IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF DELAWARE

In re: BOY SCOUTS OF AMERICA and DELAWARE BSA, LLC, Debtors.	Civil Action No. 20-cv-00798 (RGA)
CENTURY INDEMNITY COMPANY, WESTCHESTER FIRE INSURANCE COMPANY and WESTCHESTER SURPLUS LINES INSURANCE COMPANY, Appellants, v. BOY SCOUTS OF AMERICA and DELAWARE BSA, LLC, Appellees.	On appeal from the U.S. Bankruptcy Court for the District of Delaware Bankruptcy Case No. 20-10343 (LSS) Bankruptcy BAP No. 20-13

APPELLANTS' REPLY BRIEF ON APPEAL

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PRELIMINARY STATEMENT

This appeal starts and ends with unchallenged factual findings made by the bankruptcy court: Sidley was Century/Chubb's counsel on the petition date, and remained counsel while Sidley filed a plan of reorganization with multiple terms impairing Century's contract rights, structured around a trust funded in large measure with Century's policies. Sidley thus indisputably had a *current* conflict of interest, thereby precluding its retention under Section 327's plain language, even under the bankruptcy court's erroneously narrow reading of that language. Applying Section 327 in conjunction with the ethical rules that govern attorney conduct in bankruptcy further underscores that result. Sidley raises many unsupported and irrelevant factual assertions, but none of them alters the dispositive finding below that Sidley had a live conflict on the date of retention, which is categorically impermissible under Section 327.

But that is not the only reason the bankruptcy court erred. On the bankruptcy court's own factual findings, Model Rules 1.7 and 1.9 provide two additional and independent reasons for disallowing the retention application. Sidley's retention plainly violates the ethical rules in light of the court's findings that (i) Sidley worked on matters for Century/Chubb involving claims it "paid or in the future would pay to BSA under insurance policies Century issued to BSA," (ii) Sidley was still Century/Chubb's counsel when BSA filed for bankruptcy and

filed BSA's plan of reorganization, and (iii) Century/Chubb never consented to or waived Sidley's conflict.

The bankruptcy court itself acknowledged that ethical rules are "not irrelevant" to retention applications in bankruptcy, but the court nevertheless declined to apply Rule 1.7, which prohibits a lawyer from representing "a client if the representation involves a *concurrent* conflict of interest." There is simply no way to reconcile Sidley's retention with that rule and the fact that Sidley was Century/Chubb's counsel when BSA filed for bankruptcy, and indeed had already been working for Century/Chubb on matters involving BSA insurance policies for nearly a year and half.

The bankruptcy court also misapplied Rule 1.9(a). Having found as a fact that "the reinsurance litigation could be '*substantially related*' to at least some aspects of Boy Scout's bankruptcy case for purposes of Rule 1.9" and that "Sidley received from Century information relevant to the BSA bankruptcy," the bankruptcy court should have barred Sidley under Rule 1.9(a). That rule prohibits a law firm that "formerly represented a client" from representing a person absent consent "in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client." The bankruptcy court's own findings easily satisfy that standard.

The conflict here is one that Sidley could not cure by dropping Century/Chubb as a client or by installing separate coverage counsel and an ethical screen between Sidley's BSA restructuring lawyers and Sidley's Century/Chubb reinsurance lawyers. As Sidley's expert admitted, a screen does nothing to mitigate a conflict that existed before it was set up. And the bankruptcy court acknowledged that Sidley's screen did not comply with the Model Rules. To protect clients, Rule 1.10 *presumes* that improper information-sharing occurs during a dual representation—the court need not make a separate finding to that effect. That protective assumption is especially essential here, given that Century/Chubb's insurance policies are both central to the bankruptcy and were the subject of Sidley's reinsurance work for Century/Chubb.

Finally, Sidley errs in trying to shift the burden of proof to Century/Chubb on the ground that the order on appeal resulted from a motion to disqualify. It did not. This is an appeal from Debtors' motion to approve Sidley as bankruptcy counsel. Century/Chubb was not the movant and did not request disqualification. Under the statute, the burden was—and is—on Sidley (and Debtors) to justify Sidley's retention despite its conflicts and adverse interests. They cannot do so.

* * *

Were this Court to allow the order on appeal to stand, lawyers in bankruptcy would consider themselves free from the obligations of Rule 1.7. The results

would be intolerable: lawyers could drop long-standing clients like "hot potatoes" to take on higher-paying debtor-clients, as long as they terminated whatever current clients posed the conflicts. That outcome would contravene attorneys' most fundamental ethical duties, particularly as they apply in bankruptcy court through Section 327.

ARGUMENT

I. THE BANKRUPTCY COURT ERRED IN APPROVING THE RETENTION UNDER SECTION 327.

A. On finding that Sidley continued to represent Century/Chubb after the petition date, the bankruptcy court lacked discretion to approve the retention under Section 327.

