CLERK, U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS

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THE DATE OF ENTRY IS ON
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The following constitutes the ruling of the court and has the force and effect therein described.

Signed November 4, 2016

United States Bankruptcy Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
FORT WORTH DIVISION

In re:	§	
	§	Jointly Administered Under
LIFE PARTNERS HOLDINGS, INC.,	§	CASE NO. 15-40289-RFN-11
et al.,	§	
	§	
Debtors.	§	
	§	
	§	
Steve South, as Trustee for, and on behalf	§	Adversary No. 15-4061
of the South Living Trust, Philip M. Garner,	§	(Consolidated with
Michael Arnold, Janet Arnold, John S.	§	Adversary No. 15-4064)
Ferris, M.D., Christine Duncan, and all	§	
others similarly situated,	§	
	§	
Plaintiffs,	§	District Court Case
	§	No. 4:16-CV-212-A
v.	§	
	§	
Life Partners, Inc.,	§	
	§	
Defendant.	§	

REPORT AND RECOMMENDATION
<u>ON THE PARTIES' AGREED MOTION FOR ATTORNEYS' FEES</u>

TO THE HONORABLE JOHN H. McBRYDE, UNITED STATES DISTRICT JUDGE:

I. Introduction

Your Honor has referred the Parties' Agreed Motion for Attorneys' Fees to me for a report and recommendation. In the motion the lead plaintiffs in this class action ask You to approve an award of attorneys' fees in the amount of $33 million for class counsel.

Nine parties have objected to the motion. Most prominent among the objectors are the Arbitration Objectors. Because most of the other objections duplicate the arguments of the Arbitration Objectors, I respond chiefly to their arguments. I find the Arbitration Objectors' arguments persuasive in two respects. First, I agree that it is more defensible to view class counsel's fees as a substantial contribution claim under section 503(b)(4) of the Bankruptcy Code than as fees to be awarded for the creation of a common fund. Second, because section 503(b)(4) is directed at post-petition contributions instead of pre-petition services, I agree that some adjustment of the fee request is warranted. I recommend that the fee be set at $25 million. Because this fee will be paid over a period of many years, its present value is approximately $3.9 million. This amount is fair and reasonable and, as such, properly compensates class counsel for its substantial contributions. I recommend that the Court grant the motion in that amount for the reasons stated herein and that it deny all other objections.

II. The Court Should Grant in Part and Deny in Part The Objections of the Arbitration Objectors

A. Class Counsel Played a Unique and Substantial Role in the Bankruptcy Case

Two themes are central to the Arbitration Objectors' objections to class counsel's request for fees. First, the Arbitration Objectors insist that class counsel's efforts have added little, if anything, to the resolution of this case. Second, they argue that to the extent that counsel's contributions are compensable at all, a combination of happenstance and legal technicalities

preclude any compensation, or at least any meaningful compensation. In order to address these themes it is necessary to evaluate class counsel's role and its contributions in the context of the entire bankruptcy case, not just the class action.

Prior to its petition in bankruptcy, LPI was in the business of selling fractionalized interests in life insurance policies. In December 2014 Judge John Nowlin, U. S. District Judge for the Western District of Texas, entered a $38 million judgment in favor of the SEC against LPHI, LPI's parent, for misleading shareholders about LPI's business practices. Although LPI's management tried to spin the meaning of that judgment to its investors, its premise was simple: LPI had fraudulently induced investors to purchase fractional interests by using artificially low life expectancies issued by Dr. Donald T. Cassidy.

The use of phony life expectancies had at least two pecuniary effects. First, it caused fractional interest investors to pay more for their investments because they thought that the policies would mature (that is, the insureds would die) sooner rather than later. Second, because part of the purchase price included an escrow for premiums up to the projected maturity date, artificially low life expectancies led to artificially low premium escrows. After a particular escrow had been exhausted, the investor was thereafter responsible for his share of premiums until the date of maturity. LPI's business model allowed it to buy low (from insureds) and sell high (to fractional interest holders). LPI used the arbitrage to sustain its business operations, to handsomely compensate LPI's management (particularly its president, Brian Pardo) and to pay dividends at the LPHI level (most of which went to Pardo and his family).

Once LPI could no longer sell fractional interests based on low-ball life expectancies, its arbitrage was reduced significantly due to lower sales and the need to allocate more of the sales proceeds to realistic premium escrows. This reduction in cash meant that there was less money to

sustain LPI's business operations, most notably its servicing platform. To compound LPI's financial stress, Pardo continued to insist on generous compensation for himself and others in management and on paying dividends to shareholders of LPHI. So dire was LPI's financial condition that in September 2014 it instituted for the first time a servicing fee. Thousands of investors were outraged. Not only were they paying premiums on policies that had long exceeded Cassidy's life expectancies, but now they were being called upon to pay a fee that had never been disclosed to them. Some paid, some did not, and many sued.

