

Square Mile Structured Deb (One) LLC v Swig
2013 NY Slip Op 31803(U)
July 23, 2013
Sup Ct, New York County
Docket Number: 603825/08
Judge: Charles E. Ramos
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SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: Ramos Justice

PART 53

Square Mile Structured
-v- Debt

INDEX NO. 603825/08

MOTION DATE

MOTION SEQ. NO. 021

Swig, K.

The following papers, numbered 1 to , were read on this motion to/for

Notice of Motion/Order to Show Cause — Affidavits — Exhibits No(s).

Answering Affidavits — Exhibits No(s).

Replying Affidavits No(s).

Upon the foregoing papers, it is ordered that this motion is

Motion is decided in accordance with
accompanying Memorandum Decision.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE
FOR THE FOLLOWING REASON(S):

Dated: 7/23/13

CHARLES E. RAMOS J.S.C.

- 1. CHECK ONE: CASE DISPOSED
2. CHECK AS APPROPRIATE: MOTION IS: GRANTED DENIED GRANTED IN PART OTHER
3. CHECK IF APPROPRIATE: SETTLE ORDER SUBMIT ORDER DO NOT POST FIDUCIARY APPOINTMENT REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION

-----X
SQUARE MILE STRUCTURED DEBT (ONE) LLC, et
al.,

Plaintiffs,

-against-

Index No.
603825/08

KENT M. SWIG, et al.,

Defendants,

-----X
KENT M. SWIG and FTI CONSULTING, INC., as
Administrator for Creditors Pursuant to
Judgment Entered October 18, 2011,

Cross-claim Plaintiffs,

-against-

KMS HOLDINGS, LLC,

Cross-claim Defendant.

-----X

HON. CHARLES E. RAMOS, J.S.C.:

Upon this motion pursuant to CPLR 4403, cross-claim
plaintiffs Kent M. Swig (Swig) and FTI Consulting, Inc.,
Administrator for Creditors (Administrator), seek to confirm in
part, and modify in part, the Report of the Hon. Ira Gammerman,
JHO (the Special Referee), filed October 24, 2012, that awarded
fees and costs related to a judgment (see notice of motion,
exhibit K), entered on October 18, 2011 (see *Square Mile
Structured Debt (One) LLC, et al. v Kent M Swig, et al.*, index
No. 603825/08 [the Judgment]), and referred certain aspects of
the decision to a Referee on June 7, 2012 (the Reference). To

this extent, the underlying facets of the litigation are not at issue, and will only be expatiated to the degree necessary.

Specifically, the Reference ordered that "the portion of the action that seeks the recovery of attorneys' fees is severed and the issue of the amount of reasonable attorneys' fees the cross-claim plaintiffs may recover against [KMS Holdings, LLC] is referred to a Special Referee to hear and determine." In eventuality, upon election of the parties, the Report referred to above was issued, rather than a determination. See notice of motion, exhibit K, 5:22-6:24.

After a hearing, including presentation of billing statements and cross-examination, the Special Referee fixed fee amounts for the cross-claim plaintiffs. The cross-claim plaintiffs agree that the portion of fees and costs incurred that the Special Referee did award is accurate, and seek to confirm those amounts as fixed. However, the cross-claim plaintiffs maintain that the Special Referee improvidently excluded from the fee award amounts that corresponded to time entries that were redacted based on attorney-client privilege and attorney work product (redaction).

As a result, of the \$289,678.05 in fees and costs sought by the Administrator of cross-claim plaintiffs, the Special Referee eliminated \$105,909.50 due to redaction. Similarly, of the \$142,827.58 sought by Mr. Swig, the Special Referee eliminated

\$18,827.50 based on the redactions. As part of the total reductions, the Special Referee reportedly eliminated amounts, even if the detail of the work performed was not redacted, where the description appeared as a summary of work that contained a redacted entry. Cross-claim plaintiffs note that the Special Referee did not allow them to cure the perceived defect and present un-redacted bills *in camera*.

Upon this motion, cross-claim plaintiffs maintain that the Special Referee, in eliminating such amounts, erred as a matter of law. More specifically, cross-claim plaintiffs request that this Court, pursuant to CPLR § 4403: (a) confirm that part of the Report which determined that the sums of \$124,000 (as to Mr. Swig), and \$183,768.55 (as to Administrator) are due and owing from cross-claim defendant for fees and expenses; (b) reject that part of the Report that denies \$124,737 worth of fees (i.e., \$105,909.50 as deducted from the Administrator's claim for fees, and \$18,827.50 as deducted from Swig's claim for fees) incurred because of redacted entries; (c) award \$68,019 (\$53,644 as for the Administrator, and \$14,375 as for Mr. Swig) in attorneys' fees the cross-claimants incurred in connection with the fees hearing; and d) direct that judgment be entered in favor of cross-claim plaintiffs and against cross-claim defendant for \$500,524.55 (the total of [a], [b], and [c] hereinabove), together with costs, interest and disbursements.