Sidley's main argument is that the bankruptcy court correctly ruled that Sidley's retention was consistent with Section 327's requirements. It plainly was not. Having found that Sidley continued to represent Century/Chubb until *after* the petition date, the bankruptcy court had no discretion to approve the retention. Where, as here, a firm has an existing conflict on the date of retention, Third Circuit precedent requires "per se disqualification" under Section 327.[1]

According to the Third Circuit "a conflict is actual, and hence *per se* disqualifying, if it is *likely* that a professional will be placed in a position

[1] *In re Marvel Entm't Grp., Inc.*, 140 F.3d 463, 476 (3d Cir. 1998); *In re Pillowtex*, 304 F.3d 246, 251 (3d Cir. 2002); *In re Fleming Cos.*, 305 B.R. 389, 393 (Bankr. D. Del. 2004); *cf. Parallel Iron, LLC v. Adobe Sys. Inc.*, No. CA 12-874-RGA, 2013 WL 789207, at *4 (D. Del. Mar. 4, 2013).

permitting it to favor one interest over an impermissibly conflicting interest."[2] Actual, disqualifying conflicts of interest are not limited only to those situations that have been previously addressed by the courts (such as voidable transfers); rather, "the term 'actual conflict-of-interest' is not defined in the Code and has been given meaning largely through a case-by-case evaluation of particular situations arising in the bankruptcy context."[3]

Sidley proffers three arguments to justify its retention under Section 327. None has merit. *First*, Sidley asserts that Century has not identified any specific "situation in which Sidley may have been unable to take actions necessary to zealously represent BSA's interests in the bankruptcy."[4] Century bears no such burden under Section 327. As just noted, under Third Circuit precedent, the rule is *categorical*: a firm subject to an existing conflict on the date of retention simply cannot be retained, without any separate inquiry into whether it can still discharge its duties despite the conflict. And the burden is squarely on the firm to show that it lacks any conflict or otherwise does not "represent an interest adverse to the estate."[5]

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2 *Pillowtex*, 304 F.3d at 251 (emphasis added).

3 *Id*. (quoting *In re BH&P, Inc.,* 949 F.2d 1300, 1315 (3d Cir. 1991).

4 Appellees' Answering Brief ("Br.") at 24.

5 *In re Vascular Access Centers, L.P.*, 613 B.R. 613, 624 (Bankr. E.D. Pa. 2020) (quoting *In re Big Mac Marine, Inc.,* 326 B.R. 150, 154 (8th Cir. BAP 2005)); *In re Duvall*, No. 19-112272, 2020 WL 1492769, at *2 (Bankr. W.D. Ky. Mar.

Second, Sidley complains that the period of concurrent representation following its formal retention was "short" and that its representation of Century/Chubb was only "technically active."[6] No case permits "just a little" dual representation. And several of the Chubb matters were more than "technically active" even post-petition; for example, the record shows that Sidley emailed an arbitration panel on Chubb's behalf on the day after BSA filed for bankruptcy.[7] There is no basis for Sidley's naked assertion that the representation here was *de minimis* or trivial. Nor did the bankruptcy court make any such finding. What is more, Sidley obviously knew that it had a conflict requiring a written waiver, given that Sidley itself sought an advance waiver in the winter of 2018–19, and then partner William Sneed emailed to ask Century/Chubb about waivers for a transactional matter and a subpoena for another matter.[8] Sidley's persistent (but unsuccessful) efforts to obtain a waiver give the lie to its opportunistic, litigation-generated contention that no waiver was required.

25, 2020) ("While the burden of proof in seeking disqualification of opposing counsel is on the party seeking disqualification, a professional seeking appointment under Section 327 bears the initial burden of proof that they meet all qualifications of the statute in order to obtain appointment.").

6 Br. at 23–24.

7 APP0858–62, Schwartz Decl. Ex. 9; APP0864–68, Schwartz Decl. Ex. 10.

8 APP0790–93, Sneed Decl. Ex. 1, 2; APP0891–1162, May 4, 2020 Hr'g Tr. ("Tr.") at 190:1–25; Appellants' Opening Br. at 9.

Third, Sidley asserts that its ongoing obligations to Century/Chubb are unrelated to the bankruptcy. Even if that assertion were true—it manifestly is not—Sidley's retention still would be impermissible under Section 327. The bankruptcy court found that "Century's insurance policies with BSA are assets of the BSA bankruptcy estate" seeking to retain Sidley, and that the policies "include the same underlying Century/BSA insurance policies" for which Century employed Sidley "to collect reinsurance from Lloyds and the second reinsurer."[9] Sidley's obligations to Century/Chubb concerning those policies unambiguously constitute interests adverse to the estate under Section 327. And the bankruptcy court also found that this dual representation by Sidley continued during the bankruptcy even before BSA ever applied to have the retention approved.[10]

Tellingly, the bankruptcy court did not agree with Sidley's contention that no conflict or adverse interest ever existed. To the contrary, the court allowed the representation *only* because insurance co-counsel was in place. If the matters were unrelated, there would have been no need for the court to order that insurance co-counsel, rather than Sidley, must handle all matters that implicate Century's coverage.[11] Moreover, Sidley could not have been that indispensable to Debtors—

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[9] APP1213–28 ("Ruling") at 11 at 2.

[10] *Id.*

[11] Ruling at 14.

as BSA and Sidley argue—given Morris Nichols' presence as general bankruptcy co-counsel.