In the face of these difficulties, LPI's management stood firm. At the same time that management was informing fractional interest holders that they must bear the burden of servicing going forward, its board ordered that LPI's last remaining $400,000 in cash be paid as dividends to shareholders of LPHI.

By January 2015 LPI was insolvent, both in terms of its operations and its balance sheet. Its known assets consisted of a small amount of cash and a wooly mammoth collection. Its income was not sufficient to sustain the servicing platform. Moreover, LPI was incurring significant legal expenses, not only in defending the SEC action, but in defending securities suits, fraud suits, and suits disputing the servicing fee. The SEC was pressing Judge Nowlin for a receiver for LPHI.

Pardo responded to this crisis by placing LPHI in bankruptcy on January 20, 2015. Shortly thereafter I appointed Thomas Moran as chapter 11 trustee. Moran then placed LPI into bankruptcy.[1] The filing of bankruptcy on behalf of LPI introduced the most controversial and complicated question in this case: "Who owns the policies?" It is safe to say that almost all

[1] For doing so, Moran has endured the unrelenting wrath of many investors who contend that LPI's bankruptcy was contrived for the purpose of permitting Moran and all professionals in the bankruptcy case to act as pigs feeding at the trough and thus perpetrate a fraud that far exceeds any of Pardo's misdeeds. This is false equivalence at its zenith. But, the myth persists and in part explains the harsh light in which many investors hold the professionals, including class counsel.

investors in fractional interests thought they were buying, directly or indirectly, interests in the policies themselves. As such, they considered themselves to be the owners of the policies. But, the legal owner of the policies was LPI. And, LPI was the named beneficiary of every policy in the portfolio.

As the head of an operationally insolvent debtor, Moran took the logical position that the policies belonged to the estate and, as such, their cash surrender values could be used to sustain the servicing platform, pay professional fees, and advance premiums on policies where one or more fractional interest holders had defaulted.

The reaction to Moran's proposal to use cash surrender values was swift and harsh. At a hotly contested hearing on Moran's motion, one investor after another stepped to the podium to insist that cash surrender values belonged to the investors and that the trustee could not use or borrow them without their consent, which they refused to give. They persuasively argued that the use of cash surrender values was the first and perhaps an irreversible step towards pooling the policies, a result that they fervently opposed. Although the trustee had a pressing need for cash, I agreed with the investors. I ruled that the trustee could not use cash surrender values unless I determined that LPI owned the policies.

Shortly after my ruling, three groups of parties filed separate adversary proceedings to resolve the ownership issue. One such group consisted of the plaintiffs in this case. Those plaintiffs were represented by the class counsel who is the movant before Your Honor. Class counsel had a long history with LPI. In 2011, well before LPI filed for bankruptcy, class counsel sued LPI on behalf of certain plaintiffs who claimed that LPI was selling securities in violation of the Texas Securities Act. *Arnold v. Life Partners, Inc.*, Case No. DC-11-02995 (Tex. Dist. Ct. 14th Dist. – Dallas). The claim itself was risky. In 1996 the United States Court of Appeals for

the District of Columbia had ruled that viatical settlements were not securities. *SEC v. Life Partners, Inc.*, 87 F.3d 536, 545-48 (D.C. Cir. 1996). In 2004 a Texas court of appeals reached the same result. *Griffitts v. Life Partners, Inc.*, 2004 Tex. App. LEXIS 4844 (Tex. App. – Waco, May 26, 2004, no pet.). So seemingly settled was the notion that life settlements were not securities that the state trial court presiding over the Arnold claims dismissed them and ordered that class counsel be sanctioned for bringing them. *Arnold v. Life Partners, Inc.*, 2011 WL 7144985 (Tex. Dist. Ct. 14th Dist. – Dallas). But, in 2013 the plaintiffs' fortunes changed. The Dallas Court of Appeals ruled for the first time that life settlements were securities. *Arnold v. Life Partners, Inc.*, 416 S.W.3d 577 (Tex. Civ. App. 5th Dist. – Dallas (2013)). That holding was affirmed by the Texas Supreme Court in 2015. *Life Partners, Inc. v. Arnold*, 464 S.W.3d 660, 684 (Tex. 2015).

It is important to pause here to emphasize an obvious, but important, point. The Arbitration Objectors make much of the fact that the bulk of class counsel's time was devoted to seeking recourse for violations of Texas securities laws, not to the ownership issue. That is true. But, prior to LPI's petition in bankruptcy, ownership was not an issue at all.

