

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re : Chapter 11
FLEMING COMPANIES, INC., *et al.*, :
Debtors. : Case Number 03-10945 (MFW)
Jointly Administered

**THE ACTING UNITED STATES TRUSTEE’S REPORT ON, AND OBJECTIONS TO,
THE FIRST INTERIM FEE APPLICATIONS OF CERTAIN
DEBTOR PROFESSIONALS
(DOCKET ENTRY #s 3195, 3209, 3211, 3235, 3296, 3596)**

In support of her report on, and objections to, the first interim fee applications of certain debtor professionals, Roberta A. DeAngelis, Acting United States Trustee for Region 3 (“UST”), by and through her counsel, avers:

INTRODUCTION

1. This Court has jurisdiction to hear and determine these objections.
2. Under 28 U.S.C. § 586(a)(3)(H), the UST is charged with monitoring applications filed under section 327 of the Bankruptcy Code “and, whenever the United States trustee deems it to be appropriate, filing with the court comments with respect to the approval of such applications.” 28 U.S.C. § 586(a)(3)(H). This duty is part of the UST’s overarching responsibility to enforce the laws as written by Congress and interpreted by the courts. *See United States Trustee v. Columbia Gas Sys., Inc. (In re Columbia Gas Sys., Inc.)*, 33 F.3d 294, 295-96 (3d Cir. 1994) (noting that UST has “public interest standing” under 11 U.S.C. § 307 which goes beyond mere pecuniary interest); *Morgenstern v. Revco D.S., Inc. (In re Revco D.S., Inc.)*, 898 F.2d 498, 500 (6th Cir. 1990) (describing the UST as a “watchdog”).

3. Under 11 U.S.C. § 307, the UST has standing to be heard on the issues raised in these objections.

GROUND/BASIS FOR RELIEF

Introduction/Overview

4. On April 1, 2003, the Debtors filed the petitions which initiated the above-captioned cases.

5. On or about April 14, 2003, the UST formed the official committee of unsecured creditors (“OCUC”) in these cases pursuant to 11 U.S.C. §1102(a)(1).

6. Pursuant to 11 U.S.C. §§ 1107(a), 327(a), and 1103(a), the Debtors and the OCUC have retained various professionals to assist them in carrying out their respective fiduciary obligations.

7. A summary of the fee requests of nearly all estate professionals^{1/} for the first interim period is attached as Exhibit A.^{2/} The following points are supported by the exhibit:

- The compensation requested by the professionals listed for the first interim period totaled approximately \$25.5 million.
- Excluding those professionals whose employment was terminated by the Debtors

^{1/}

Exhibit A does not include professionals paid pursuant to this Court’s order authorizing the Debtors to employ professionals in the ordinary course of their businesses (Docket Entry #s 661 (motion), 1029 (order)). Further, Exhibit A does not include certain professionals involved in the Debtors’ asset disposition efforts; the fee and expense requests of Retail Consulting/Staubach (Docket Entry #s 942 (application), 1361 (order)) and Dovebid/AMH (Docket Entry #s 916 (application), 1359 (order)) are not listed on the exhibit. The Debtors have filed applications to retain certain professionals that have not been approved by this Court (e.g., Deloitte & Touche LLP). If the proposed professional has not filed a fee request, the professional is not listed on the exhibit. Finally, AP Services, LLC recently filed compensation reports for the months of April through June 2003. The UST has requested electronic time detail from the firm. The fee requests of AP Services, LLC will be reviewed separately.

^{2/}

While described as “attached,” the exhibits to this report/objections will be separately filed.

during April, the fee requests of the listed professionals employed by the Debtors' averaged approximately \$7.3 million/month during the first interim period. The fee requests of OCUC professionals averaged approximately \$780,000/month during the first interim period.

- The fee requests of Debtors' "327(a)" counsel (Kirkland & Ellis LLP and Pachulski, Stang, Ziehl, Young, Jones & Weintraub, P.C.) for the first interim period averaged approximately \$2.5 million/month. The fee requests of OCUC counsel (Milbank, Tweed, Hadley & McCloy LLP and Pepper Hamilton LLP) for the 1st interim period averaged approximately \$425,000/month.

