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**UNITED STATES DEPARTMENT OF JUSTICE**

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**TRACY HOPE DAVIS**

**UNITED STATES BANKRUPTCY COURT**  
**DISTRICT OF NEVADA**

In re:

**TELEXFREE, LLC,**☐ AFFECTS THE DEBTOR☒ AFFECTS ALL DEBTORS☐ AFFECTS TELEXFREE, INC.☐ AFFECTS TELEXFREE FINANCIAL, INC.

CASE NO. BK-S-14-12524  
Chapter 11

**[PROPOSED]****Jointly Administered with:**

14-12525-abl Telexfree, Inc.  
14-12526-abl Telexfree Financial, Inc.

Date: April 21, 2014  
Time: 1:30 p.m. (PT)

**OBJECTION OF THE UNITED STATES TRUSTEE TO DEBTORS'  
EMERGENCY APPLICATION FOR ORDER AUTHORIZING THE  
EMPLOYMENT OF KURTZMAN CARSON CONSULTANTS LLC AS  
CLAIMS AND NOTICING AGENT FOR DEBTORS**

To the Honorable August B. Landis, United States Bankruptcy Judge:

Tracy Hope Davis, United States Trustee for Region 17, hereby files her objection (the  
"Objection") to *Debtors' Emergency Application For Order Authorizing the Employment of*



1 *Kurtzman Carson Consultants LLC as Claims and Noticing Agent for Debtors* (the  
 2 “Application”) [Docket Nos. 16, 17 and 42] filed by Telexfree, LLC, Telexfree, Inc. and  
 3 Telexfree Financial, Inc. (collectively, “Debtors”) and respectfully requests that the Application  
 4 be denied.  
 5

6 In support the United States Trustee states the following:

7 **MEMORANDUM OF POINTS AND AUTHORITIES**

8 **BACKGROUND FACTS**

9 1. Debtors commenced this case by filing voluntary petitions under Chapter 11 of  
 10 title 11 of the United States Code, 11 U.S.C. §§ 101-1532 (as amended, the “Bankruptcy Code”)  
 11 on April 13, 2014. [Docket No. 1; *see also In re Telexfree, Inc.*, Case No. 14-12525-ABL  
 12 (“Telexfree Inc. Case”), Telexfree Inc. Case, Docket No. 1; *see also In re Telexfree Financial,*  
 13 *Inc.*, Case No. 14-12526-ABL (“Telexfree Financial Case”), Telexfree Financial Case, Docket  
 14 No. 1.]  
 15

16 2. On April 13, 2014, Debtors filed a motion to jointly administer the Debtors’ cases  
 17 with *In re Telexfree, LLC*, Case No. 14-12524-ABL as the proposed lead case. [See Docket No.  
 18 4.] At a hearing on April 17, 2014, the Court granted the motion for joint administration on an  
 19 interim basis and set a final hearing on the joint administration motion for May 2, 2014. [See  
 20 Declaration of Edward M. McDonald Jr., dated April 21, 2014 (“McDonald Declaration”).]  
 21

22 3. On April 14, 2014, Debtors filed the Application, which is supported by the  
 23 Declaration of Evan J. Gershbein. [See Docket Nos. 16 & 17.]  
 24

25 4. The Application seeks entry of an order employing Kurtzman Carson Consultants  
 26 LLC (“KCC”) “*nunc pro tunc* to the Petition Date as the claims and noticing agent in Debtors’  
 27 Chapter 11 Cases, pursuant to 28 U.S.C. § 156(c) and Bankruptcy Rule 2002, as provided in the  
 28

Application, on the terms and conditions set forth in the Engagement Agreement, and consistent with the Guidelines governing claims agents issued by the Bankruptcy Court in this District.”

[See Docket No. 16-1, p. 2 of 4; ¶ 2 (emphasis added).]

5. On April 18, 2014, Debtors filed an Amended Declaration of Evan J. Gershbein that attached KCC’s fee structure as Exhibit 2 thereto. [See Docket No. 42, p. 1 of 6; footnote 1.]

6. On April 18, 2014, the Court entered an order setting the hearing on the Application for April 21, 2014 at 1:30 p.m. Any opposition to the Application must be filed and served by that date and time. [See Docket No. 45, p. 2 of 2.]