"Ownership" is a buzzword for what were in fact many issues. For example, what are the legal consequences of "owning" a fractional interest in a life insurance policy? For a purchaser who had invested through an IRA (which a majority of LPI investors did) did "ownership" mean they had invested in a life insurance product, thus subjecting the investment as well as the entire IRA to immediate taxation? Did "owning" a fractional interest bestow upon the owner the right to direct servicing of his interest to a particular servicer, or were servicing rights severable and controlled solely by LPI?

The legal questions raised by the ownership issue went hand-in-hand with two practical problems. First, until the time the ownership issue was resolved, how would the value of the portfolio be preserved? In order for fractional interests to have any value, someone had to collect premiums, send premiums to carriers, monitor policy maturities, file claims on matured policies, and collect and distribute policy proceeds. In the absence of capital to sustain the servicing platform, who would perform these vital functions?

Just as importantly, how would the debtor manage policy defaults? Prior to LPI's bankruptcy, when a fractional interest holder failed to pay his portion of the policy premium, his interest was defaulted and sold by LPI, with the proceeds used to cure the default. But, because the Texas Supreme Court ruled in *Arnold* that fractional interests were securities and could only be sold in compliance with the Texas Securities Act, that source of revenue was gone. In the absence of capital to cure defaults, even one defaulted position placed an entire policy at risk of termination.

And, speaking of capital, the very pendency of the ownership issue placed the capital markets beyond LPI's reach. Lenders — conventional or otherwise — look to loan against known assets. Until the ownership issue was resolved, LPI had a mere claim of ownership to the policies and nothing more.

These problems and many others led several constituencies in the bankruptcy case to a simple and inescapable conclusion — litigation was a zero-sum game. Those parties grasped the reality that the delay occasioned by litigation could significantly harm if not destroy the value of the portfolio. And, those who claimed to be owners came to realize that even a declaration to that effect did not solve the problems relating to servicing and defaulted positions. Only a comprehensive solution could save LPI's portfolio and protect its investors. Class counsel, along

with the trustee, the unsecured creditors' committee, other investors, and their respective professionals stepped forward to provide that solution.

In September 2015 several parties entered into a term sheet that was to be the template for a settlement that would resolve the ownership issue. Not only did the term sheet represent the first step toward the resolution of the ownership issue but it provided for LPI's access to a $25 million DIP loan from policy maturities. The DIP loan was essential to LPI's survival for the next 11 months of the case.

Achieving an agreement that substantively resolved the ownership issue was only part of the puzzle. Just as critical was implementing a procedure to approve that agreement and make it binding. The only procedural vehicle that could resolve the ownership issue was an adversary proceeding. Rule 7001 is clear on this point. It says that "a proceeding to determine the validity, priority, or extent of . . . [an] interest in property" is an adversary proceeding. Fed. R. Bankr. P. 7001(2). *See also In re Eastman Kodak Co.*, 2012 Bankr. LEXIS 2746 at *6 (Bankr. S.D.N.Y. 2012) ("Since the relief Kodak seeks is, for all intents and purposes, an action for a declaratory judgment to determine an interest in property . . . the plain meaning of Rule 7001 indicates that it must be brought as an adversary proceeding, not as a contested Rule 9014 motion."); *In re Hearthside Baking Co., Inc.*, 397 B.R. 899, 902 (Bankr. N.D. Ill. 2008) (determination of whether an insurance policy was property of the estate required an adversary proceeding). So, even though the Arbitration Objectors intimate otherwise, resolution of the ownership issue could only have occurred in the context of an adversary proceeding.

A logical corollary to this conclusion is the notion that a plan of reorganization, by itself, could not effect this relief. And, to the extent that a plan proponent attempted to resolve these issues through a plan alone, any such plan would have had no preclusive effect on those issues that

should have been raised in an adversary proceeding. *SLW Cap., LLC v. Mansaray-Ruffin (In re Mansaray-Ruffin)*, 530 F.3d 230, 242 (3d. Cir. 2008).

The problem of preclusion was particularly acute in this case. More than 21,000 investors held fractional interests in 3,400 policies. In total, more than 90,000 positions were purchased. Investors not only differed with respect to their understandings of the nature of the interests they had purchased, but also with respect to the level and type of information they relied on when they bought their interests. Some executed operative documents; others did not. And to the extent that investors signed documents, not all operative documents were the same.

Although three groups filed adversary proceedings to resolve ownership, they differed in their approaches. Your Honor is familiar with the adversary proceeding brought by Pillar. Pillar sought to determine only its own ownership rights, not those of others. Indeed, Pillar fought class certification and the approval of the class action settlement because it insisted upon an individualized determination of ownership as to itself.