I. ELECTRONIC FEE REVIEW

8. Pursuant to the amended administrative order approved by this Court on July 29, 2003 (Docket Entry # 2568), estate professionals are obligated to submit their time to the UST in electronic format for review. The UST notes that compliance with the electronic data provisions of the amended administrative order has been spotty. A copy of the amended administrative order is attached as Exhibit B. The UST is separately contacting those professionals whose submissions are delinquent to request that they contact the UST's staff promptly to resolve any technical issues. The UST intends to object to payment of monthly applications for compensation and reimbursement on a going-forward basis if professionals fail to comply with the terms of the amended order.

II. PROFESSIONALS

A. Debtors' "327(a)" Counsel – Kirkland & Ellis LLP; Pachulski, Stang, Ziehl, Young, Jones & Weintraub, P.C.

Staffing/Hourly Rates Charged

9. During the first interim period, Kirkland & Ellis LLP (“Kirkland”) and Pachulski, Stang, Ziehl, Young, Jones & Weintraub, P.C. (“Pachulski”) staffed the Fleming engagement with the following number of attorneys and paraprofessionals:

- Attorneys -- from Kirkland, a total of 75 attorneys (27 partners, 2 “of counsel,” 42 associates, 3 contract attorneys, and 1 “visiting attorney”), 33 of which billed more than 100 hours during the interim period (15 partners, 17 associates, and the visiting attorney); from Pachulski, a total of 26 attorneys (10 shareholders, 8 “of counsel,” and 8 associates), seven of which billed more than 100 hours during the interim period (4 shareholders, 2 “of counsel,” and 1 associate).
- Paraprofessionals -- from Kirkland, a total of 40 paraprofessionals (3 law clerks, 5 conflicts analysts, 13 legal assistants, 4 contract legal assistants, 9 project assistants, 4 case assistants, and 2 file assistants), 9 of which billed more than 100 hours during the interim period (5 legal assistants, 1 contract legal assistant, 2 project assistant, and 1 case assistant); from Pachulski, 21 paraprofessionals (1 law clerk, 10 paralegals, 1 legal document assistant, and 9 case management assistants), 2 of which (both paralegals) billed more than 100 hours during the interim period.

10. The blended hourly rate for Kirkland attorney fees during the interim period is \$421.11 ($\$5,552,437 \div 13,185$). The blended hourly rate for Pachulski attorneys during the interim period is \$419.07 ($\$1,333,956.70 \div 3,183.10$). The blended hourly rates for the “100 + hours” subset groups within both firms are slightly higher than the aforementioned blended hourly rates. For Kirkland, the blended hourly rate is \$424.92 ($\$5,031,782.50 \div 11,841.7$). For Pachulski, the blended hourly rate is \$421.60 ($\$1,287,722.70 \div 3,054.40$). The hours worked by the Kirkland “100 +

hours” subset break down as follows: 5,399.3 partner hours, 6,271.5 associate hours and 170.9 “visiting attorney” hours. The hours worked by the Pachulski “100 + hours” subset break down as follows: 1,502 partner hours, 826.5 “of counsel” hours and 725.9 associate hours.

11. The blended attorney hourly rates indicate that, on average, both the Kirkland and Pachulski firms are billing junior to mid-level partner hourly rates for attorney time. In Kirkland’s case, the blended hourly rate is higher than the hourly rates charged by Maureen Sweeney, a corporate partner admitted to practice in 1996 (\$410) and Damian Capozzola, a litigation partner admitted to practice in 1996 (\$410). In Pachulski’s case, the blended hourly rate is close to the hourly rate charged by Kenneth H. Brown (\$425), a shareholder with more than twenty years of experience.

12. Kirkland bankruptcy lawyers bill at higher rates than attorneys practicing certain non-bankruptcy disciplines. Using Ms. Sweeney and Mr. Capozzola’s hourly rates as examples, Kirkland charges hourly rates for the services of Ms. Sweeney and Mr. Capozzola that are \$10/hour less than the hourly rate charged for the services of Shirley Cho, a bankruptcy associate admitted to practice in 1997 (\$420) and \$50/hour less than the hourly rate charged for the services of Geoffrey Richards, a Kirkland partner admitted to practice the same year as Ms. Sweeney and Mr. Capozzola. Similarly, Kirkland charges \$50/hour more for the services of Richard Wynne, a bankruptcy partner admitted in 1982 (\$670) than it does for the services of Gregg Kirchhoefer, an intellectual property partner admitted to practice in 1982 (\$620). The only exception to this trend appears to be Kirkland’s taxation department, where certain attorneys are billed at a higher hourly rate than comparable bankruptcy personnel (for example, compare Natalie Keller, a tax associate admitted to practice in 1997, billing at \$425/hour with Ms. Cho’s \$420 rate, but also compare Robert Jason, a tax partner

admitted to practice in 1981, billing at \$615/hour compared to Robbin Itkin, a bankruptcy partner admitted to practice in 1984, billing at \$625/hour).

