IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

In re:	**Chapter 11**
IEH AUTO PARTS HOLDING LLC, *et al.*,[1]	**Case No. 23-90054 (CML)**
Debtors.	**(Jointly Administered)**

UNITED STATES TRUSTEE'S OBJECTION TO FIRST AND FINAL FEE APPLICATION OF THE LAW OFFICE OF LIZ FREEMAN FOR ALLOWANCE AND PAYMENT OF FEES AND EXPENSES AS CO-COUNSEL AND CONFLICTS COUNSEL TO THE DEBTORS FOR THE PERIOD FROM JANUARY 31, 2023 THROUGH JUNE 16, 2023

TO THE HONORABLE CHRISTOPHER M. LOPEZ
UNITED STATES BANKRUPTCY JUDGE:

Kevin M. Epstein, the United States Trustee for the Southern District of Texas (the "U.S. Trustee"), objects (the "Objection") to the *First and Final Fee Application of the Law Office of Liz Freeman as Co-Counsel and Conflicts Counsel to the Debtors for the Period from January 31, 2023 Through June 16, 2023* [ECF No. 991] (the "Fee Application"). The Law Office of Liz Freeman seeks $257,839.95 in fees and expense reimbursements. *Id*.

[1] The Debtor entities in these chapter 11 cases, along with the last four digits of each Debtor entity's federal tax identification number, are: IEH Auto Parts Holding LLC (6529); AP Acquisition Company Clark LLC (4531); AP Acquisition Company Gordon LLC (5666); AP Acquisition Company Massachusetts LLC (7581); AP Acquisition Company Missouri LLC (7840); AP Acquisition Company New York LLC (7361); AP Acquisition Company North Carolina LLC (N/A); AP Acquisition Company Washington LLC (2773); Auto Plus Auto Sales LLC (6921); IEH AIM LLC (2233); IEH Auto Parts LLC (2066); IEH Auto Parts Puerto Rico, Inc. (4539); and IEH BA LLC (1428). The Debtors' service address is: 112 Townpark Drive NW, Suite 300, Kennesaw, GA 30144.

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I. INTRODUCTION

1. This Court should deny the Fee Application in its entirety given Ms. Freeman's violation of her disclosure, ethical, and fiduciary obligations. Ms. Freeman was in an undisclosed, intimate relationship and living with former United States Bankruptcy Judge David R. Jones, the appointed mediator in this case, during her employment as debtors' counsel. Ms. Freeman never informed the Court or the other parties of this relationship when Judge Jones was proposed or appointed as mediator and never amended her disclosures, either before or after she participated personally in the mediation.

2. Ms. Freeman's failure to disclose her relationship with Judge Jones violated her continuing obligation to disclose all of her connections under Federal Rule of Bankruptcy Procedure 2014 ("Rule 2014") and under the order approving her employment, as well as her commitment in her sworn declaration to do so. Her failure also violated this Court's Local Rules, requiring parties to inform the presiding judge of any conflicts with the mediator. *See* S.D. Tex. L.R. 16.4.I(2).[2] Likewise, her disclosure failures violated, at a minimum, the following Texas Disciplinary Rules of Professional Conduct ("Disciplinary Rules") that all lawyers are required to follow in this District.[3]

- 3.03 (Candor Toward the Tribunal);
- 3.04 (Fairness in Adjudicatory Proceedings);
- 3.05 (Maintaining Impartiality of Tribunal); and

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[2] The district court's local rules apply in this Court. *See* BLR 1001-1(b) ("In addition to these rules, the Local Rules of the District Court, the Administrative Procedures for CM/ECF, and the standing and general orders govern practice in the bankruptcy court.").

[3] All attorneys practicing before this Court must comply with "the Texas Disciplinary Rules of Professional Conduct." S.D. Tex. L.R., App. A, R. 1(A).

- 4.01 (Truthfulness in Statements to Others).

3. Once Judge Jones was appointed mediator, Ms. Freeman was no longer qualified to serve as debtor's counsel because she was not disinterested and labored under an actual conflict of interest with the estate and the creditors. Ms. Freeman breached her fiduciary duty to the estate and the Court by depriving the parties of a fair and impartial mediation that resulted in a settlement incorporated in the confirmed plan. Her lack of candor and misconduct has gravely undermined public confidence and tarnished the reputation of this Court. This Court should exercise its statutory and equitable authority to deny the Fee Application in its entirety.

II. FACTUAL BACKGROUND

A. General Information.

4. On January 31, 2023, the Debtors filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code. The Court ordered these cases to be jointly administered on February 1, 2023 [ECF No. 25].