RELEVANT BACKGROUND

Prior to the finalization of a restructuring agreement with Swig's creditors and a related judgment, cross-claim defendant KMS Holdings, LLC (KMSH), a family trust previously controlled by Mr. Swig, but subsequently controlled by his estranged wife, claimed an interest in one of the assets subject to the judgment, to wit, certain receivables from loans Mr. Swig had made to KMSH. Mrs. Swig claimed that the financings were not loans, but gifts of some sort. Justice Fried, who then presided over this matter, provided for a process whereby the parties would resolve the issue of entitlement to the \$3,374,294.50 balance due of the Swig loans to KMSH (the KMSH Loans) by filing claims and litigating that question.

In this regard, as of November 16, 2011, Swig filed a cross claim against KMSH for a declaration that the KMSH Loans were a due, valid, and payable obligation. That claim included a prayer for reasonable attorneys' fees, legal expenses, and costs. On November 17, 2011, the Administrator joined in the cross claim. After discovery, KMSH demanded a jury trial of the issue of liability on the loans, and cross-claim plaintiffs moved for summary judgment.

On June 7, 2012, Justice Fried granted cross-claim plaintiffs their motion for summary judgment, finding that the KMSH loans were due, valid, and payable obligations, and rejected

the assertion that the loans were gifts. He then directed entry of judgment on the amounts owing on the loans and ordered a reference to hear and determine the amount of attorneys' fees and costs owing to cross-claim plaintiffs under certain indemnification provisions of the applicable Operating Agreement. On July 5, 2012, KMSH filed a notice of appeal.

On July 6, 2012, as directed in Judge Fried's judgment, cross-claim plaintiffs served a copy of the judgment on the Special Referee Clerk with notice of entry, and, by notice dated August 8, 2012, the court scheduled a Special Referee Hearing to calculate attorneys' fees for October 17, 2012 (the Fee Hearing).

On October 16, 2012, the day before the scheduled Fee Hearing, KMSH moved, by order to show cause, to vacate the cross-claim judgment (CPLR 5015), and for a temporary restraining order staying the Fee Hearing pending determination on its motion to vacate. Judge Jeffrey K. Oing heard and denied both the motion to vacate the judgment, and KMSH's application for a temporary restraining order.

The following day, on October 17, 2012, the Special Referee proceeded with the Fee Hearing to assess the attorneys' fees incurred by Swig and the Administrator, and owed by KMSH, pursuant to the cross-claim judgment. At the Fee Hearing, the Special Referee, eliminated, apparently sua sponte, all of the attorneys' fees for billing entries that had been redacted for

preservation of attorney client/work product privilege (the Report).

At that time, cross-claim plaintiffs requested leave to "cure" the issue by submitting un-redacted billing statements, and the request was denied. See notice of motion, exhibit K, Fee Hearing tr at 17:1-5.

After the Fee Hearing, counsel for the Administrator filed a submission with the Special Referee, which included un-redacted billing statements for *in camera* review. The Special Referee declined to change the determination based on the submission, and the Report was filed on October 24, 2012.

ANALYSIS

In support of their motion, cross-claim plaintiffs assert that this Court should confirm the Special Referee's Report to the extent of the attorneys' fees already awarded, but reject it insofar as it excludes amounts based on entries redacted to preserve attorney-client privilege, and modify the Report so as to include such fees. The cross-claim plaintiffs maintain that the Special Referee committed clear error in excluding the fees, and also seek attorneys' fees incurred preparing for, and attending, the Fee Hearing ("fees on fees").

Cross-claim defendants cross-move this Court to reject the Special Referee's award of legal fees and expenses to the Administrator, and deny cross-claim plaintiffs' request for "fees

on fees" because the indemnity provision in KMSH's operating agreement does not specifically authorize such recovery. Alternatively, KMSH maintains that cross-claim plaintiffs' legal fees are excessive, and should be reduced. In any event, KMSH, argues, at the very least, the Special Referee's deduction of attorneys' for billing entries which contained redactions was proper.