13. While 11 U.S.C. § 330(a) was intended to prevent bankruptcy attorneys from leaving the field because they earned less than their non-bankruptcy counterparts, the UST submits that the statutory subsection was not intended to enable firms to charge higher rates for the services of bankruptcy attorneys than those charged for the services of comparable non-bankruptcy attorneys. *See In re Busy Beaver Building Centers, Inc.*, 19 F.3d 833, 850-51 (3d Cir. 1994) (citing congressional Joint Explanatory Statement in footnote 24). In these cases, the information submitted by Kirkland suggests that the services of bankruptcy attorneys are billed at higher rates than non-bankruptcy professionals with similar experience. The UST submits that Kirkland has to provide a satisfactory explanation of its rate structure to this Court; absent a satisfactory explanation of Kirkland's rate structure, this Court should reduce the rates Kirkland charges for bankruptcy attorney services to bring them in line with the rates Kirkland charges for non-bankruptcy attorney services.

14. One factor to consider in evaluating whether a firm's fee request is reasonable is the overall staffing of the engagement. Specifically, top-heavy arrangements where partners bill a disproportionate amount of time are impermissible. Here, the numbers overwhelmingly suggest that the Pachulski firm has staffed the Fleming engagement with a disproportionate number of senior personnel. In addition to the "blended rate" analysis discussed previously, the UST took the list of all attorneys from Kirkland and Pachulski that billed time during the first interim period and grouped them into the following categories: senior partner (admitted to practice 1990 or earlier), junior partner (admitted to practice 1991 through the present), senior associate (admitted to practice 1997 or earlier), and junior associate (admitted to practice 1998 through the present). With respect to

Pachulski, the category “of counsel” was included in the grouping because it was a significant category. The UST then added up the number of hours worked by each category of attorneys at the firm and expressed those totals as a percentage of the whole. An exhibit detailing the results of the UST’s work is attached as Exhibit C. Exhibit C demonstrates that the number of hours worked by senior Pachulski personnel constitutes approximately 85% of the total hours worked by attorneys at the firm. The UST submits that it is inappropriate to be paying, on average, partner-level rates for the services of two law firms in these cases, especially where the expectation is that Pachulski will be primarily serving as local counsel. A downward adjustment of Pachulski’s compensation requests is warranted to bring the blended attorney hourly rates to a reasonable level.

15. Further, there are 61 Kirkland/Pachulski attorneys that did not bill 100 + hours. The more attorneys that are added to an engagement, the greater the likelihood that related inefficiencies are taxing the Debtors’ estates. Usually, each new attorney that is added to an engagement to perform a particular, discrete task has to have a certain level of background information regarding the cases in order to complete that task. Regardless of whether that background information is communicated to the new attorney or whether the new attorney has to undertake research to get that information, there is a cost associated with that process. The cost of introducing a new attorney to an engagement is reduced by limiting the total number of individuals assigned to the engagement. The UST submits that a reduction of Kirkland and Pachulski’s compensation requests to account for “introduction” costs is warranted.

Duplication of Effort – Internal Conferences/Meetings; Multiple Professionals Attending Conferences/Meetings

16. Another factor in considering the reasonableness of attorney compensation requests

is attendance at conferences and the cost associated with such conferences. The UST recognizes that, in the above-captioned cases, there was a fair amount of activity shortly after their inception. The demands of the Bankruptcy Code (e.g., the preparation of bankruptcy schedules) and the particular circumstances Fleming found itself in (e.g., ongoing sale processes) necessitate a certain level of communication between members of an engagement team regarding their respective assignments. That being said, this Court has both the authority and the obligation to reduce compensation requests where multiple members of the same firm excessively and repeatedly participate in discussions and teleconferences, a reduction of the firm's fees and expenses may be justified. Additionally, the Debtors' estates should not pay for excessive attorney time spent discussing matters internally.