KLI also filed an adversary proceeding to decide ownership. That adversary proceeding was met with 110 motions to intervene until I ordered that it be abated. Questions immediately arose as to the logistics of managing such an adversary proceeding. Those questions started with service and notice issues and ended with questions of when, where and how to try a case with more than 110 parties, most of whom shared similar legal concerns but relied upon more than 110 different sets of facts. And, of course, at the conclusion of that adversary proceeding, only those who actually participated would be bound. The court's ruling might have been instructive, but not binding on more than 20,000 other investors.

Class counsel correctly judged that only a class action could provide a workable procedural framework for resolving the ownership issue. Class counsel negotiated the final settlement

agreement with LPI and the committee, procured my approval of the settlement, procured class certification from Your Honor, procured Your approval of the class action settlement, and then helped procure confirmation of the plan that incorporated the class action settlement. So, while it is true that others were pursuing the ownership issue in one way or another, only the class counsel stepped forward to provide both a substantive resolution and a procedural framework that offered any hope of finality.

B. The Common Fund Doctrine Does Not Appear to be the Appropriate Theory for Fee Recovery

Class counsel seeks fees pursuant to the common fund doctrine. That doctrine "provides that a private plaintiff, or plaintiff's attorney, whose efforts create, discover, increase or preserve a fund to which others also have a claim, is entitled to recover from the fund the costs of his litigation including attorney's fees." *In re High Sulphur Content Gasoline Prods. Liab. Litig.*, 517 F.3d 220, 228 n. 10 (5th Cir. 2008) (citation omitted). Because the common fund doctrine is an equitable and flexible doctrine intended to avoid unjustly enriching parties who benefit from the settlement without contributing to it, it is not limited to lump sum awards. *Boeing Co. v. Van Gemert*, 444 U.S. 472, 478 (1980).

Here, class counsel calculates the common fund in several ways. First, class counsel places the value of the common fund at $1.28 billion. This represents the amount of claims entitled to rescission as a result of class counsel's efforts in the *Arnold* state court action. But, this figure cannot form the benchmark for the value of the common fund. This amount represents the total amount of rescission *claims*, not a fund or stream of payments earmarked to pay rescission claims. Indeed, under the settlement, rescission claims are to be paid from the Creditors' Trust, a litigation trust whose ultimate return is uncertain. What is certain is that the Creditors' Trust will not pay $1.28 billion.

Next, class counsel values the settlement result at $1.078 billion. This amount represents the present value of the stream of payments that will be paid to class members pursuant to the settlement. Using this approach, class counsel's proposed fee of $33 million would be approximately 3% of the common fund.

I have a conceptual difficulty with this approach. First, it values the stream of *all* payments to class members throughout the life of the portfolio. In doing so, the approach aggregates the stream of payments on two different forms of relief under the plan. One form of relief is the option to remain a continuing interest holder. Under that option, a continuing interest holder is considered to be the beneficial owner of his fractional interests. A continuing interest holder is required to pay his own proportionate premiums going forward, contribute 5% of his beneficial interest to the Position Holder Trust, and pay a servicing fee of 2.65% upon the maturity of the policy.

There are several aspects of continuing interest holder treatment that do not neatly fit the paradigm of a common fund. First, except as to the 5% contribution to the Position Holder Trust, the continuing interest holder does not "pool" his interests. He retains his interest to the exclusion of all others. It is difficult to view individually retained interests as a "common fund." Second, although the plan gives the continuing interest holder an interest in the Position Holder Trust to the extent of his 5% contribution, that contribution represents a concession by the continuing interest holder, not a concession by LPI. Given these nuances, it is difficult to view revenue streams attributable to continuing interests as a common fund.

But, the plan did create a vehicle that could be described as a common fund: the Position Holder Trust. The Position Holder Trust certainly bears many of the hallmarks of a common fund. Under the Position Holder Trust option, fractional interest holders contribute their interests to the trust for a proportionate interest in the returns from the trust. The chief benefit of this option is

that interest holders are no longer responsible for paying policy premiums. This is no small matter because many investors faced crippling premium obligations and, under Pardo's system, defaults on premiums would have resulted in forfeiture of the interests altogether.

Class counsel has not attempted to place a value on the income stream attributable to the Position Holder Trust. For the sake of analysis, I will assume its value is half of the total value of the stream of payments generated by all policies in the portfolio, say $500 million. But even doing so, I confront another conceptual challenge. While the Position Holder Trust is a laudable option for thousands of fractional interest holders, the result is not necessarily different from the one investors would have achieved had LPI prevailed on the ownership issue.

Perhaps in response to this concern, class counsel posits the "nominal value" approach. Under this approach, class counsel assumes that if LPI had prevailed on ownership, it would have sold the entire portfolio and distributed that liquidation value to investors. Under this assumption, the alleged benefit to investors from the settlement would be $578 million. To reach this result, class counsel takes total class benefits, $1.078 billion, and deducts a liquidation value of $500 million. But the fundamental premise of this approach—that LPI would have sold the policies—is speculative.