ANALYSIS

CONFIRMATION OF REFEREE'S REPORT

Generally, the report of a Special Referee should be confirmed whenever the findings are substantially supported by the record, the issues have been properly defined and addressed, and matters of credibility have been resolved (*Thomas v Thomas*, 21 AD3d 949 [2nd Dept 2005], *lv denied* 6 NY3d 704 [2006]).

Here, however, it appears that there has been a misapprehension or misapplication of the law. As a matter of law, "billings redacted on the ground of privilege [may be] properly included" in a fee application (*BDP Intl. Fin. Corp. v Castillo*, 55 AD3d 451, 452 [1st Dept 2008], citing *Soiefer v Soiefer*, 17 AD3d 268, 269 [1st Dept 2005] ["[t]he attorneys' bills were properly redacted so as to safeguard defendant's attorney-client privilege"]; see also *Teich v Teich*, 245 AD2d 41, 41 [1st Dept 1997] ["the order on appeal properly (permitted) the redaction of all material contained in defendant's attorney's

bills other than the number of hours worked and the dollar amount charged"]. Thus, the Special Referee's assertion that bills submitted for consideration may not, in the first instance, be redacted, is at odds with the prevalent case law.

However, the Special Referee has the right to challenge any such redactions if determining the reasonableness of such bills requires sight of the redacted information. To wit, and as argued by cross-claim defendants, an "at issue" waiver may be applicable because in order to determine the reasonableness of the services rendered by cross-claim plaintiffs' counsel, the Special Referee may need to invade the privilege to assess vital information (*Deutsche Bank Trust Co. of Ams. v Tri-Links Inv. Trust*, 43 AD3d 56, 63-64 [1st Dept 2007] ["'[a]t issue' waiver of privilege occurs where a party affirmatively places the subject matter of its own privileged communication at issue in litigation, so that invasion of the privilege is required to determine the validity of a claim or defense of the party asserting the privilege, and application of the privilege would deprive the adversary of vital information"])).

The cross-claim plaintiffs did not, technically, place their bills "at issue" voluntarily. Rather, the judgment of Judge Fried made those bills the subject of the Fee Hearing. To this extent, it would be inappropriate to charge cross-claim plaintiffs with creating a waiver. Nonetheless, it is certainly

within the purview of the Special Referee to require sight of the redacted material where a determination as to the reasonableness of the fees, which is the very substance of the reference, cannot be accomplished without more specific information, or where there is a threat of duplication of services, or where the services may not be commensurate with the amounts claimed (See e.g. *Matter of Karp v Cooper*, 145 AD2d 208, 215 [1st Dept 1989]). In such situations, the Special Referee might rightly consider *in camera* review of the relevant documentation as a necessity (Compare *De La Roche v De La Roche*, 209 AD2d 157, 159 [1st Dept 1994] [as "bills showing services, conversations, and conferences between counsel and others are protected from disclosure ... plaintiff [may be] directed to submit the challenged material for *in camera* inspection"])).

Moreover, there is ample law that by the very act of seeking to recover attorneys' fees and expenses, cross-claim plaintiffs place the reasonableness, necessity, and value of their attorneys' services squarely in issue (See e.g. *Margolin v Grossman*, 254 AD2d 158 [1st Dept 1998]). Thus, this Court concludes that any party subject to a request for *in camera* review of un-redacted billing records would be bound to comply, or potentially have the material excluded, or otherwise handled within the powers delegated to the Special Referee.

While this Court does not take issue with the Special

Referee's determination that "if you are claiming a fee, you can't redact" (see Fee Hearing tr at 27:26-28:2), this Court finds that the provident course of action would have been for the Special Referee to review the redacted billing entries in order to determine whether the fees sought were reasonable.

As a result, this Court rejects the Report (CPLR 4403), and exercises its power to make a new finding with regard to attorneys' fees based upon its *in camera* review of all of the billing records.

In order to make this determination, this Court has considered, among other factors, the reported time, and expected labor required, including consideration of the difficulty of the questions involved, and the putative skill required to handle the problems presented, the reported experience, ability, the reputation of the attorneys, the amount involved and benefit resulting to the client from the services, and customary fees charged for such services in the experience of the court (See *Matter of Freeman*, 34 NY2d 1, 9 [1974]); *Diaz v Audi of Am.*, 57 AD3d 828, 830 [2nd Dept 2008]). Having had sight of all entries, this Court replaces the amounts indicated in the Report with awards of \$231,742.44 in fees to the Administrator, and \$114,262.06 to Swig.