7. Portions of the copy of the Engagement Agreement that was filed with the Gershbein Declaration and Amended Gershbein Declaration are illegible, including the section concerning limitations on the liability of and indemnification of KCC. [See Docket No. 17-1, p. 2 of 9; § I(E); *see also* Docket No. 17-1, p. 6 of 9; § IX(A); *see also* Docket No. 42-1, p. 2 of 13; § I(E); *see also* Docket No. 42-1, p. 6 of 13; § IX(A).]

8. The Application seeks permission to compensate KCC pursuant to the Engagement Agreement and Fee Structure:

The fees to be charged by KCC in connection with these Chapter 11 Cases are set forth in the Engagement Agreement. The Debtors propose that the cost of KCC's services be paid from the Debtors' estates as provided by 28 U.S.C. § 156(c) and 11 U.S.C. § 503(b)(1)(A). Debtor respectfully submits that KCC's rates for its services in connection with the notice, claims processing, and solicitation services are competitive and comparable to the rates charged by their competitors for similar services.

[Docket No. 16, p. 12 of 13; ¶ 28 (emphasis added); *see also* Docket No. 42-1, pp. 1-13 of 13.]

1           9.       The Engagement Agreement provides that KCC's fees and expenses shall be paid  
2 as administrative expenses. [See Docket No. 17-1, pp. 3-4 of 9; § II(F); *see also* Docket No. 42-  
3 1, pp. 3-4 of 13; § II(F).]

4           10.      KCC has also received a \$ 350,000 retainer. [See Docket No. 17-1, p. 4 of 9; §  
5 II(G); *see also* Docket No. 42-1, p. 4 of 13; § II(G).]

6           11.      The Engagement Agreement also provides that KCC and the Debtors' are  
7 independent contractors of each and that no employment relationship exists because of the  
8 Engagement Agreement. [See Docket No. 17-1, p. 7 of 9; § XI; *see also* Docket No. 42-1, p. 7  
9 of 13; § XI.]  
10

11           12.      The Engagement Agreement provides that KCC may open accounts as an agent  
12 for the Debtors:  
13

14                   At the Company's request, KCC shall be authorized to establish  
15 accounts with financial institutions in the name of and as agent for  
16 the Company.

17 [See Docket No. 42-1, p. 6 of 13; § VIII; *see also* Docket No. 17-1, p. 6 of 9; § VIII.]

18           13.      The Application provides that Debtors and KCC may agree to expand the scope  
19 of KCC's services with a corresponding increase in fees. The Application does not provide for  
20 Court approval of any change to the scope of KCC's services. [See Docket No. 16, p. 9 of 13; ¶  
21 18; *see also* Docket No. 17, p. 2 of 6; ¶ 5; *see also* Docket No. 42, pp.2-3 of 6; ¶ 5.]  
22

23           14.      KCC can terminate the Engagement Agreement with a 30 day notice to the  
24 Debtors. [See Docket No. 17-1, p. 5 of 9; § VI-A; *see also* Docket No. 42-1, p. 5 of 13; § VI-A.]  
25 The Engagement Agreement does not appear to require Court approval before KCC may  
26 terminate the Engagement Agreement. [See Docket No. 17-1; *see also* Docket No. 42-1, pp. 2-9  
27 of 13.]  
28

1           15.     The Application provides:

2                     The Debtors request authorization to compensate KCC on a  
3                     monthly basis, in accordance with the terms and conditions set  
4                     forth in the Engagement Agreement, upon KCC's submission to  
5                     the Debtors of invoices summarizing in reasonable detail the  
6                     services rendered and expenses incurred in connection with  
7                     services provided by KCC to the Debtors.

8           [Docket No. 16, p. 12 of 13; ¶ 29.]

9           16.     The Application also provides:

10                    The Debtors request the Court enter an order, pursuant to 28  
11                    U.S.C. 156(c), Bankruptcy Rule 2002, and the Guidelines,  
12                    authorizing the retention and employment of KCC as Debtors'  
13                    claims and noticing agent in the Chapter 11 Cases. The Debtors  
14                    respectfully submit that the fees and expenses that would be  
15                    incurred by KCC under the Engagement Agreement would be  
16                    administrative in nature and, therefore, should not be subject to  
17                    standard fee application procedures of professionals.