B. Under Third Circuit law, a court should consider ethics rules in applying Section 327.

While Sidley's retention contravenes Section 327 on its own terms, that conclusion is reinforced here by ethical rules that govern practice in bankruptcy court. Sidley suggests that the ethical rules are irrelevant to Section 327, but Sidley is wrong. As the Third Circuit explained in *Congoleum*, "attorneys retained in bankruptcy proceedings" must satisfy *both* "the restrictions imposed by Section 327" *and* "the standards established by professional ethics."[12] The *Collier* treatise recites the same rule, stating that "apart from the particular requirements of the Bankruptcy Code or rules," attorneys practicing in bankruptcy court are "bound by" the relevant ethical codes.[13]

Illustrating the interconnection between Section 327 and the ethical rules, courts have applied the ethical rules to determine whether an "actual conflict" exists under Section 327.[14] As the *Congoleum* court observed, "[o]ur discussion of

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[12] *In re Congoleum Corp.*, 426 F.3d 675, 688 (3d Cir. 2005); *see also In re Star Broadcasting, Inc.*, 81 B.R. 835, 839 (Bankr. D.N.J. 1988) ("In addition to the standards in Section 327(a) … many courts have relied on the Rules of Professional Conduct for guidance in determining whether a conflict-of-interest exists in a law firm's representation of parties to a bankruptcy.").

[13] 1 Collier on Bankruptcy, § 8.03[2] (16th ed. 2020).

[14] *Congoleum*, 426 F.3d at 692; *Rome v. Braunstein*, 19 F.3d 54, 60 n.4 (1st Cir.

the Rules of Professional Conduct demonstrates that [conflicted counsel] also cannot meet the Bankruptcy Code's requirement of disinterestedness contained in section 327(a)."[15] To be sure, not every violation of any ethical rule will necessarily constitute a Section 327 violation. But because Section 327 is expressly concerned with conflicts and adversity, the conflict-of-interest rules have special force under that provision. Indeed, courts have recognized that because of the many parties and interests involved in a bankruptcy, there is a *heightened* need to avoid ethical conflicts among actually and potentially competing interests. Bankruptcy courts thus "often set higher standards for the application" of ethical concepts "such as loyalty, independent judgment and even who is considered a client."[16] Bankruptcy courts enforce these rules "through, among other mechanisms, disqualifications of counsel or disapproval of the appointment of

1994) (noting that "[t]he Bankruptcy Code provisions dealing with conflicts-of-interest find their counterparts in the ABA Code of Professional Responsibility") (internal quotations omitted).

15 *Congoleum*, 426 F.3d at 692.

16 *Id.*; 1 Collier on Bankruptcy ¶ 8.01[1] ("Ethical rules are often considered more necessary and applicable in bankruptcy cases."); *id* ¶ 8.03[1] ("Conflict of interest rules are more strictly applied in the bankruptcy context than in other areas of the law, at least insofar as they relate to professionals retained by the estate.").

counsel."[17] In so doing, "doubts as to the existence of an asserted conflict of interest should be resolved in favor of disqualification."[18]

As shown in the following sections, Sidley's retention violates Rules 1.7 and 1.9. Those violations themselves constitute violations of Section 327. In this respect, at least, Section 327 does not look exclusively to the interests of the estate, as Sidley and the bankruptcy court contend. But to the extent it does, Section 327 still prohibits the kind of concurrent representation at issue here, because Sidley's obligations to the estate were necessarily in conflict with Sidley's obligations to Chubb vis-à-vis BSA's policies, which were central to the plan of reorganization that Sidley drafted for BSA and critical estate assets. Sidley thus held an interest adverse to the estate, mandating per se disqualification under Section 327. *See supra* at I.A.[19]

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[17] *In re Berger McGill, Inc.*, 242 B.R. 413, 418 (Bankr. S.D. Ohio 1999); *see In re Universal Bldg. Prods.*, 486 B.R. 650, 661 (Bankr. D. Del. 2010) (violation of Model Rules was grounds to disqualify counsel from employment under section 327 of the Bankruptcy Code); *Baron & Budd, P.C. v. Unsecured Asbestos Claimants Comm.*, 321 B.R. 147, 164 (D.N.J. 2005) ("Not only are state ethical laws imposed upon professionals in the bankruptcy context, but the Bankruptcy Code and Federal Rules of Bankruptcy Procedure contain specific references and directives imposing additional ethical obligations upon attorneys and other professionals.").

[18] *In re Meridian Auto. Sys.-Composite Operations, Inc.*, 340 B.R. 740, 750 (Bankr. D. Del. 2006).