FEEES ON FEEES

In addition, Swig and the Administrator seek an award of

\$68,019 (\$53,644 as for the Administrator, and \$14,375 as for Mr. Swig) in attorneys' fees they incurred in connection with the Fees Hearing. KMSH characterizes this application as one for "fees on fees," and cross-moves this Court to reject the application. The award of fees for the Fee Hearing is granted, and the cross motion is denied.

At the outset, the Court does not readily accept the characterization of the assessment of the reasonableness of fees as conducted in the Fee Hearing as evocative of "fees on fees." Submission of attorney bills are a normal incident of litigation whenever reasonable attorneys' fees must be determined, as, for example, upon a determination of a right to indemnification pursuant to any application for fees. Such applications are normally part of the assessed costs, and do not fall within the special category of "fees on fees" (See e.g. *Matter of Rahmey v Blum*, 95 AD2d at 301 ["[h]ours reasonably spent by counsel in preparing the fee application and in litigating a fee award are also compensable"], citing *Gagne v Maher*, 594 F2d 336, 344 [2nd Cir 1979], *affd sub nom Maher v Gagne*, 448 US 122 [1980] ["time reasonably spent by plaintiff's attorneys in establishing their fee would be compensable"]; *Giarrusso v City of Albany*, 174 AD2d 840, 841 (3rd Dept 1991) ["[t]he hours reasonably spent on the fee application ... are compensable"] [citations omitted]).

There is no indication that "the clock stops" as soon as the

issue of reasonable attorneys' fees is raised in the latter stages of trial, or, indeed, that a change of the jurisprudential personality hearing that phase of the trial somehow transforms the application from a normal part of litigation into an application for fees on fees.

In all events, most fees-on-fees decisional law has been made in the context of appeals to recover attorneys' fees awarded in an underlying judgment (See e.g. *Diaz* 57 AD3d at 831-32 ["an award of an additional attorney's fee for the litigation of this appeal is reasonable"]; *Duell v Condon*, 200 AD2d 549 (1st Dept 1994), *affd* 84 NY2d 773 [1995] [remanding case for the purpose of establishing amount of fees on fees]; *Washburn v 166 East 96th St. Owners Corp.*, 166 AD2d 272, 273 [1st Dept 1990] [remanding to determine the "amount of attorneys' fees and disbursements to be awarded plaintiff as a result of having to respond to this appeal"]).

Despite this, there is no per se rule against fees on fees articulated by New York Courts (See *546-552 W. 146th St. LLC v Arfa*, 99 AD3d 117, 121 [1st Dept 2012]). To be fair, there has been considerable confusion on the matter of fees on fees, as the topic presents an overlap between common-sense readings of contractual language, applicable statutory provisions, and New York public policy (See *Id.*). As a matter of public policy, New York strenuously adheres to the "American Rule," which provides

that attorneys' fees are incidents of litigation, and a party that prevails may not collect them from the a party that loses unless such an award is explicitly authorized by agreement between the parties, by statute, or by other specific court rule (*Hooper Assoc. v AGS Computers*, 74 NY2d 487, 491 [1989]).

With reference to statutory provisions, the Court of Appeals has found that it is generally implicit in legislation that attorneys' fees are not to be awarded absent explicit statements that such an award is recoverable (*See Chapel v Mitchell*, 84 NY2d 345, 349 [1994]; accord *Buckhannon Bd. & Care Home, Inc. v West Virginia Dept. of Health & Human Resources*, 532 US 598, 602 [2001]).

Despite this, many statutory provisions have been analyzed for the possibility of allowing fees on fees with varying outcomes (*See e.g. Baker v Health Mgt. Sys.*, 98 NY2d 80 [2002] [in the context of Business Corporation Law §§ 722, 723 (a), and 724 (a), fees on fees should not be awarded]; *Posner v S. Paul Posner 1976 Irrevocable Family Trust*, 12 AD3d 177, 179 [1st Dept 2004]; *Senfeld v I.S.T.A. Holding Co.*, 235 AD2d 345, 345-346 [1st Dept 1997], *lv denied* 92 NY2d 818 [1998] ["it is now settled in this Department that a 'fee on a fee' ... is recoverable under Real Property Law § 234"]; *Hempstead Gen. Hosp. v Allstate Ins. Co.*, 106 AD2d 429, 431 [2nd Dept 1984], *affd* 64 NY2d 958 [1985] [fee on fee is not authorized under 11 NYCRR 65.16 (c) (8)]).

While with reference to statutory provisions, the prevailing view of the Court of Appeals has been that attorneys' fees are not, absent explicit statements, recoverable. Here, there is no statutory reference, but only contractual language that may be brought to bear.