Had LPI prevailed on the ownership issue, all fractional interests would have been pooled. The most immediate effect of this pooling would have been that LPI would have had substantial cash in the form of policy maturities and cash surrender values. That cash would have been available to fund the servicing platform and cover premiums. Under those circumstances, there would have been no need, much less urgency, for LPI to sell the portfolio. Instead, LPI could have proposed a plan that provided for a proportionate payment of investors' claims over time.

While it is certainly possible that LPI could have sought to sell the portfolio pursuant to section 363, Moran never demonstrated any such inclination in the bankruptcy case. But, more importantly, I highly doubt that I would have approved such a sale over the objections of investors if it could have been shown—which it was at confirmation—that the portfolio would generate a positive cash flow. And, I am certain that the objections to any such sale would have been numerous and strenuous.

So, how does this analysis affect class counsel's reliance upon the Position Holder Trust as a common fund? It boils down to this: pooling of interests (which is what the Position Holder Trust is) was a worst-case scenario for ownership claimants. It was the very treatment they would get if they lost, not if they won.

C. Class Counsel Should be Awarded Fees For Its Substantial Contribution to the Case

I respectfully submit that the proper procedural framework within which to analyze class counsel's request for fees is section 503(b)(4) of the Bankruptcy Code. In this respect I agree with the Arbitration Objectors. But, I disagree with the Arbitration Objectors when they argue that class counsel made no substantial contribution.

The first question that I confront when I consider substantial contribution is whether I should recommend that the parties supplement the record and their briefing on this issue. After all, while the Arbitration Objectors have addressed substantial contribution, class counsel has not except to say that it does not apply and that it is not pursuing such a claim. After reviewing the record on the current motion and bringing to bear my own observations in the underlying bankruptcy case, I believe it is appropriate to address the issue now. After all, both parties will have the opportunity to respond to this report.

The authority for class counsel's substantial contribution claim starts with 11 U.S.C. § 503(b)(3). Under that section, a court can authorize an administrative expense for "the actual, necessary expenses, other than compensation and reimbursement specified in paragraph (4) of this subsection, incurred by . . . a creditor . . . in making a substantial contribution in a case under chapter 9 or 11 of this title." 11 U.S.C § 503(b)(3)(D). The court can then, in turn, authorize an administrative expense for "reasonable compensation" for services rendered by an attorney for a party who is entitled to a substantial contribution claim under section 503(b)(3). 11 U.S.C. § 503(b)(4).

A "substantial contribution" is a contribution that is "considerable in amount, value or worth." *Hall Fin. Group, Inc. v. DP Partners, Ltd. P'ship (In re DP Partners Ltd. P'ship)*, 106 F.3d 667, 673 (5th Cir. 1997). Services that make a substantial contribution are "those which foster and enhance, rather than retard or interrupt the progress of reorganization." *Id.* at 672. While determination of substantial contribution is made on a case-by-case basis, the court should "weigh the cost of the claimed fees and expenses against the benefits conferred upon the estate which flow directly from those actions." *Id.* When it comes to such fees, Your Honor has "broad equitable — and hence discretionary — powers to award attorney's fees." *Smith v. Mirant Corp. (In re Mirant)*, 308 Fed. Appx. 824, 828 (5th Cir. 2009) (citations omitted). Finally, "while some actions may result in 'benefit[s] that often can be measured by the actual cost of necessary goods or services supplied,' there may be 'less readily calculable benefits' conferred to the estate, 'such as the ability to conduct business as usual.'" *Bodin Concrete, LP v. Concrete Opp. Fund II, LLC (In re Bodin Concrete LP)*, 616 Fed. Appx. 738, 742 (5th Cir. 2015). So, the benefit to the estate need not be reduced to, or expressible in, monetary terms. *In re American Plumbing & Mech., Inc.*, 327 B.R. 273, 281 (Bankr. W.D. Tex. 2005).

This is a case in which class counsel's contribution cannot necessarily be reduced to or expressed in monetary terms. Here, no monolithic set of facts, understandings, expectations, or desires led to a simple resolution of the ownership issue. For example, while many investors felt they had been defrauded by LPI, others felt they were fully informed and knowingly assumed the risks attendant to fractional ownership. Almost all investors went into the case wanting to preserve their individual ownership rights. But, after learning of the real risks and costs associated with fractional ownership, many investors opted to pool their interests. As the case progressed it became clear that what investors truly desired were options based upon individual personal circumstances.