[19] The *Marvel*/*Pillowtex* rule requiring per se disqualification for an existing interest adverse to the estate is amplified by the lack of any materiality requirement for such an adverse interest. By contrast, the statute prohibits

II. SIDLEY'S RETENTION IS IMPERMISSIBLE UNDER THE RULES OF ETHICS.

A. After finding that Sidley had a current conflict, the bankruptcy court erred in not applying Rule 1.7 to disallow the retention application

The bankruptcy court correctly held that Rule 1.7 "prevents an attorney from representing one current client against another current client absent a written waiver."[20] The court also rightly noted that the rule "reflects the complete and undivided loyalty an attorney owes to its client."[21] The court, however, stopped there and did not apply Rule 1.7, despite finding that Sidley (i) still represented Century/Chubb after the bankruptcy petition was filed and (ii) never obtained a waiver of "any conflict with respect to its concurrent representation of Century in reinsurance matters and BSA in restructuring matters."[22] Indeed, the bankruptcy court found that Sidley had been representing Century/Chubb and BSA

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conflicts with the interests of *creditors* only when the conflict is material. *See Pillowtex*, 304 F.3d at 252 n.4 ("disinterested person" standard "requires that a professional be free of 'an interest *materially* adverse to the interest of … any class of creditors.'" (emphasis added) (quoting 11 U.S.C. § 101(14)(E)). No such materiality qualifier exists in the statutory prohibition against interests adverse to the estate.

[20] Ruling at 7; *see* Model R. Prof'l Conduct 1.7.

[21] Ruling at 7.

[22] *Id.*

concurrently with respect to BSA's Century/Chubb policies here for well over a year.[23]

In that time, Sidley sought to resolve BSA's sexual-assault liabilities by using insurance proceeds, including from Century/Chubb's policies. The proposed plan of reorganization and disclosure statement—which Sidley filed on BSA's behalf—contemplate a trust funded in large measure with Century/Chubb's policies.[24] These documents and the positions they advocate were—and remain—adverse to Century/Chubb's interests. And given the length of these documents (the proposed plan alone is 60 pages) Sidley must have worked on them for weeks or months before filing the petition, all while Sidley was representing and carrying a duty of loyalty to Century/Chubb.

The bankruptcy court specifically found that Sidley was still Century/Chubb's counsel on three matters on the date of BSA's bankruptcy petition.[25] Sidley's conflict thus ran from October 2018—when it began advising both entities concurrently—through and beyond the filing date, when it was formally appointed counsel to the estate. The facts here constitute a straightforward breach of Sidley's duty of loyalty to its longstanding client

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[23] Ruling at 1–2.

[24] APP0240–41, Debtors' Chapter 11 Plan at 28–29; APP0171, Debtor's Mediator Motion at 9; APP0330, Debtors' Disclosure Statement at 26.

[25] Ruling at 2.

Century/Chubb. As this Court has held, "[b]ecause the interest sought to be protected by Rule 1.7 is one of loyalty, a *per se* rule of disqualification should be applied when that rule is breached."[26]

Sidley makes two Rule 1.7 arguments, neither of which is relevant to the analysis. *First*, Sidley asserts that there has been no proceeding directly between Century/Chubb and Sidley, and that Sidley has not cross-examined a Century/Chubb witness in connection with coverage issues (though Sidley cross-examined Chubb's Christine Russell and Joshua Schwartz in trying to secure its retention).[27] That is both beside the point and inaccurate. BSA and Century/Chubb have been adverse since before Sidley took on BSA as a client.[28] And, crucially, Century/Chubb and BSA have been on opposite sides of contested matters in the bankruptcy since its inception. Sidley's dual representation of both entities is more than sufficient to establish a violation of Rule 1.7.[29] And there was active adversity between BSA and Century/Chubb in this bankruptcy from the start. In Sidley's own words, "[a]fter appearing, and before the bankruptcy court

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[26] *Parallel Iron*, 2013 WL 789207 at *4 (*quoting Manoir–Electroalloys Corp. v. Amalloy Corp.*, 711 F. Supp. 188, 195 (D.N.J.1989)).

[27] Br. at 49.

[28] APP0540, APP0546–62, APP0577–613, April 14 Panchok-Berry Decl. ¶¶ 3, 5, Ex. B, D.

[29] *In re Cendant Corp. Sec. Lit.*, 124 F. Supp. 2d 235, 243 (D.N.J. 2000) (internal quotations omitted).

approved Sidley's retention, Century filed or joined no fewer than four objections on various matters in addition to Sidley's employment."[30] Sidley thus started litigating against Century/Chubb's interests immediately, and has continued to do so since.

Second, Sidley misunderstands Century/Chubb to be arguing that *any* marginal involvement by Sidley in this bankruptcy would make it adverse to Century/Chubb.[31] Century/Chubb argues no such thing. Rather, Century/Chubb argues, and the undisputed facts are, that Sidley is BSA's *lead* counsel in the bankruptcy, where insurance proceeds are a *central asset*. By BSA's own account, insurance "will comprise a substantial portion" of the trust Sidley will be litigating to establish as part of its formulation and confirmation of a plan of reorganization.[32] If Sidley is as irreplaceable to BSA's workout as it suggests, it cannot plausibly blind itself to such a critical estate asset and wholly ignore insurance issues that could be resolved adversely to Chubb's interests.

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[30] Br. at 16, n.5. These motions included substantive issues impairing Century's rights, including the preservation of privilege. *See* Appellants' Opening Br. at 13–15.

[31] *See* Br. at 49.

[32] APP0082, Whittman Decl. ¶ 57; *see also* APP0332, Disclosure Statement at 28 ("As a general matter, the amount of remaining coverage under these policies is substantial, and the BSA expects that the proceeds of these policies will comprise a significant portion of the assets contributed to any victims compensation trust.").