To wit, section 5.8 of the Operating Agreement indicates that KMSH

"shall indemnify and defend the Managing Member ... against and hold them harmless from any and all losses, judgments costs, damages, liabilities, fines, claims and expenses (*including, but not limited to, reasonable attorneys' fees and court costs, which shall be paid by [KMSH] as incurred*) that may be made or imposed upon such Persons ... by reason of any act or inaction which is determined by the Managing Member in good faith to have been in the best interest of [KMSH] so long as such conduct shall not constitute willful misconduct or gross negligence" (Emphasis added).

A proper putative reading of this language has been suggested by the Appellate Division, First Department. That court noted that where provisions are limited to authorize indemnification only with respect to claims and demands, and they do not "specifically authorize expenses or legal fees incurred in obtaining indemnification [they are not] 'unmistakably clear' [and] fees on fees [are not] contemplated." However, the court then went on to propose that where, as here, the "indemnity clause ... of [an] operating agreement[] expressly states that it covers 'any and all losses, claims, damages, liabilities, expenses (*including legal fees and expenses*)'" (546-552 W. 146th

St. LLC, 99 AD3d at 122 [emphasis added]), fees on fees may be recoverable. As such, the language of this Operating Agreement suggests that even if the application for fees is characterized as fees on fees, they are, nonetheless, compensable.

The Referee's Report also observes that fees on fees may not be recoverable because "the claim for fees terminates at the entry of the judgment unless there is a subsequent order that permits the attorney seeking fees to seek fees for the time spent in seeking fees" (Report at 36:12-15; see also *Pincus v Wells*, 35 AD3d 569, 570 [2nd Dept 2006] ["the right of direct appeal (as to attorneys' fees) terminated with the entry of judgment in the action"]; *Conklin v Town of Ramapo*, 259 AD2d 585 [2nd Dept], *lv dismissed* 93 NY2d 1038 [1999]).

Despite this accurate reportage of salient law, here, there has been no entry of judgment. Judge Fried ordered that "the portion of the action that seeks the recovery of attorneys' fees is severed and the issue of the amount of reasonable attorneys' fees the cross-claim plaintiffs may recover against KMSH is referred to a Special Referee" (Decision and Order of 6/7/12 [emphasis added]); *Kline v Town of Guilderland*, 289 AD2d 741, 742 [3rd Dept 2001], quoting *Grullon v Servair*, 121 AD2d 502 [2nd Dept 1986] [where a cause of action is severed, "it becomes 'a separate action which may be terminated in a separate judgment'"]. There is considerable gravitas in the assertion

that if the recovery of attorneys' fees was subject to the issuance of a separate judgment, the order severing the cause of action could not simultaneously be a judgment that terminates the right of recovery.

Further, in this matter, KMSH has not disavowed its right to fees for the Fee Hearing (See *Kumble v Windsor Plaza Co.*, 161 AD2d 259, 260 [1st Dept], *lv denied* 76 NY2d 709 [1990] ["it was not error to make allowance for a fee on a fee in the absence of argument by the landlord that he himself would not have been entitled to such an allowance under the parties' lease had he prevailed"]).

It is accepted that "an award of reasonable attorney's fees may include the value of the time expended in proving the value of the services" (*Galasso Langione & Botter, LLP v Liotti*, 22 Misc 3d 450, 453 [Sup Ct, Nassau County 2008], *affd* 81 AD3d 880 [2nd Dept 2011], citing *Posner*, 12 AD3d at 177). At the risk of oversimplification, from an equitable stance, evaluation of reasonable attorneys' fees are a natural part of litigation where the extent of due indemnification is at issue. The severance of that part of the litigation, and the hearing of the particulars of the matter before a Special Referee did not suddenly transform fees that would be a normal part of a fee application into unrecoverable expenses.

Having reviewed the applicable indemnification provision,

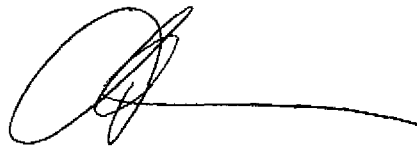
and the specific enumeration of fees, this Court determines that fees in the amount of \$34,868.60, as for the Administrator, and \$9,343.75, as for Mr. Swig, are due in addition to the other fees listed hereinabove.

The Court has considered the other arguments made with regard to confirmation or rejection of the Referee's Report, and finds them unavailing or moot in light of the foregoing determinations.

Settle order.

Dated: July 23, 2013

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J.S.C.