5. On March 2, 2023, Debtors filed the *Application to Retain the Law Office of Liz Freeman, PLLC as Co-Counsel and Conflicts Counsel for the Debtors and Debtors in Possession* [ECF No. 183] (the "Employment Application"). The Debtors sought to employ Ms. Freeman as their bankruptcy co-counsel and as conflicts counsel to represent them along with the Debtors' lead bankruptcy counsel, Jackson Walker LLP ("Jackson Walker").[4] The Employment Application did not identify any particular conflict requiring her retention by the Debtors; rather,

[4] Ms. Freeman was previously an equity partner at Jackson Walker until December 2022 when she resigned her partnership in Jackson Walker by mutual agreement after the firm confirmed that she was in a relationship with Judge Jones, *see*, *e.g.*, *In re JC Penney Direct Marketing Services, LLC*, No. 20-20184, ECF No. 1244 (Bankr. S.D. Tex. Nov. 13, 2023) (Jackson Walker's "Preliminary Response"). Nevertheless, neither Ms. Freeman nor Jackson Walker acted to prevent Judge Jones from thereafter mediating this case.

she was to "provide legal advice and services on any matter on which JW may have a conflict or as needed based on specialization." *Id.* at ¶ 8.

6. In support of her Employment Application, Ms. Freeman attested that "[b]ased on the conflicts search I conducted, to the best of my knowledge, neither I, nor the Firm, have any connections with the Debtors, their creditors, or other parties in interest, their respective attorneys and accountants other than what is disclosed in this Declaration," and that she would "periodically review both the changes in identifiable parties in interest of the Debtors and clients of the Firm as such information becomes available or relevant and will update this disclosure as appropriate." *Declaration of Liz Freeman in Support of the Application to Retain the Law Office of Liz Freeman as Co-Counsel and Conflicts Counsel for the Debtors and Debtors-in-Possession* [ECF No. 183 at p. 16 ¶ 7] (the "Freeman Declaration").

7. On April 3, 2023, the Court approved the employment of Ms. Freeman and her firm. *Order Authorizing the Retention and Employment of the Law Office of Liz Freeman, PLLC as Co-Counsel and Conflicts Counsel for the Debtors and Debtors in Possession* [ECF No. 320] (the "Employment Order"). The Employment Order required Ms. Freeman's firm to "review its files periodically during the pendency of these Chapter 11 Cases to ensure that no conflicts or other disqualifying circumstances exist or arise. If any new relevant facts or relationships are discovered or arise, the Firm will use reasonable efforts to identify such further developments and will promptly file a supplemental declaration, as required by Fed. R. Bankr. P. 2014(a)." Employment Ord. at p. 2 ¶ 3.

B. The Mediation.

8. Three days after the Court approved Ms. Freeman's employment, on April 6, 2023, the Debtors, the Official Committee of Unsecured Creditors (the "Committee"), and the DIP Lender, American Entertainment Properties Corp., filed a *Stipulation and Agreed Order* [ECF No.

347] (the "Stipulation") agreeing to mediate before former Judge Jones. The Stipulation states that "[a]t all times in the performance of his mediation duties," Judge Jones would be "acting in his official capacity as a United States Bankruptcy Judge." Stipulation at p. 1 ¶ 1.

9. When the parties submitted the Stipulation, Ms. Freeman and Judge Jones were in an undisclosed, romantic relationship that began sometime before they bought a house together in 2017, where they lived. Although allegations of the relationship between Ms. Freeman and Judge Jones surfaced in March 2021 in the *McDermott* bankruptcy case, the facts only became public knowledge in October 2023, when Judge Jones admitted the relationship to the Wall Street Journal. *Complaint Identified by the Chief Judge of the Fifth Circuit Court of Appeals Against United States Bankruptcy Judge David R. Jones, Southern District of Texas, Under the Judicial Improvements Act of 2002*, Complaint No. 05-24-9002 (5th Cir. Oct. 13, 2023) ("Ethics Complaint"); *see also* Alexander Gladstone & Andrew Scurria, *Bankruptcy Judge Jones Named in Lawsuit Over Romantic Relationship with Local Lawyer*, Wall Street Journal Pro, Oct. 7, 2023.

10. Neither Judge Jones nor Ms. Freeman disclosed their relationship to the Court or to the other parties to the mediation. On April 10, 2023, the Court approved the Stipulation and entered an order appointing Judge Jones as the mediator.

11. Judge Jones conducted the mediation on April 19-20, 2023. *Debtors' Emergency Motion for Entry of an Order Approving the Settlement Between the IEH Debtors, AEP, PEP Boys, the Committee and the Committee Members* [ECF No. 444 p. 3 ¶ 22] (the "Settlement Motion").

12. Ms. Freeman billed the Debtors for services and expenses in connection with the mediation, including appearances at the mediation conducted by Judge Jones. Fee Application at pp. 8–9; *see also* the Time Records for the Fee Application [Fee Application-4] (the "Time Records") at p. 2.

13. On May 2, 2023, the Court approved a settlement negotiated in the mediation that ultimately dictated material terms of the Debtors' plan (the "Settlement"). *Order Approving Debtors' Emergency Motion for Entry of an Order Approving the Settlement Between the IEH Debtors, AEP, PEP Boys, the Committee, and the Committee Members* [ECF No. 469] (the "Settlement Order").