B. Sidley fails to establish that the hot-potato doctrine does not apply

Under the hot-potato doctrine, Sidley did not eliminate its conflict by dumping Century/Chubb just before BSA requested that the bankruptcy court approve the retention. Not only was the appointment retroactive to the petition date, when Sidley *still* represented Century/Chubb, but what matters under Rule 1.7 is whether a concurrent representation existed at that time of the dual representation.[33]

Sidley's effort to eliminate the conflict before the court evaluated its retention falls squarely within the hot-potato doctrine recognized by other courts in this Circuit. While Sidley makes a half-hearted attempt to distinguish those cases by limiting them to their facts,[34] it fails to explain why the principal—that courts should not permit parties to game the ethical rules through tactical withdrawals—is not equally applicable here. Sidley had a concurrent conflict that endangered a

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[33] *See*, *e.g.*, *Unified Sewerage Agency of Wash. v. JELCO, Inc.*, 646 F.2d 1339, 1345 n.4 (9th Cir. 1981) ("[T]he present-client standard applies if the attorney simultaneously represents clients with differing interests. *This standard continues even though the representation ceases prior to the filing of the motion to disqualify*." (emphasis added)); *Atl. Specialty Ins. Co. v. Premera Blue Cross*, No. C15-1927-TSZ, 2016 WL 1615430, at *13 (W.D. Wash. Apr. 22, 2016); *Merck Eprova AG v. ProThera, Inc.*, No. 08CIV0035RMBJCF, 2009 WL 10696470, at *6 (S.D.N.Y. Oct. 6, 2009); *Florida Ins. Guar. Ass'n v. Carey Canada, Inc.*, 749 F. Supp. 255, 261 (S.D. Fla. 1990).

[34] Br. at 41.

lucrative opportunity to work for BSA, and it attempted to escape the implications of that conflict by dumping Century/Chubb as a client and then arguing that only the *former* client rules apply.[35] The hot-potato doctrine bars an attorney from resolving a conflict under Rule 1.7 by simply withdrawing from the original representation. "To hold otherwise," one court explained, "would allow such unethical behavior to continue unrestricted because a law firm could always convert a present client to a former client merely by seeking to withdraw after suing a present client."[36] This is the nub of the hot potato doctrine:

> [A] firm may not circumvent Model Rule 1.7 by dropping a present client or characterizing him as a former client in order to take on a conflicting and, quite possibly, more lucrative client. Were it otherwise, both the duty of undivided loyalty to the client and public confidence in attorneys and the legal system would be undermined.[37]

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[35] *Santacroce v. Neff*, 134 F. Supp. 2d 366, 370 (D.N.J. 2001); *Int'l Longshoremen's Ass'n, Local Union 1332 v. Int'l Longshoremen's Ass'n*, 909 F. Supp. 287, 293 (E.D. Pa. 1995); *Davis v. Kraft Foods N. Am*, No. 03-6060, 2006 WL 237512, at *12 (E.D. Pa. Jan. 31, 2006); Appellants' Opening Br. at 39.

[36] *Ransburg Corp. v. Champion Spark Plug Co.*, 648 F. Supp. 1040, 1044 (N.D. Ill. 1986) (emphasis added).

[37] *Santacroce*, 134 F. Supp. 2d at 371 (quoting *Schiffli Embroidery Workers Pension Fund v. Ryan, Beck & Co.*, No. 91-5433, 1994 WL 62124 at *3 n.2 (D.N.J.1994)).

Trying to "cure" a conflict by withdrawing from the original representation is fundamentally wrong because no attorney should elevate his or her financial incentives over the clients' interests.[38]

Accordingly, even after Sidley tried to drop Century/Chubb as a client post-petition, its obligations under Rule 1.7 continued.[39] And while the bankruptcy court found that Sidley continued to be Century/Chubb's attorney after the petition date, it erroneously failed to apply Rule 1.7 and preclude BSA from retaining Sidley to work on a bankruptcy inherently at odds with Century/Chubb's interests.[40]

Sidley responds that the Third Circuit never adopted the hot-potato doctrine. While the Third Circuit has not yet had occasion to address the question directly, its holding in *Congoleum* that attorneys retained in bankruptcy must satisfy "the standards established by professional ethics" anticipates the answer: it is exceedingly unlikely the court would not render Rule 1.7 functionally

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[38] *See* Geoffrey C. Hazard, Jr. & W. William Hodes, *The Law of Lawyering* § 20.10 at 20–24 (3d ed. 2001); Richard W. Painter, *Advance Waiver of Conflicts*, 13 Geo. J. Legal Ethics 289, 322 (2000); Charles W. Wolfram, *Symposium: Restatement of the Law Governing Lawyers, Former-Client Conflicts*, 10 Geo. J. Legal Ethics 677, 708 (1997).

[39] *Santacroce*, 134 F. Supp. 2d at 370–71.

[40] Ruling at 7–11.

meaningless by allowing attorneys to drop a current client to vitiate an existing conflict with a new, higher-paying debtor-client.