18           [See Docket No. 16, p. 5 of 13; ¶ 15 (emphasis added).]

19           17.     The Engagement Agreement also provides that KCC and the Debtors' are  
20                    independent contractors of each and that no employment relationship exists because of the  
21                    Engagement Agreement. [See Docket No. 17-1, p. 7 of 9; § XI; *see also* Docket No. 42-1, p. 7  
22                    of 13; § XI.]

23           18.     The Engagement Agreement also provides that KCC shall be entitled to attorney's  
24                    fees, court costs and other expenses if it prevails in any legal action to enforce the Engagement  
25                    Agreement. [See Docket No. 17-1, p. 8 of 9; § XVIII; *see also* Docket No. 42-1, p. 8 of 13; §  
26                    XVIII.]

27           19.     At the hearing on the first day motions on April 17, 2014, the Court expressed  
28                    concern regarding actions already taken by KCC in these cases and stated that the Court would  
29                    review any KCC fees that may be related to those actions. [See McDonald Declaration.]

20. The United States Trustee requests that the Court take judicial notice of the pleadings and documents filed in this case pursuant to FED. R. BANKR. P. 9017 and FED. R. EVID. 201. To the extent that this Objection contains factual assertions predicated upon statements made or documents filed by the Debtors, KCC, or their agents or representatives, the United States Trustee submits that such factual assertions are supported by admissible evidence in the form of admissions of a party opponent under FED. R. BANKR. P. 9017 and FED. R. EVID. 801(d) (2).

21. The United States Trustee requests that the Court take judicial notice of a case currently pending in the District of Massachusetts entitled *Securities and Exchange Commission v. Telexfree, Inc. et al*, Case No. 1:14-cv-11858-DJC (D. Mass. filed Apr. 15, 2014) (the “S.E.C. Action”).

### ARGUMENT

22. It is important to note that the court may “issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.” 11 U.S.C. § 105 (a). In addition “[n]o provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, *sua sponte*, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.” *Id.*

23. In addition, four principles for Courts to consider with regard to first day motions are:

First, the requested relief should be limited to that which is minimally necessary to maintain the existence of the debtor, until such time as the debtor can affect appropriate notice to creditors and parties in interest. In particular, a first day order should avoid substantive rulings that irrevocably determine the rights of parties.

Second, first day orders must maintain a level of clarity and simplicity sufficient to allow reasonable confidence that an order will effect no unanticipated or untoward consequences.

Third, first day orders are not a device to change the procedural and substantive rights that the Bankruptcy Code and Rules have established. In particular, first day orders should provide no substitute for the procedural and substantive protections of the plan confirmation process.

Fourth, no first day order should violate or disregard the substantive rights of parties, in ways not expressly authorized by the Bankruptcy Code.

*In re The Colad Group, Inc.*, 324 B.R. 208, 213-14 (Bankr. W.D.N.Y. 2005).

24. The Application proposes that KCC perform, pursuant to 28 U.S.C. § 156(c), certain duties usually performed by the Clerk. [Docket No. 16, p. 4 of 13; ¶ 12.] That section of the U.S. Code provides:

§156. Staff; expenses

....

(c) Any court may utilize facilities or services, either on or off the court's premises, which pertain to the provision of notices, dockets, calendars, and other administrative information to parties in cases filed under the provisions of title 11, United States Code, where the costs of such facilities or services are paid for out of the assets of the estate and are not charged to the United States. The utilization of such facilities or services shall be subject to such conditions and limitations as the pertinent circuit council may prescribe.

28 U.S.C. § 156(c) (emphasis added).

25. The Bankruptcy Noticing Center (“BNC”) is the organization established by the Administrative Office of the U.S. Courts to assist in preparation and service of routine bankruptcy notices. *See* website of the United States Bankruptcy Court, District of Nevada,

1 <http://www.nvb.uscourts.gov/electronic-case-filing/resources-documentation/electronic->  
2 [bankruptcy-noticing/](http://www.nvb.uscourts.gov/electronic-case-filing/resources-documentation/electronic-bankruptcy-noticing/) (last visited April 18, 2014). The BNC provides noticing services for  
3 hearings and the entry of orders for Office of the United States Trustee. [See McDonald  
4 Declaration.]  
5

6 26. Because the BNC was established by and is a function of the United States  
7 Courts, if KCC is employed pursuant to 28 U.S.C. § 156(c), KCC should provide noticing  
8 services to the same entities served by BNC, including the Office of the United States Trustee.  
9

10 27. Because Application seeks Court approval to employ KCC pursuant to, *inter alia*,  
11 the terms of the Engagement Agreement, the Application should not be approved until Debtors  
12 file a legible copy of the Engagement Agreement.