14. Ms. Freeman did not supplement the Freeman Declaration to disclose her connections to Judge Jones at any time after Judge Jones was proposed or appointed as mediator.

15. On June 16, 2023, the Court approved the Debtors' Disclosure Statement and confirmed the Plan of Liquidation. *Order Confirming the Third Amended Combined Disclosure Statement and Joint Plan of Liquidation of IEH Auto Parts Holding LLC and its Debtor Affiliates Pursuant to Chapter 11 of the Bankruptcy Code* [ECF No. 749] (the "Confirmation Order"); *Third Amended Combined Disclosure Statement and Joint Plan of Liquidation of IEH Auto Parts Holding LLC and its Debtor Affiliates Pursuant to Chapter 11 of the Bankruptcy Code* [ECF No. 738] (the "Plan"). The Plan incorporated the Settlement that resulted from the mediation. *Debtors' Emergency Motion for Entry of an Order (i) Conditionally Approving the Disclosure Statement; (ii) Approving the Solicitation and Notice Procedures; (iii) Approving the Forms of Ballots and Notices in Connection Therewith; (iv) Approving the Combined Hearing Timeline; and (v) Granting Related Relief* [ECF 443 p. 4 ¶ 5].

16. On October 6, 2023 (the "Effective Date"), the Debtors filed a *Notice of (I) Entry of Confirmation Order (II) Occurrence of Effective Date, and (III) Related Bar Dates* [ECF No. 922] (the "Effective Date Notice").

17. The next day, the news of Ms. Freeman's and Judge Jones's undisclosed relationship became public. *See, e.g.*, Ethics Complaint; Alexander Gladstone & Andrew Scurria,

Bankruptcy Judge Jones Named in Lawsuit Over Romantic Relationship with Local Lawyer, Wall Street Journal Pro, Oct. 7, 2023.

III. OBJECTION

18. The Bankruptcy Code prohibits the estate from employing counsel who are not disinterested or who hold any interest adverse to the estate or its creditors. 11 U.S.C. § 327.

19. In addition, because this Court's local rules prohibit the appointment of a mediator whose impartiality can reasonably be questioned, S.D. Tex. L.R. 16.4.I(1), those local rules also require parties to inform the presiding judge of potential conflicts of interest with the mediator, S.D. Tex. L.R. 16.4.I(2).

20. Courts cannot enforce these requirements if counsel does not make complete and honest disclosures and update them as circumstances change. Accordingly, multiple rules—including bankruptcy and mediation specific rules and Disciplinary Rules—required Ms. Freeman to disclose her relationship with Judge Jones when he was proposed as a mediator. But Ms. Freeman did not.

21. In failing to disclose her relationship with Judge Jones, Ms. Freeman violated her duty under Rule 2014, the Employment Order, and the Freeman Declaration to disclose all her "connections," which violated her duty under Local Rule 16.4.I(2), and violated the Disciplinary Rules, including, *inter alia*, her duty of candor to the parties and the Court, thereby breaching her fiduciary duty to the estate.

22. Ms. Freeman's failure to disclose deprived the parties of a fair and impartial mediation that dictated the terms of the confirmed Plan. Therefore, the Court should exercise its statutory and inherent authority to deny the Fee Application in its entirety.

A. Under Rule 2014 and this Court's Local Rules, Ms. Freeman Was Required to Disclose Her Connections with Judge Jones.

23. All professionals seeking retention as estate-paid professionals under 11 U.S.C. § 327 must be disinterested and conflict free.

24. To enforce these statutory requirements, professionals must file a Rule 2014 verified statement disclosing all the professional's connections with the "debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States [T]rustee or any person employed in the office of the United States [T]rustee." Fed. R. Bankr. P. 2014. One of the overarching goals of the retention and disclosure requirements is "to preserve public confidence in the fairness of the bankruptcy system." *In re Sundance Self Storage-El Dorado LP*, 482 B.R. 613, 625 (Bankr. E.D. Cal. 2012).

25. Rule 2014 disclosures are not limited to connections that would—in the professional's view—render the professional unable to be employed under 11 U.S.C. § 327(a) because of an adverse interest, conflict, or lack of disinterestedness. Rather, Rule 2014 requires the disclosure of *all* known connections. Professionals "cannot pick and choose which connections are irrelevant or trivial." *In re EWC, Inc*., 138 B.R. 276, 280 (Bankr. W.D. Okla. 1992). The requirement to disclose all connections is not subjective because "[t]he decision as to what facts may be relevant should not be left up to the professional, 'whose judgment may be clouded by the benefits of potential employment.'" *In re Fibermark, Inc.,* No. 04-10463, 2006 WL 723495 at *8 (Bankr. D. Vt. March 11, 2006) (quoting *In re Lee*, 94 B.R. 172, 177 (Bankr. C.D. Cal. 1988)). Said differently, "the existence of a conflict of interest is not the quid pro quo for whether or not disclosure must be made." *In re Matco Elecs. Grp., Inc*., 383 B.R. 848, 853 (Bankr. N.D.N.Y. 2008).