C. After finding that Sidley's work "could be 'substantially related'" to the bankruptcy case, the court below erred in allowing the retention application under Rule 1.9

The court also improperly failed to find a retention-preventing conflict under Rule 1.9, which precludes a firm from representing a client in a matter "substantially related" to its work for a former client. The bankruptcy court held that the matters "could be 'substantially related,'" and then stated that "the question becomes therefore whether … conflicts counsel solves any ills here."[41] This passage must be taken as a finding of a substantial relationship; otherwise there would have been no reason to consider the effectiveness of conflicts counsel. That finding should have precluded Sidley's retention under Rule 1.9.

In relying on conflicts counsel to excuse the of Rule 1.9 violation, the bankruptcy court departed from the model rules and Third Circuit law applying those rules. Whether conflicts counsel could prevent confidences from actually being shared is irrelevant. The Third Circuit held in *In re Corn Derivatives Antitrust Litigation* that Rule 1.9 is a "prophylactic rule" that presumes that, where a former and current representation are substantially related, the former client's

[41] Ruling at 10–11.

confidences are at risk and "disqualification is proper."[42]

Sidley's argument that no substantial relationship exists cannot overcome either the bankruptcy court's finding, or precedent in the Third Circuit and this Court holding that Rule 1.9 applies whenever there is merely "the *potential* that a former client's confidences and secrets may be used against him."[43] As this Court has held, matters are "substantially related" where there is "factual overlap" between them that "raises 'a common-sense inference'" that knowledge gained in a former representation "*could* be" used against that client in the present litigation.[44] The former client need not prove that its information *actually* has been used, as Sidley asserts.

As the facts that the bankruptcy court found demonstrate, there is much more than "potential" that Sidley received confidential information that could be used against Century/Chubb in the bankruptcy:

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[42] *See In re Corn Derivatives Antitrust Litig.*, 748 F.2d 157, 162 (3d Cir. 1984); *Intellectual Ventures I LLC v. Checkpoint Software Techs.*, No. CIV. 10-1067-LPS, 2011 WL 2692968, at *5 (D. Del. June 22, 2011) (internal quotation marks and citations omitted).

[43] *In re Corn Derivatives Antitrust Litig.*, 748 F.2d 157, 162 (3d Cir. 1984) (emphasis added).

[44] *Innovative Memory Sols. v. Micron Tech.*, No. CV 14-1480-RGA, 2015 WL 2345657, at *3 (D. Del. May 15, 2015) (emphasis added) (quoting *Intellectual Ventures*, 2011 WL 2692968, at *5); *see also Rohm & Haas Co. v. Am. Cyanamid Co.*, 187 F. Supp. 2d 221, 228 (D.N.J. 2001) ("The ***mere possibility*** that a lawyer might have possession of confidential information satisfies the 'substantially related' test under RPC 1.9." (emphasis added)).

- Century/Chubb was a longtime Sidley client both for "specific arbitration proceedings and general counseling matters";
- Sidley's work included matters involving "claims Century paid or in the future would pay to BSA under insurance policies Century issued to BSA";
- the insurance policies at issue in the two BSA-related reinsurance matters Sidley was handling for Century/Chubb are "assets of the BSA bankruptcy estate."[45]

The Court also credited the testimony of Christine Russell that Sidley had received detailed information about the policies that Century/Chubb issued to BSA and that the relief sought in the matters Sidley was representing Chubb in "included not only relief with respect to claims already paid under the policies Century issued to BSA, but claims that BSA would make under the policy in the future," and "that those future claims [for reinsurance payments] were significant assets of Chubb."[46] The court noted that Ms. Russell's account was supported by its own review of the record in one of Sidley's BSA-related engagements for Century, which reflected that the "matter did not involve only the reinsurance contract" but "also involved an agreement between BSA and Century—the First

[45] Ruling at 1–2. While Sidley tries to split hairs on page 44 of its opposition brief about how much and what privileged information was conveyed, the record below was undisputed that privileged information was conveyed between Chubb and Sidley concerning BSA. Sidley acknowledged this, Tr. at 161:13–15, 256:5–7, and the bankruptcy court did not find otherwise. Ruling at 10–11.

[46] Ruling at 9.

Encounter agreement."[47] That same agreement, the bankruptcy court noted, "has already been the subject of testimony in this court in connection with the BSA's motion for preliminary injunction with respect to the abuse victims' lawsuits."[48]

Despite these findings, the court failed to apply Rule 1.9. The court instead relied on the presence of a belated ethical screen and co-counsel as curative measures.[49] But neither is sufficient to cure the conflict.

It was improper for the court to rely on insurance co-counsel, who were retained for a limited role in the bankruptcy under Section 327(e), to cure Sidley's conflict as general bankruptcy counsel retained under Section 327(a). Lawyers that are retained for the purpose of advising on a plan of reorganization are retained under Section 327(a) as "general" bankruptcy counsel and are subject to heightened scrutiny.[50] Under the statutory scheme of Section 327, tasks such as developing the plan of reorganization by definition fall under 327(a), and are not subject to delegation to conflicts counsel retained under the much narrower terms of 327(e).[51] Nor was it possible to do so as the plan of reorganization is entirely

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[47] Ruling at 10. Sidley's account at pages 5–6 of its brief that there was only one remaining substantive issue between Century and Lloyd's is inconsistent with this finding.