Class counsel helped make those options available. Under the class action settlement, non-IRA investors were given the following options: (1) to remain continuing interest holders and retain 95% of the economic benefit of their fractional interests, subject to continuing premium obligations and a 2.65% servicing fee; (2) to contribute their fractional interests to the Position Holder Trust, with ongoing premium and servicing obligations to be borne by the trust; or (3) to rescind their investment in exchange for an interest in the Creditors' Trust. IRA investors (who comprised a majority of fractional interest holders) were given the following options: (1) to receive a fixed, tax-compliant note representing 32% of maturities attributable to their fractional interests; (2) to hold interests in a partnership with a pool of fractional interests; (3) to rescind their investment in exchange for an interest in the Creditors' Trust; or (4) to elect non-IRA status and opt to become continuing interest holders. Non-voting investors would be placed in the Position Holder Trust.

Class counsel has presented evidence that the present value of the income from these various options is $1.078 billion. While I have difficulty characterizing that income stream as a

common fund, I have no difficulty in reporting that the value contributed by class counsel in making these options available is both real and substantial. Any one of these options standing alone would have been unsatisfactory. This was simply not a "one-size-fits-all" case. This case demanded creativity in crafting a solution that would accommodate the diverse desires and financial capabilities of thousands of investors. The intangible value of those choices cannot be minimized.

Class counsel next contributed to the case by devising a remedy for creditors who were victims of LPI's sharp practices, but were no longer fractional interest holders. These creditors were given claims against the Creditors' Trust, a litigation trust with $12 million in capital to pursue claims against third parties.

Next, as part and parcel of a September 2015 term sheet, class counsel helped pave the way to a $25 million DIP facility that would fund LPI's operations for the next 11 months. This facility was critical to LPI's survival until it could procure its only DIP loan from an outside source (plan co-proponent Vida) in August 2016.

Next, it was not sufficient merely to craft a set of options that would solve ownership as a substantive matter. As I have noted, simply incorporating those options into a plan would not have sufficed because while investors can affirmatively agree to have their disputes resolved in the plan, many investors would not vote at all or would vote against the plan. Because these investors were entitled to have their disputes resolved in an adversary proceeding, their rights could not be compromised simply by having other investors out-vote them. And, leaving ownership unresolved as to dissident or non-voting investors was no solution either. After all, dissident and non-voting investors had to bear their share of premiums and servicing in order to preserve the value of the portfolio for all investors.

Class counsel realized that only class certification and a class action could solve this problem. It alone stepped forward to provide this essential ingredient to the plan process. This contribution – the provision of a binding procedural framework – is solely attributable to class counsel.

The contributions of a substantive resolution and a binding procedural framework produced consequential benefits. Once those elements were in place, other suitors were presented with a template for competing plans. Vida Corporation was the first competitor to grasp the importance of the settlement. It filed a competing plan incorporating the settlement. Later, it joined the debtor and became a co-proponent of the debtor's plan.

The class action settlement also led to a competing plan by Transparency Alliance, albeit reluctantly. Transparency believed that it could propose a workable plan without a class action settlement. I ruled otherwise, and Transparency ultimately adopted the class action settlement.[2]

During confirmation, other suitors came forward to express interest in LPI. They submitted informal offers. Those offers prompted Vida to lower its cost of servicing and lending, thus bestowing additional benefits upon the estate. This spirited competition would not have taken place without the groundwork laid by class counsel.

So, how does one place a value on services whose benefit cannot be precisely expressed in dollars and cents? I start with the agreement of the parties themselves. Those parties – Moran (on behalf of LPI and LPHI) and the creditors committee – placed the value of class counsel's services at $33 million, or approximately 3% of the $1.078 billion revenue stream. Because these parties

[2] Transparency eventually withdrew its plan after solicitation when creditors expressed a preference for the LPI/Vida plan.

litigated against and then worked with class counsel on these matters, I find their evaluations to be persuasive. But the parties have agreed that Your Honor is not bound by that agreement.

I respectfully recommend that the fee be adjusted downward by $8 million, or approximately 25%. This would result in an award of $25 million, which as I understand it, would have a present value of approximately $3.9 million.

There are several factors that lead to this proposed adjustment. First, when Moran and the committee agreed to the $33 million figure, they, like class counsel, viewed the recovery as a common fund. As such, they might reasonably have viewed the class action settlement as the culmination of the *Arnold* class action that was begun in 2011. Viewed as such, $33 million might seem imminently reasonable.

But, because I do not believe that this case fits the common fund paradigm — even with some equitable massaging — I believe the emphasis should be on class counsel's work and contributions post-petition. As I noted above, those contributions are considerable.