26. Moreover, the requirement to be disinterested "does not evaporate once the attorney's employment is approved." *In re Sundance Self Storage-El Dorado*, 482 B.R. at 625. As a result, Rule 2014 also "requires professionals to reveal connections that arise after their retention." *In re Granite Partners, L.P.*, 219 B.R. 22, 35 (Bankr. S.D.N.Y. 1998); s*ee also I.G. Petroleum, L.L.C. v. Fenasci (In re W. Delta Oil Co.)*, 432 F.3d 347, 355 (5th Cir. 2005) (quoting *Kravit, Gass & Weber, S.C. v. Michel (In re Crivello)*, 134 F.3d 831, 836 (7th Cir. 1998) ("Although [Rule 2014(a)] does not explicitly require ongoing disclosure, case law has uniformly held that under Rule 2014(a), (1) full disclosure is a continuing responsibility, and (2) an attorney is under a duty to promptly notify the court if any potential for conflict arises.") (internal quotation marks omitted)); *In re eToys, Inc.,* 331 B.R. 176, 190 (Bankr. D. Del. 2005) ("[T]he duty to disclose is ongoing."). Ms. Freeman also acknowledged her obligation to update her Rule 2014 disclosures. *See* Freeman Decl. ¶ 7. *See also* Employment Ord. at p. 2 ¶ 3 (reiterating her continuing duty to disclose).[5]

27. Although judges and mediators are not specifically mentioned in Rule 2014, the duty of disclosure is consistently held to be exceedingly broad, and even unintentional omissions of connections are at the professional's peril. *See, e.g.*, *I.G. Petroleum*, 432 F.3d at 355. Consistent

[5] In *Free Speech Systems*, the Court denied the employment applications of two professionals because they failed to update their Rule 2014 disclosures during new connections. There the Court stated, "[t]he lack of transparency and the lack of disclosures required under Bankruptcy Rule 2014, which says any connections, give this Court a lot of concern about whether these professionals can impartially represent [the debtor], which may include making difficult decisions about other parties, if necessary." *In re Free Speech Systems, LLC,* No. 22-60043 Tr. September 20, 2022, at p. 247. "I think I'm making the right decision under the law. I think I'm commanded by the law, the Fifth Circuit case law, to make this decision." *Id*. at p. 249. As in *Free Speech Systems*, this Court should not hesitate to hold Ms. Freeman accountable and deny all compensation for her intentional failure to disclose her connections with former Judge Jones.

with the case law, the Advisory Committee notes to Rule 5002 state that professionals should make "appropriate disclosure" under Rule 2014 of their connections with a judge if those connections might render their employment improper. *See* Fed. R. Bankr. P. 5002(b) (Advisory Committee note to 1985 amendment). Parties to a mediation are entitled to know that their mediator would be going home with Debtors' counsel. "Perceptions are important; how the matter likely appears to creditors and to other parties in legitimate interest should be taken into account." *In re Martin*, 817 F.2d 175, 182 (1st Cir. 1987).

28. There can be little question that Rule 2014 disclosures must include connections with judges and mediators. In *In re Smith*, 524 B.R. 689, 695 (Bankr. S.D. Tex. 2015), the court considered whether a former judge serving as mediator was a "professional person" within the meaning of 11 U.S.C. § 327 and Rule 2014. The court acknowledged that, "as a mediator in the instant dispute, he would have had substantial discretion over a very important and high-dollar issue central to the administration of the Debtor's . . . case." *Id.* at 695. Moreover, even if the former judge were not a professional, the court found it necessary to "use its § 105(a) powers" to apply section 327 and by extension Rule 2014 "to prevent any abuse of the process of selection of ex-bankruptcy judges as mediators—*including the appearance of an abuse of this selection process*." *Id.* at 697 (emphasis in original). These concerns are heightened when the mediator is a judge sitting on the same bench.

29. Not only was disclosure required under Rule 2014, the local rules of this Court expressly require parties to inform the presiding judge of potential conflicts of interest with the mediator: "Issues concerning potential ADR provider conflicts shall be raised with the judge presiding in the case relating to the ADR proceeding." S.D. Tex. L.R.16.4.I(2).

30. As a result, the selection and appointment of Judge Jones as mediator triggered an immediate obligation by Ms. Freeman to supplement the Freeman Declaration to disclose her relationship. But Ms. Freeman never disclosed her relationship to Judge Jones after his selection as mediator and, therefore, she violated Rule 2014, the Employment Order, and her sworn commitment, as well as this Court's local rules.

B. Ms. Freeman Ceased to Be Disinterested Once Judge Jones Was Appointed as Mediator, and That Appointment Created a Conflict of Interest.

31. Judge Jones's appointment as mediator also rendered Ms. Freeman no longer disinterested as required for employment under 11 U.S.C. § 327(a) (debtors "may employ one or more attorneys . . . that are disinterested persons . . . ").