[48] *Id.*

[49] Ruling at 11.

[50] 11 U.S.C. § 327(a).

[51] *Congoleum*, 426 F.3d at 692; *see* Appellants' Opening Br. at 47 n.162.

infected with and structured around insurance issues. Sidley does not contest this basic rule or distinguish any of the cases cited by Century on this point.[52]

The bankruptcy court also improperly relied on Sidley's self-serving assurance that no information had passed between its BSA bankruptcy lawyers and Chubb's reinsurance counsel Sneed. Under Model Rule 1.10, a screen is only permissible to cure imputation of a former-client conflict where (i) the screen is timely; (ii) written notice of the screen is given to the former client; and (iii) ongoing certifications of compliance are given to the former client.[53] The bankruptcy explicitly acknowledged that Sidley's untimely screen did *not* suffice to avoid or cure its violation of the ethical rules, but it simply declined to enforce the rules here.[54] That ruling cannot be reconciled with settled Third Circuit precedent and other authority holding that courts not only must apply ethical rules in bankruptcy proceedings, they must apply those rule with extra rigor.[55]

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[52] *Id.*

[53] Model R. Prof'l Conduct 1.10(a)(2).

[54] Ruling at 11–12 ("While a retroactive ethical screen may not work for purposes of violations of the Rules of Professional Conduct, based on the unrefuted testimony, I conclude that any confidential or privileged information that Mr. Sneed received in his representation of Century in its reinsurance matters has not and will not be passed along to Sidley's restructuring team.").

[55] *See supra* note 16 and accompanying text.

Sidley misses the point in arguing that testimony about its screen was "unrefuted."[56] That testimony was irrelevant in the first place. Only an "appropriate" ethical screen rebuts the presumption of shared confidences "in the proper circumstances,"[57] which does *not* include a screen erected more than a year into the dual representation, long *after* confidences could have been shared.[58] Sidley only claimed to put a screen in place in November 4, 2019 (after Chubb called out the dual representation that had been ongoing since October 2018) and did not even inform Chubb of the screen, or its terms, until a month later.[59] Just as a bell cannot be unrung, a screen cannot be effective when it is not in place while a conflict is ongoing.[60]

These rules are logical because a client would be hard-pressed in many circumstances to adduce evidence that would refute a claim by a firm that no information had passed or confidences had been revealed, as Sidley claims

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[56] Br. at 35.

[57] *Apeldyn Corp. v. Samsung Elecs. Co.*, 693 F. Supp. 2d 399, 404 (D. Del. 2010); *see also EON Corp. IP Holdings LLC v. Flo TV Inc.*, No. CIV.A. 10-812-RGA, 2012 WL 4364244, at *1 (D. Del. Sept. 24, 2012).

[58] APP0803, Schwartz Decl. ¶ 15; APP0839–43, Schwartz Decl. Ex. 4.

[59] APP0839–43, Schwartz Decl. Ex. 4.

[60] *United States ex rel. Bahsen v. Bos. Sci. Neuromodulation Corp.*, 147 F. Supp. 3d 239, 249 (D.N.J. 2015) *see also Atasi Corp. v. Seagate Technology*, 847 F.2d 826, 831 (Fed. Cir. 1988) (holding that presumption of shared confidences was not overcome where there was no evidence that screening measures were taken at the time of disqualified attorney's move to the firm).

happened here.[61] It is precisely because such a self-serving assertion is difficult for an aggrieved client to verify that Rule 1.10(a) *presumes* that information has been shared when matters are substantially related. Nor does Rule 1.9 require any factual showing that one member of a law firm shared information with another member of a law firm.[62] Here, for example, since the leakage of Century/Chubb's confidences may not become apparent until later in this case when trust distribution procedures come out.

III. SIDLEY'S UNSUPPORTED AND IRRELEVANT FACTUAL ASSERTIONS DO NOT ALTER THE DISPOSITIVE FINDING BELOW THAT SIDLEY HAD A LIVE CONFLICT ON THE DATE OF RETENTION

On appeal Sidley places heavy emphasis on its assertion that Chubb purportedly knew about its representation of BSA as early as December 2018 and never objected. But the bankruptcy court held that Sidley "abandoned" this argument at the hearing.[63] And after considering all the testimony, the bankruptcy court found that Century/Chubb did *not* possess sufficient actual knowledge of the

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[61] Br. at 42–43.

[62] *See* Model R. Prof'l Conduct 1.9(a); *id*. cmt. [3] ("A conclusion about the possession of [confidential] information may be based on the nature of the services the lawyer provided the former client and information that would in ordinary practice be learned by a lawyer providing such services.").