Moreover, I do not agree with the Arbitration Objectors that class counsel's pre-petition work is irrelevant. On the contrary, I believe that class counsel's pre-petition efforts caused it to be well-versed in LPI's operations, its methods of doing business, the injuries sustained by interest holders, and the nuances pertaining to various classes of investors. This formative grounding not only provided class counsel with insight into how to resolve the ownership issue, but led it to the conviction that only a class action could bring about a binding result. So, the Arbitration Objectors are wrong to say that class counsel's pre-petition efforts have no bearing. Class counsel's ability to achieve the result that it did is due in no small part to the knowledge and experience that it brought to the table when LPI filed for bankruptcy.

Still, when LPI filed for bankruptcy, the tenor of all claims against LPI changed. While litigants may previously have focused on fraud, the Texas Securities Act, servicing fees or the like, the focus now was on ownership, an issue that simply had not existed before. It was class counsel's efforts in resolving that issue, not rescission claims, that contributed the greatest value to the case. Not only were those efforts performed post-petition, but they do not stand alone when it comes to credit for the final outcome. The superior benefits that I identified could not have been achieved without the collaboration of Moran, the committee, and their counsel.

In making this recommendation, I have also considered the fact that except for servicing fees, the interests to be awarded to class counsel are burden-free. Under the settlement, class counsel is to receive a certain proportion of abandoned policy positions calculated to generate a $33 million return. But, the premiums to keep these interests in effect will be paid from the Position Holder Trust. Those premiums are projected to be $13.6 million. Because of this the Arbitration Objectors place the true value of the proposed fee at $46.6 million. Class counsel says this is irrelevant because the agreement called for a fee of $33 million net of expenses.

Either argument is defensible depending on one's perspective. My observation is that the feature of having premiums advanced on class counsel's interests is unique. Continuing interest holders pay their own premiums. Those who participate in the Position Holder Trust are subject to reduced distributions due to premiums paid by the trust. Viewed one way, an $8 million adjustment would result in class counsel bearing $8 million of the $13.6 million in premiums necessary to sustain a $33 million income stream. That does not seem unreasonable.

D. *Johnson* Cross-check Supports Class Counsel's Fees

As a cross-check to the reasonableness of the recommended fee I address the factors set forth in *Johnson v. Georgia. Highway Express, Inc.*, 488 F.2d 714 (5th Cir. 1974).

1. Time and Labor Required

As of the date of its application, class counsel had devoted 5,600 hours to this matter. Most of these hours were devoted to services performed by class counsel prior to LPI's petition in bankruptcy. Because I believe emphasis should be placed on the value of class counsel's contributions to the bankruptcy estate, I believe that a lodestar analysis is only minimally instructive. Still, I recommend that in order to permit a full review of its post-petition services, class counsel should supplement the record before Your Honor to provide a summary of all post-petition services thus far.

In this regard, I note that since class counsel filed the motion for fees, it has attended the contested confirmation hearing, which spanned five weeks. Of course, court attendance during that time was merely the tip of the iceberg. I have no doubt that class counsel devoted substantial additional time to confirmation issues. It also will devote additional time responding to the appeal of Your order granting class certification and approving the class action settlement. And, of course, it likely will be called upon to respond to an appeal of any award of fees by Your Honor. Finally, it is likely that class counsel will be called upon to assist in responding to an appeal of my order confirming the plan. So, not only have the demands on counsel's time been exhaustive, they will continue to be so.

2. Novelty and Difficulty of the Issues

For the reasons I have outlined above, it is clear that the issues in this case were both novel and difficult. LPI stands alone when it comes to the uniqueness, size and complexity of issues addressed by class counsel.

3. The Amount Involved and Results Achieved

I have addressed these factors above. Still, it bears repeating that the results obtained in this case were superior, both in terms of creativity and ultimate return to investors.

4. Skill Required

This case demanded a high degree of skill on the part of all professionals. Class counsel demonstrated that skill. The skill that class counsel brought to bear was due in no small part to its pre-petition work in the *Arnold* litigation. That experience bolstered the quality and efficiency of the work performed by class counsel.

5. Preclusion of Other Employment

Class counsel represents that it has been precluded from accepting other matters as a result of this. Given my own experience in this case, I find this representation to be highly credible.

6. Whether the Fee Is Fixed or Contingent

Class counsel has requested a percentage fee. It is true that a percentage fee will result in class counsel being awarded compensation that is greater than if its compensation were calculated on a lodestar basis. Such compensation is justified. Had the class representatives approached me when this case was commenced—which as creditors they were not required to do—and asked for authority to retain class counsel on a 2.5% contingency fee basis, I could and would have agreed to it. *See Holston Asset Mgt., LLC v. American Media, Inc. (In re Anderson News, LLC)*, 2013 U. S. Dist. LEXIS 174895 at *9 (D. Del. 2013).