32. Section 101(14) defines "disinterested" as meaning that a professional cannot "have an interest materially adverse to the interest of the estate or of any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor, *or for any other reason*." 11 U.S.C. § 101(14)(C) (emphasis added). The latter portion of the definition, which is commonly referred to as the "catch-all clause," is sufficiently broad to include any professional with an "interest or relationship that would even faintly color the independence and impartial attitude required by the Code." *In re Crivello*, 134 F.3d at 835 (quoting *In re BH & P Inc.*, 949 F.2d 1300, 1308 (3d Cir. 1991)).

33. Because of the cohabiting, intimate relationship between Judge Jones and Ms. Freeman, Ms. Freeman was not—and could not be—disinterested in this case. Ms. Freeman had a secret relationship with Judge Jones that created an undisclosed, unlevel "playing field" potentially favoring the Debtors, which is an interest materially adverse to all non-debtor stakeholders, including creditors and equity holders. As a result, Ms. Freeman and her firm had a

materially adverse interest to the creditors and equity security holders. But no one knew about her adverse interest because she failed to disclose it as required.

34. Ms. Freeman also had an economic interest in hiding the connection to Judge Jones because, if disclosed, she would be disqualified from working on cases where he presided or that he mediated. Jackson Walker said so in its communications with its ethics counsel in 2021 once it learned of the relationship:

> The firm, for its part, had concluded and has advised Elizabeth that any romantic, intimate, or sexual relationship between a firm lawyer and a federal judge would create too much risk of disqualification to be compatible with any lawyer in the firm continuing to appear before that judge.

Prelim. Resp., Ex. 1, at p. 4. This pecuniary interest was adverse to the estate's interest in retaining a disinterested mediator. Not only was a disinterested mediator important for the mediation to be effective, but subsequent discovery that the mediator was not disinterested could have jeopardized any settlement reached at the mediation.[6]

C. Ms. Freeman Violated Her Fiduciary Duties to the Estate and the Court Her Ethical Duties Under the Disciplinary Rules.

35. Ms. Freeman's failure to disclose her relationship with Judge Jones also violated her fiduciary duty to the estate and her ethical duties as a lawyer, including several Disciplinary Rules. *See* Disciplinary Rules 3.03 (Candor Toward the Tribunal), 3.04 (Fairness in Adjudicatory Proceedings), 3.05 (Maintaining Impartiality of Tribunal), and 4.01 (Truthfulness in Statements to Others).

36. Ms. Freeman had an independent duty—both fiduciary and otherwise—to abide by the law governing proper conduct in bankruptcy cases. "It is undisputed that counsel of a debtor-

[6] Although no party has complained about the outcome of the mediation, that does not change the fact that Ms. Freeman was operating under a conflict of interest.

in-possession owes certain fiduciary duties to both the client debtor-in-possession and the bankruptcy court." *ICM Notes Ltd. v. Andrews & Kurth, L.L.P.*, 278 B.R. 117, 123 (Bankr. S.D. Tex. 2002); *see also Futuronics Corp. v. Arutt, Nachamie, & Benjamin (In re Futuronics Corp.)*, 655 F.2d 463, 470 (2d Cir. 1981) (explaining that a debtor's counsel's duty to disclose "arises not solely by reason of the bankruptcy rules, but also is founded upon the fiduciary obligation owed by counsel for the debtor to the bankruptcy court.") (internal quotation marks omitted).

37. This duty is to the estate and to creditors generally but not to any creditor specifically. *ICM Notes Ltd.,* 278 B.R. at 126. Ms. Freeman's failure to object to Judge Jones's service as mediator was a breach of fiduciary duty to the estate and to the creditor body at large and a less than faithful execution of her duties as counsel to the debtor-in-possession.

38. This Court's local rules further provide that attorneys must act as "responsible professionals" and that "the minimum standard of practice is the Texas Disciplinary Rules of Professional Conduct." S.D. Tex. L.R., App. A, R. 1(A). Thus, when Ms. Freeman violated multiple Disciplinary Rules, she also violated this Court's local rules.

39. Ms. Freeman violated, among others, Disciplinary Rule 3.03 that requires candor toward the tribunal and prohibits lawyers from knowingly making a false statement of fact: "There are circumstances where failure to make a disclosure is the equivalent of an affirmative misrepresentation." Disciplinary R. 3.03, Comment 2. By failing to disclose her connection to the mediator, Ms. Freeman effectively made an affirmative misrepresentation and violated the duty of candor. *See also U.S. v. Gellene*, 182 F.3d 578, 587 (7th Cir. 1999) ("[T]he omission of material information in a bankruptcy filing impedes a bankruptcy court's fulfilling of its responsibilities just as much as an explicitly false statement.") (quotation marks omitted) (affirming attorney's conviction for bankruptcy fraud).