13 28. Although the Application asserts that the KCC's Fee Structure is competitive and  
14 comparable to the rates charged by their competitors for similar services, neither of the  
15 Gershbein declarations provide evidence to support this assertion. [See Docket Nos. 17-1 & 42-  
16 1.] The Application, including the Fee Structure, should not be approved until Debtors provide  
17 evidence that the proposed Fee Structure is competitive and comparable to the rates charged by  
18 KCC's competitors for similar services.  
19

20 29. In addition, the Application provides that Debtors and KCC may agree to expand  
21 the scope of KCC's services with a corresponding increase in fees. However, neither the  
22 Application, supporting declarations, Engagement Agreement or Fee Structure provide an  
23 explanation of how the Fee Structure will increase if KCC's scope of services are expanded. The  
24 Application should not be approved until Debtors provide this information.  
25

26 30. To the extent that the Application is approved, KCC should only be employed  
27 pursuant to 28 U.S.C. § 156(c). Any services to be provided by KCC outside of the context of  
28



1 28 U.S.C. § 156(c) should be subject to an application for employment pursuant to 11 U.S.C. §  
2 327.

3 31. The priority of KCC's compensation should be limited to only that amount that  
4 KCC is entitled to pursuant to 11 U.S.C. § 507.

5 32. Because KCC's employment is being approved pursuant to Court order and will  
6 perform certain services normally performed by the Clerk, a change in the scope of KCC's  
7 services and or the withdrawal of KCC as Noticing Agent should be subject to Court approval.

8 33. Emergency motions allowing the Debtors to make payments or utilize funds were  
9 continued by the Court and/or made subject to any temporary restraining order currently  
10 enjoining Debtors in other actions, including the S.E.C. Action. [See McDonald Declaration.]  
11 The Application should be denied because it allows Debtors to use KCC as an agent to establish  
12 financial accounts for the Debtors.

13 34. The Application seeks permission for the Debtors to compensate KCC on a  
14 monthly basis without KCC being subject to the standard fee application procedures of  
15 professionals. However, the Court has already expressed both a concern regarding actions KCC  
16 has taken in these cases and a desire to review KCC's fees. Accordingly, if the Court grants the  
17 Application, KCC should be required to provide interim invoices to any official committee  
18 appointed in these cases and to the United States Trustee, to file a final application for approval  
19 of fees, and hold in trust twenty percent of its fees so that any fees ordered by the Court to be  
20 disgorged are readily available.

21 35. In the event that KCC must seek employment under 11 U.S.C. § 327 for duties  
22 outside the context of 28 U.S.C. § 156(c), Section XI of the Engagement Agreement, which  
23 provides that KCC is an independent contractor that is not employed by the Debtors, will be  
24

1 inconsistent with KCC's fiduciary duties as a retained professional. Therefore Section XI should  
2 be removed from the Engagement Agreement or the Application should make clear that this  
3 section of the Engagement Agreement shall not apply if KCC ultimately must be employed  
4 pursuant to 11 U.S.C. § 327.  
5

6 36. The retainer amount obtained by KCC should be drawn down and not be held as  
7 an evergreen retainer.

8 37. The section of the Engagement Agreement that grants KCC attorney's fees and  
9 costs should be stricken. KCC's compensation should be limited to the reasonable fees and costs  
10 for the services it performs.  
11

12 38. For the reasons set forth herein, the Court should deny the Application, or at a  
13 minimum should grant it on an interim basis pursuant to the changes suggested herein.

14 **WHEREFORE**, the United States Trustee requests that the Court enter an order denying  
15 the Application and granting such other and additional relief as is just and equitable.  
16

17 Dated: April 21, 2014

18 **TRACY HOPE DAVIS**  
19 **UNITED STATES TRUSTEE, REGION 17**

20 By: /s/J. Michal Bloom  
21 J. Michal Bloom, Esq.  
22 Attorney for the United States Trustee  
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