17. In these cases, pursuant to the amended administrative order approved by this Court on July 29, 2003 (Docket Entry # 2568), estate professionals are obligated to submit their time to the UST in electronic format for review. Using the information submitted by the Kirkland and Pachulski firms, the UST searched for relevant terms. For example, a search of the fee program for the term "confer" generated spreadsheets which reflected the results of the UST's search. The Kirkland "confer" spreadsheet contains more than 3,700 time entries, and the Pachulski "confer" spreadsheet contains 1,600 time entries.

18. Based upon the UST's preliminary review of the "confer" spreadsheets, it appears that there are numerous instances in which two or more attorneys from Kirkland and/or Pachulski were present on a telephone call or at a meeting. The UST intends to report to this Court at a later date regarding her findings as to the reasonableness of fees charged for attendance at conferences and meetings after completing her analysis of the relevant data.

Duplication of Effort -- Attendance at Hearings

19. This Court's docket indicates that, during the first three months of these cases, Kirkland and Pachulski attorneys represented the Debtors at hearings before this Court as listed below (telephonic appearances noted with a parenthetical "T"):

- 4/3/03 – “First Day” Hearing (Sprayregen, Wynne, Cho (Kirkland); Jones, Kharasch, Lhulier (Pachulski)).
- 4/10/03 – Critical trade, interim DIP financing, etc. (Wynne (Kirkland); Jones, Lhulier (Pachulski)).
- 4/21/03 - 4/22/03 – Omnibus hearing (Wynne, Richards, Myers, Cho (T), Kotarba (Kirkland); Jones, Kharasch, McFarland (Pachulski)).
- 5/1/03 – Sara Lee, Alfred Nickles, Superior Dairy TRO hearing (Wynne, Capozzola (Kirkland); Brown, Lhulier (Pachulski)).
- 5/6/03 – Omnibus hearing (Wynne, Richards, Running, Sweeney, Kotarba (Kirkland); Jones, Lhulier (Pachulski)).
- 5/19/03 - 5/20/03 – Omnibus hearing (Wynne, Richards, Capozzola (T), Cho (T), Horwitz (Kirkland); Jones, Kharasch, Lhulier (Pachulski)).
- 5/23/03 – Telephonic hearing (Debtors' emergency motion to approve fifth Save-Mart letter agreement) (Richards (Kirkland)).
- 5/27/03 – Relief from cash management, class certification, TRO, etc. (Wynne, Richards, Liebler (Kirkland); Jones, Lhulier (Pachulski)).
- 6/4/03 – Omnibus hearing (Wynne, Richards, Anderson (Kirkland); Jones, Kharasch, Lhulier (Pachulski)).
- 6/25/03 – Omnibus hearing (Wynne, Richards, Liebler (T), Bledsoe (T), Cho (T) (Kirkland); Jones, Kharasch, Lhulier (Pachulski)).

20. While the UST recognizes that the Debtors should be adequately represented before this Court, that does not mean that the Debtors need to have five or six attorneys in court every time there is a hearing in these cases. The UST submits that a reduction in fees and corresponding

expenses is warranted to bring the staffing of hearings down to an appropriate level; at most hearings, three or four attorneys (assisted by paraprofessional staff, where appropriate) should be more than sufficient to represent the Debtors' interests.

Duplicate/Triplicate Time Entries

21. There appear to be duplicate time charges for the services of Willard J. Fraumann, P.C. on April 8, 2003. Similarly, there appear to be duplicate and triplicate time charges for the services of Richard L. Wynne on May 1, 2003. Pages from the relevant fee applications are attached as Exhibit D.

B. PricewaterhouseCoopers LLP

Variance from Fee Estimate

22. In Paragraph 11 of the Ranallo affidavit appended to the Debtors' application to employ PricewaterhouseCoopers LLP ("PwC"), Mr. Ranallo stated that the fees that PwC would charge for services to be rendered to the Debtors' estates would total "approximately \$500,000, excluding expenses."

23. During the first interim period, PwC billed approximately \$1.25 million. PwC's fees continue to accrue; for the months of July 2003 (the first month of the second interim period), PwC billed \$186,635 in fees and \$5,740.68 in expenses to the Debtors' estates (Docket Entry # 3364).