40. Similarly, Ms. Freeman also violated Disciplinary Rule 3.04, which addresses the fairness of court proceedings and prohibits lawyers from concealing evidence. Her failure to update her Rule 2014 disclosures concealed evidence that would have allowed parties the opportunity to object to Judge Jones mediating a case where his live-in companion represented the debtor. As Comment 1 to Disciplinary Rule 3.04 states: "Fair competition in the adversary system is secured by prohibitions against . . . concealment of evidence."

41. Disciplinary Rule 3.05 protects the impartiality of a tribunal. And Comment 2 to the Rule states basic principles that should govern alternative dispute resolution, such as mediations: "In such [alternative dispute resolution] situations, as in more traditional settings, a lawyer should avoid any conduct that is or could reasonably be construed as being intended to corrupt or to unfairly influence the decision-maker." Surely having an undisclosed live-in relationship with the mediator could reasonably be construed as intended to unfairly influence him.

42. Disciplinary Rule 4.01 requires truthfulness in statements to others. Whether a falsehood arises from affirmative representation or by omission, it is a falsehood nonetheless. Thus, Ms. Freeman's failure to disclose violated Rule 4.01, too.

43. Nevertheless, despite having an affirmative obligation to do so under both the rules of this Court and the Disciplinary Rules, Ms. Freeman never informed this Court or the other parties to the mediation that she had a disqualifying conflict with Judge Jones that should have disqualified her from continuing to serve as debtors' counsel (or Judge Jones from serving as mediator). Her silence allowed a tainted mediation to proceed.

D. Ms. Freeman's Failures Deprived Parties of their Right to an Impartial Mediator.

44. By failing to disclose her relationship with Judge Jones, Ms. Freeman deprived the parties to the mediation of their right to an impartial and unbiased mediator and sullied the mediation process, which then served as the basis for the confirmed plan.

45. For example, non-debtor parties may now reasonably suspect that Judge Jones favored Ms. Freeman's client in the mediation. Conversely, the estate could have been harmed if Ms. Freeman were constrained in pushing back against Judge Jones's suggested compromises, which could have negatively affected her efficacy as an advocate. *See In re Granite Partners*, 219 B.R. at 38 (holding firm's failure to disclose connection to target of investigation violated bankruptcy disclosure requirements, even if firm properly discharged its investigative duties, because "[b]ankruptcy is concerned as much with appearances as with reality"). "[T]he question will always linger whether it [the firm] held back, or failed to bite the hand that feeds it quite as hard as the circumstances warranted." *Id.*

46. Moreover, because of Ms. Freeman's participation in the mediation before Judge Jones, parties might also be concerned that their confidences could have been disclosed. *See CEATS, Inc. v. Cont'l Airlines, Inc.*, 755 F.3d 1356, 1363 (Fed. Cir. 2014) ("[B]ecause parties are encouraged to share confidential information with mediators, those parties must have absolute trust that their confidential disclosures will be preserved.").

47. The bias—whether actual or potential—created by this relationship undermined the very purpose of the mediation. Mediators "serve a vital role in our litigation process." *CEATS*, 755 F.3d at 1362. "Courts must feel confident that they are referring parties to a fair and effective process when they refer parties to mediation. And parties must be confident in the mediation process if they are to be willing to participate openly in it." *Id*.

48. "Because parties arguably have a more intimate relationship with mediators than with judges, it is critical that potential mediators not project any reasonable hint of bias or partiality." *Id*.; *see also* Kenneth R. Feinberg, *Mediation—A Preferred Method of Dispute Resolution*, 16 Pepperdine L. Rev. 5, 29 (1989) ("[T]he mediator must be perceived by the parties as completely neutral and impartial. This is necessary not only to ensure openness, but also to preserve the integrity of the mediation process.").

E. The Court Should Exercise Its Statutory and Inherent Authority to Deny All Fees to Ms. Freeman.

49. Ms. Freeman's breach of her duties was more than a simple technical oversight; it was blatant.[7] In fact, her omission contradicts the disclosure practices of national firms she had worked with as local counsel for years.[8] More telling, in spring 2022, Ms. Freeman's counsel advised her to disclose the relationship in amended Rule 2014 disclosures and in new cases going forward.[9]

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[7] Failures to disclose connections undermine the integrity of the bankruptcy process. *See generally Gellene*, 182 F.3d at 578 (prosecution of law firm partner for intentional omissions in his Rule 2014 disclosures).

[8] That national firm routinely includes Southern District of Texas bankruptcy judges on its schedules of material parties and discloses relationships with judges and courthouse staff as part of its employment application and accompanying Rule 2014 disclosures. *See, e.g., In re Smile DirectClub Inc*., No. 23-90786 (Bankr. S.D. Tex.), ECF No. 188, ¶¶ 22, 52 and schedule 1(n) (disclosing that a firm lawyer is a former clerk for a S.D. Tex. bankruptcy judge). Even while Ms. Freeman was still a partner at Jackson Walker, it sometimes searched for connections to judges and then wrongly attested "N/A" that there were no such connections. *See Supplemental Declaration of Kristhy Pegeuro,* pp. 6, 20, *In re GWG Holdings, Inc*., No. 22-90032, ECF No. 828 (Bankr. S.D. Tex. Oct. 6, 2022.

