the court cannot alter those terms unless it finds the original terms ‘to have been improvident in light of developments not capable of being anticipated at the time of the fixing of such terms and conditions.’” *In re Reimers*, 927 F.2d 1127, 1128 (9th Cir. 1992) (quoting *In re Confections by Sandra, Inc.*, 83 B.R. 729 (B.A.P. 9th Cir. 1987)). Here, the proposed terms are reasonable for several reasons.

28. First, a contingency fee is appropriate because the likely source of potential significant recovery on general unsecured claims will be from any Contingency Litigation Claim(s). Any recovery on the Contingency Litigation Claims requires significant legal services and there is a serious risk of nonpayment for Diamond McCarthy. The ability of the Estate to pay administrative expenses may even depend, as a practical matter, upon the successful prosecution of the Contingency Litigation Claims. The Trustee projects that it could take many months and several thousand more hours of attorney services to prosecute the Contingency Litigation Claims to resolution.

29. Second, the Trustee would likely be unable to retain counsel to prosecute the Contingency Litigation Claims without the contingent fee arrangement provided in this

1 Application, or a similar or less favorable contingent fee arrangement, based upon the risk of
2 nonpayment. The Trustee does not believe it is a prudent expenditure of Estate funds to prosecute
3 any Contingency Litigation Claim(s) to resolution on an hourly basis when the contingency fee
4 arrangement can ease that burden on the Estate. The contingency fee arrangement will permit
5 prosecution of any Contingency Litigation Claim(s) and compensate Diamond McCarthy for the
6 risk of nonpayment.

7 30. Third, the particular contingency fee arrangement provides reduced compensation
8 to Diamond McCarthy if Recoveries to the Estate are recovered relatively early in the prosecution
9 of any Contingent Litigation Claim(s). Thus, the potential for a fee recovery out of proportion
10 with the risk taken is tempered. Accordingly, the contingency fee arrangement as set forth above
11 reasonably protects all interests.

12 WHEREFORE, the Trustee prays that this Court enter an order authorizing the
13 employment of Diamond McCarthy as special litigation counsel to the Trustee in the Bankruptcy
14 Case.

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16 Dated: September 13, 2017

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18
19 By /s/ Michael G. Kasolas
MICHAEL G. KASOLAS
20 Chapter 7 Trustee

21 SUBMITTED BY:

22
23 Diamond McCarthy LLP

24 By /s/ Kathy Bazoian Phelps
25 KATHY BAZOIAN PHELPS
26 Proposed Special litigation counsel for Michael G.
Kasolas, Chapter 7 Trustee