[63] Ruling at 15.

conflict, nor did it fail to take timely action and thereby waive its objection to the retention.[64]

The record more than supports the bankruptcy court's conclusion: Mr. Sneed admitted that, when asked about the anonymous attribution in a *Wall Street Journal* article, he told Century/Chubb he could not comment on it but expressly assured Century/Chubb that Sidley was "conflict free."[65] Century/Chubb relied on this representation,[66] and Sidley did not raise its BSA representation in its subsequent prospective waiver discussions with Century/Chubb.[67] Ferreting out this conflict was not Century/Chubb's duty as the client. As this Court has put it, "it is incumbent upon law firms to iron out risks of conflicts before the risks mature into live controversies."[68]

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64 *Id.*

65 APP0784, Sneed Decl. ¶ 27.

66 Tr. at 191:14–22 (Schwartz testimony).

67 APP0802, Schwartz Decl. ¶ 11.

68 *Parallel Iron*, 2013 WL 789207, at *3. For the same reason, Sidley's account of the phone call between Mr. Sneed and Mr. Schwartz on page 11 of its brief is wholly misleading. There was nothing to "remind" Mr. Schwartz of because Mr. Sneed, by his own admission, never disclosed Sidley's representation of BSA to Mr. Schwartz. Tr. at 72:1–2 (Sneed testimony); Tr. at 191:16–19 (Schwartz testimony); APP0784, Sneed Decl. ¶ 27.

Likewise, Sidley's attempt to suggest that BSA hired Sidley before Chubb did is both contrary to the undisputed record and legally irrelevant.[69] It was undisputed that Chubb was a longtime client of Sidley's Insurance and Financial Services Group going back fifteen years.[70] At the time BSA hired Sidley, the record shows that Sidley was engaged on a matter that it started for Chubb in May 2017,[71] and that Sidley did not attempt to resign until 2020.[72] It remained an ongoing matter[73] and Sidley was Chubb's counsel on that matter up until Sidley's unilateral withdrawal in 2020.[74]

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[69] Sidley claims that Mr. Sneed "sought a new engagement letter" when Century/Chubb contacted him about the first BSA reinsurance matter in October 2018. Br. at 8. This is nowhere on the record. Rather, the record shows that Mr. Sneed asked for and received Sidley's still-effective Service Level Agreement ("SLA"), which Sidley had ***acknowledged in 2015***. Ruling at 2; APP0790–91, Sneed Decl. Ex. 1; Tr. at 59:3–4 (Sneed testimony). The SLA was sent more than a month into the engagement, and it was not until two weeks later that Mr. Sneed raised anything about a prospective waiver. APP0790–91, Sneed Decl. Ex. 1. In that same series of emails, he acknowledged that "we [Sidley] represented ACE Companies for years pursuant to the ACE SLA." *Id.*

[70] Tr. at 136:22–12 (Russell testimony); APP0799, Schwartz Decl. ¶ 2; Sneed Decl. ¶ 9; *id.* Ex. 1; Ruling at 1.

[71] APP0778, Sneed Decl. ¶ 9; APP0801, Schwartz Decl. ¶ 8.

[72] APP0853–56, Schwartz Decl. Ex. 8; APP0786–787, APP1231–33, Sneed Decl. ¶ 37, Ex. 13.

[73] APP1029, Tr. at 139:1–10 (Russell Testimony).

[74] *Id.*; APP0853–56, Schwartz Decl. Ex. 8.

Sidley also misrepresents the terms of the parties' Service Level Agreement ("SLA").[75] That Chubb refers to its reinsurance as "non-claims" that are "unrelated to the defense of an insurance claim" in the SLA does not alter the information to which Sidley was privy. Also, that is not language that defines the scope of a lawyer's engagement, as the SLA expressly states that "[n]otwithstanding" that the "SLA pertains to Non-Claims Services, … [it] ***should not be taken as any form of instruction to limit your role*** or to reduce the quality of the representation provided."[76]

Finally, Sidley reiterates the bankruptcy court's claim that BSA would be severely prejudice should Sidley be required to exit. But this issue was legally irrelevant to the issues before the bankruptcy court in this retention application under Section 327, where actual conflicts are per se disqualifying and Sidley carried the burden to prove that it did not hold any conflicts.[77] In any case, Morris, Nichols, Arsht & Tunnel, which has been involved in this matter since at least the petition date as "BSA's Delaware-based bankruptcy co-counsel," has its own

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[75] Br. at 43.

[76] APP001240 (emphasis added).

[77] *In re Pillowtex*, 304 F.3d at 251.

dedicated, top-tier restructuring team at BSA's disposal.[78] Sidley and BSA offered nothing to explain why it could not seamlessly assume Sidley's role.

CONCLUSION

For the foregoing reasons, the order appointing Sidley as BSA's counsel in the bankruptcy proceeding should be reversed.

[78] Br. at 24.

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Respectfully Submitted,

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CERTIFICATE OF COMPLIANCE

Pursuant to Federal Rule of Bankruptcy Procedure 8015(h), the undersigned certifies that the above memorandum complies with the applicable type-volume limitation of Federal Rule of Bankruptcy Procedure 8015(a)(7)(B)(i) because, excluding the parts of the memorandum exempted by Federal Rule of Bankruptcy Procedure 8015(g), this brief contains 6378 words. The above brief also complies with the typeface requirements of Federal Rule of Bankruptcy Procedure 8015(a)(5) and type-style requirements of Federal Rule of Bankruptcy Procedure 8015(a)(6).

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