[9] At the time, Ms. Freeman was a partner at Jackson Walker. Ms. Freeman's counsel nevertheless maintained that he did not believe Jackson Walker had a legal obligation to disclose, which the U.S. Trustee disputes.

50. The Court has broad authority to fashion an appropriate remedy for both Ms. Freeman's violation of her many disclosure obligations and her breach of her ethical and fiduciary duties, even absent evidence that she did not professionally discharge her duties. *See In re Cruz*, No. 18-10208, 2020 WL 5083326, at *35 (Bankr. S.D. Tex. Aug. 27, 2020) ("[B]ankruptcy courts have broad leeway in determining an appropriate sanction for unethical behavior."); *In re Granite Partners*, 219 B.R. at 42 (no evidence is required to show firm failed to exercise its duties professionally and fairly before denying compensation). Further, courts have a "responsibility to supervise the conduct of attorneys who are admitted to practice before it." *In re Cruz*, 2020 WL 5083326, at *35.

51. Among other remedies, the Court may deny all compensation to a professional who fails to disclose a connection under Rule 2014. "[C]ounsel who fail to disclose timely and completely their connections proceed at their own risk because failure to disclose is sufficient grounds to revoke an employment order and deny compensation.'" *I.G. Petroleum, L.L.C,* 432 F.3d at 355.

52. As a fellow Texas bankruptcy judge recently ruled, the failure to disclose results in "strict-liability" for the professional:

> The remedy for anything short of full disclosure is denial of compensation and disgorgement of sums already paid. *Prudhomme*, 43 F.3d at 1003 (after discussing nondisclosure, holding "concealment [is] misconduct justifying disgorgement"). No exceptions are made for slipshodness or good faith. *Matter of Kero-Sun, Inc.*, 58 B.R. 770, 780 (Bankr. D. Conn. 1986) (citing *Gen. Motors Acceptance Corp. v. Undike (In re H. L. Stratton, Inc.)*, 51 F.2d 984, 987–88 (2d Cir. 1931)). This strict-liability principal [*sic*] is the law across the country. *See, e.g. In re Downs*, 103 F.3d 472, 477 (6th Cir. 1996) (citing *In re Chapel Gate Apartments, Ltd.*, 64 B.R. 569, 575 (Bankr. N.D. Tex. 1986); *In re Inv. Bankers, Inc.*, 4 F.3d 1556, 1565 (10th Cir. 1993) (citations omitted); *Futuronics Corp. v. Arrut (Matter of Futuronics Corp.)*, 655 F.2d 463, 469 (2d Cir. 1981)).

In re Chris Pettit & Associates, P.C., No. 22-50591, 2022 WL 17722853, *10 (Bankr. W.D. Tex. Dec. 13, 2022).

53. In the case of *In re Granite Partners*, the court denied more than $2 million in fees for a law firm related to an investigation that was tainted by the law firm's conflicts and failure to disclose its connections. It did so even though "there [was] no evidence that [the firm] failed to discharge its duties in a thoroughly professional manner," because "such proof need not be offered." 219 B.R. at 42. The court explained that "[t]he estate and the other objectors are not required to prove that [the firm's] conflicts skewed the investigation or its results" because, "[f]irst, parties in interest, particularly clients, should not be forced to prove that a conflicted lawyer exercised his professional judgment partially and contrary to the estate's interests," and, "[s]econd, the estate could prove this only by redoing the investigation." *Id.*[10] The court also found it was "impossible to separate completely the tainted investigation from the subsequent settlements with the other broker-dealers . . . ." *Id.* at 43.

54. Section 328(c) also provides that "the court may deny allowance of compensation for services and reimbursement of expenses of a professional person employed under section 327 or 1103 of this title if, at any time during such professional person's employment under 327 or 1103 of the title, such professional person is not a disinterested person, or represents or holds an interest adverse to the interest of the estate with respect to the matter on which such professional person is employed." 11 U.S.C. § 328(c); *see also S. Rep. No. 95–989* (July 14, 1978) ("The

[10] The court sub-divided the fee application into two parts. About half of the fees related to investigative services; the other half related to legal work. The court denied all fees for the investigative services, reduced the fees for legal work by about 15%, and required the firm to bear the costs of an investigation into its conduct, giving rise to a total reduction in fees of 59%. *Id.* at 44.

subsection provides a penalty for conflicts of interest."). "'[R]reasonable compensation for services rendered' necessarily implies . . . disinterested service . . . ." *Woods v. City Nat. Bank & Tr. Co. of Chi.*, 312 U.S. 262, 268 (1941) (case under the Chandler Act, the predecessor bankruptcy law to the current Bankruptcy Code).