Contrary to the Arbitration Objectors, I regard limiting class counsel to lodestar compensation as not only heedless of the significance of its contributions but of the risks it took in making those contributions. I find it significant that: (1) no other lawyer was willing to act as class counsel in this case; (2) class counsel undertook the representation with no assurance of any

payment at all; (3) even though class counsel has sought to vindicate the rights of LPI investors for five years, it has yet to be compensated at all; and (4) class counsel has agreed to be compensated from a revenue stream that may last for 30 years. This last factor is significant in two ways. First, it means that the payment of class counsel's fee is subject to risk and uncertainty and may never result in counsel's receipt of $25 million real dollars. Second, class counsel's agreement to accept payment of an administrative expense claim over time significantly reduces the financial burden on the reorganized debtor, who otherwise would be required to pay the current value of this stream of payments, $3.9 million, on the effective date of the plan.

7. The Undesirability of the Case

I need not dwell long on this factor. Although the Arbitration Objectors argue that anyone could have done what class counsel did, the fact is that no one else did. And, there is good reason for that. In August 2015 few lawyers would have taken on the role as class counsel. At that time, there was no assurance that there was "any there, there." Class counsel demonstrated great courage and commitment by taking on this challenge.

8. The Customary Fee

Although class counsel has submitted considerable evidence to demonstrate that its requested fee falls within the range of fees awarded for similar work, the fact is that there is no other case like LPI. As I have noted, class counsel's most valuable contribution was the basket of options presented to investors. And, although it is difficult to place a value on one option or another, each had real value. For example, the Position Holder Trust had no value to an investor who wanted to continue to own his interests. And, the option to continue to own one's fractional

interests had no value to an investor who could not afford the premiums. The fact that no customary fee applies to these types of options does not belie their value to real people.[3]

III. The Court Should Grant in Part and Deny in Part the Objections of Other Parties

Janet Davis, Joseph Zeuch, Charlene and Richard Sevcik, Mary and Eric Mattingly, Kamlesh Shingari, Elyse Bailey, Howard Carr, and Steven Hufstetler also filed objections to class counsel's request for fees. For the most part these objections duplicate some of those lodged by the Arbitration Objectors: that the fees are excessive, that class counsel did not contribute to the resolution of the case, and class counsel should not be compensated for pre-petition services. I recommend that Your Honor grant the objections to the extent that they go to any fee in excess of $25 million, but that You otherwise deny them.

Steven Hufstetler raises a unique objection that deserves a specific response. Hufstetler argues that class counsel should not be compensated at all because it actually injured investors of LPI by procuring a ruling from the Texas Supreme Court that life settlements are securities under the Texas Securities Act. Hufstetler observes that this ruling impaired the free transferability of LPI's life settlements. One of the consequences of this decision was that defaulted interests no longer could be sold to new investors in order to cover premium defaults. According to Hufstetler, this injured those investors who did pay premiums and counted on the resales to cover defaulted positions. Hufstetler's observations are accurate, and many investors agree with him. But, Hufstetler's complaint must be recognized for what it is — an endorsement of the Pardo system.

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[3] My conclusion that class counsel's fee should be evaluated as a substantial contribution claim obviates the need for me to address the Arbitration Objector's other objections including: that class counsel's fees are not permitted under section 506(b); that common fund fees may not be awarded in bankruptcy cases; and that the allowance of class counsel's fees is governed by state law. I respectfully recommend that Your Honor deny these objections.

Many investors, but not all, were misled about fractional interests. Others, but not all, were simply misinformed. Many misled or misinformed investors lost their investments when they could no longer pay premiums. Under the Pardo system, the interests of those unfortunate investors were simply sold to other investors, some of whom may have been similarly misled or misinformed. Hufstetler's complaint is that this system should have been allowed to persist for the benefit of those who could afford their premiums. But, Hufstetler speaks only for the strong. In any scheme where some profit at the expense of others, there will always be winners and losers. And, naturally, the winners think the system is not broken. But this is one of the reasons securities laws exist in the first place — to place all investors on an equal footing when it comes to the opportunity to evaluate risk and reward. Whether investors fully avail themselves of that opportunity is another thing. But, as a matter of law, one simply cannot say that investors were injured because LPI was required to comply with the law. This objection must be denied.

IV. Conclusion

As Hufstetler's objection makes clear, the class action settlement engineered and implemented by class counsel is not without its critics. To those critics, the settlement presented options, but not the options they wanted. Ultimately, the critics want the bargain they struck with Pardo. But that bargain is history, not because of the professionals in this case, but because of ingredients common to many failed companies, greed and mismanagement. This was a legacy that class counsel inherited, not created. Class counsel has substantially contributed to ameliorating the effects of that legacy. It should be compensated accordingly.

* * * END OF REPORT AND RECOMMENDATION * * *