24. The UST submits that, while a reasonable variance from the fee estimate submitted by PwC at the outset of these cases may be allowable upon an appropriate factual showing, a variance approaching 200% of the estimated amount (which is where the PwC account presently stands) is unwarranted. The Debtors have not sought to expand the scope of the initial PwC

retention, and PwC has not explained in any of its fee applications why the Debtors' estates should be saddled with a variance of approximately \$1 million from PwC's initial \$500,000 fee estimate. Given that PwC was working for Fleming prior to the inception of these cases, PwC's fee estimate should be accurate. The UST submits that the failure of the Debtors to provide advance notice of, and a reasonable explanation for, the variance from the estimate to this Court warrants a substantial reduction of PwC's fee request.

Lack of Detailed Time Entries

25. Pursuant to Del. Bankr. LR 2016-2(d)(ii), fee applications must contain complete and detailed activity descriptions.

26. The UST notes that a number of the time entries logged by PwC's partners fell below the "complete and detailed" standard mandated by the local rules. Entries such as "[r]eview workpapers" (Reddin, 4/3/03) or "review documents" (Ranallo, 4/11/03) do not specifically identify what is being reviewed and the purpose for the review. "Project management" (O'Hare, 4/17) does not describe what project is being managed and, more specifically, the persons who the partner is directing. "Discussions with Counsel" (Ranallo, 4/30/03) does not identify the identity of counsel and what the purpose of the call was. The examples listed in this paragraph are merely that – examples. There are additional vague entries in PwC's time sheets. The UST submits that a reduction in fees may be warranted due to PwC's noncompliance with Local Rule 2016-2(d)(ii).

C. Baker Botts

Time Spent on Retention Issues

27. The Baker Botts firm seeks an award of approximately \$53,000 for time spent on issues related to the firm's retention. This Court previously expressed concerns regarding the

representation by Baker Botts of both Fleming and the company's directors and officers in connection with the pending Securities and Exchange Commission investigation. The efforts expended by Baker Botts in removing itself from its conflicted position should not be charged to the Debtors' estates; the \$53,000 amount is excessive and should be reduced.

Redacted Time Entries/Time Spent Related to Baker Botts' Representation of Directors and Officers

28. The Baker Botts' fee applications contain several pages containing time entries that are marked "redacted." The Baker Botts firm should file a motion seeking to file the time entries under seal and, if cause for sealing is established, nevertheless provide the redacted entries to the UST.

29. Further, it appears that Baker Botts attorneys may have logged time entries related to Baker Botts' representation of Fleming's directors and officers under the "SEC Investigation" matter. The UST cannot determine the extent of this practice because Baker Botts submitted redacted time entries under that header without prior approval of this Court. The UST reserves the right to request that the Baker Botts fee request be reduced in an appropriate amount after the UST has reviewed and identified all of the relevant time entries.

D. Ernst & Young LLP

Disclosure of Connections with C&S

30. Undersigned counsel was previously advised by counsel to Ernst & Young LLP ("E&Y") that E&Y planned to file a supplemental affidavit disclosing its connection(s) with C&S Wholesale Grocers, the purchaser of a portion of the Debtors' wholesale grocery division.

31. The UST has searched the docket for the supplemental affidavit as filed without success. The UST requests that E&Y produce a copy of the executed affidavit for her review. If

E&Y has not filed the supplemental affidavit, it should do so immediately. The UST reserves all rights related to the timing of the filing of the supplemental affidavit and matters to be disclosed therein. If E&Y has not filed the supplemental affidavit, the UST submits that no further interim compensation and reimbursement should be awarded to E&Y until it files the document.

E. Rider Bennett

32. In a number of instances, the Rider Bennett time entries violate Del. Bankr. LR 2016-2(d)(vii), which requires that activity descriptions each have a separate description and time allotment. After reviewing the “lumped” time entries in the Rider Bennett application, the UST suggests that a nominal reduction of the fee request and an agreement by Rider Bennett to correct the deficiency in future applications would be appropriate.

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CONCLUSION

33. The UST reserves all discovery rights in connection with these objections.

34. Any objections not specifically raised in this pleading are reserved for a hearing on final approval of the professional's compensation and reimbursement.

WHEREFORE the UST requests that this Court issue an order consistent with this report/these objections.

Respectfully submitted,

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Date: September 22, 2003