55. In addition to its authority under Rule 2014 and section 328(c), the Court has authority to remedy Ms. Freeman's ethical misconduct based on its inherent powers, which derive from the nature of the bankruptcy court as a court of justice. *See Chambers v. NASCO, Inc.*, 501 U.S. 32, 45-48 (1991); *Caldwell v. Unified Capital Corp. (In re Rainbow Mag.)*, 77 F.3d 278, 284-85 (9th Cir. 1996) (holding that the bankruptcy court has the same inherent authority "that *Chambers* recognized . . . within Article III courts"). Such remedies may include the denial of a professional's fee application. *See Mapother & Mapother, P.S.C. v. Cooper (In re Downs)*, 103 F.3d 472, 477 (6th Cir. 1996) (holding that "bankruptcy court is vested with the inherent power to sanction attorneys for breaches of fiduciary obligations," including by disallowance of professional fees); *Citizens Bank & Tr. Co. v. Case (In re Case)*, 937 F.2d 1014, 1023 (5th Cir. 1991) ("We conclude that the bankruptcy court has the inherent power to award sanctions for bad-faith conduct in a bankruptcy court proceeding."); *In re Cruz*, 2020 WL 5083326, at *28 ("The Court has the power to police conduct of attorneys who appear in this Court and to take action with respect to those attorneys who misbehave.").

56. Here, the egregious nature of Ms. Freeman's violations and their impact on other parties' rights to an unbiased mediator and plan process warrants denial of the Fee Application in its entirety. As an experienced bankruptcy professional, Ms. Freeman is well aware of her disclosure obligations under Rule 2014, Local Rule 16.4(I), and the Employment Order, as well as her ethical obligations as an officer of this Court. She knew the impropriety that would result

from her live-in, intimate partner mediating a case in which she represented one of the parties. And yet she did nothing to inform the parties to the mediation or the Court of these facts and did not seek to withdraw from her representation as Debtors' counsel. Ms. Freeman's misconduct compromised the mediation and plan process to the discredit of this Court and the detriment of all parties.

57. To restore and to maintain the integrity of the bankruptcy system and to enforce the many retention, disclosure, and attorney conduct requirements that apply and were violated here, the Court should deny the Fee Application in full.

IV. CONCLUSION

WHEREFORE, the U.S. Trustee respectfully requests that the Court deny the Fee Application in full and grant such other relief as is just and proper.

Dated: January 29, 2024

Respectfully Submitted,

KEVIN M. EPSTEIN
UNITED STATES TRUSTEE

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CERTIFICATE OF SERVICE

I hereby certify that on January 29, 2024, a true and correct copy of the foregoing was served by electronic means via ECF transmission to all Pacer System participants in these bankruptcy cases.

/s/ Jayson B. Ruff
Jayson B. Ruff

CERTIFICATE OF CONFERENCE

I hereby certify that on January 11, 2024 and January 29, 2024, the U.S. Trustee attempted to confer with counsel for the Debtor pursuant to BLR 9013-1(g), but the parties were unable to resolve the matter. The U.S. Trustee remains open to working to resolve this Objection prior to any hearing on the Fee Application.

/s/ Jayson B. Ruff
Jayson B. Ruff

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

IN RE:	§	**Chapter 11**
	§	
IEH AUTO PARTS HOLDING LLC, *et al*.,[1]	§	**Case No. 23-90054 (CML)**
	§	
DEBTORS.	§	**(Jointly Administered)**

ORDER DENYING FIRST AND FINAL FEE APPLICATION OF THE LAW OFFICE OF LIZ FREEMAN FOR ALLOWANCE AND PAYMENT OF FEES AND EXPENSES AS CO-COUNSEL AND CONFLICTS COUNSEL TO THE DEBTORS FOR THE PERIOD FROM JANUARY 31, 2023 THROUGH JUNE 16, 2023

[Related ECF No. 991]

CAME ON for consideration the *First and Final Fee Application of the Law Office of Liz Freeman as Co-Counsel and Conflicts Counsel to the Debtors for the Period from January 31, 2023 Through June 16, 2023* [ECF No. 991] (the "Fee Application"), and the Objection of the U.S. Trustee to the Fee Application. For the reasons set forth on the record, it is hereby

ORDERED that approval of the Fee Application is **DENIED**.

[1] The Debtor entities in these chapter 11 cases, along with the last four digits of each Debtor entity's federal tax identification number, are: IEH Auto Parts Holding LLC (6529); AP Acquisition Company Clark LLC (4531); AP Acquisition Company Gordon LLC (5666); AP Acquisition Company Massachusetts LLC (7581); AP Acquisition Company Missouri LLC (7840); AP Acquisition Company New York LLC (7361); AP Acquisition Company North Carolina LLC (N/A); AP Acquisition Company Washington LLC (2773); Auto Plus Auto Sales LLC (6921); IEH AIM LLC (2233); IEH Auto Parts LLC (2066); IEH Auto Parts Puerto Rico, Inc. (4539); and IEH BA LLC (1428). The Debtors' service address is: 112 Townpark Drive NW, Suite 300, Kennesaw, GA 30144.