SDTX Bankruptcy Bench Bar Conference

Independent Directors

April 28, 2026

Appointment of Independent Directors

Common Scenarios

- Need for director with restructuring expertise
- Lender or creditor group request
- Special committee investigation needed for insider transactions or other prepetition activities
- Intercompany conflicts

Selection of Independent Directors

Guidelines

- Plan sufficiently in advance of any chapter 11 process or other restructuring transaction
- Compile a list of potential candidates, review CVs and conduct interviews
- Focus on transparency and merits of candidates
- Encourage debate among existing board members
- Consider appointing multiple directors (discussion of special committees to follow)
- Keep in mind that combination of independence and expertise is the key value proposition

How is Independence Determined?

- No Bright Line Test in Bankruptcy
  - Bankruptcy Code does not set out a specific standard for director independence.
  - NYSE and Nasdaq independence guidelines are helpful reference points.
    - Under the NYSE, an “independent director” is one whom the board “affirmatively determines” has no “material relationship” with the company.
    - Under Nasdaq, it is one who has no relationship that would “interfere with the exercise of independent judgment” (Nasdaq Rule 5605(a)(2)).
    - Both exchanges apply “bright-line” disqualification tests (e.g., no employment within last 3 years, no compensation over $120,000, no auditor relationships) as well as a subjective overall assessment. Stock ownership alone is not disqualifying under either exchange.

How is Independence Determined?

- Case Law Guidance
  - Some states, such as Delaware, engage in a heavily fact-specific analysis, considering not only traditional economic conflicts but also relationships which may be perceived as bias producing.
  - Courts have scrutinized personal relationships, co-ownership of unique assets, overlapping business ties, and shared philanthropic contributions. Diep v. Trimaran Pollo Partners, L.L.C., 280 A.3d 133, 152 (Del. 2022).
  - The legal standard for independence is whether the director was adequately informed and exercised independent judgment. This has been upheld consistently in case law. *See In re Maxwell Techs., Inc. Derivative Litig.*, 2014 WL 2212155, at *6 (S.D. Cal. May 27, 2014); *In re Sabine Oil*, 555 B.R. at 189.

Fiduciary Duties

Overview

- Independent directors owe the same fiduciary duties as all board members.

  Duty of care (to be informed and act with reasonable diligence)

  Duty of loyalty (to act in good faith and in the best interests of the entity and its stakeholders)

- Counsel and other independent professionals (e.g., financial advisors) often guide independent directors in restructuring scenarios, ensuring proper process and documented decision-making.
- The business judgment rule will apply to decisions of independent directors who are truly independent and exercise their duties of care and loyalty.

Critiques

Are all independents truly independent?

- Some critics argue that bankruptcy directors exhibit "auditioning bias"—performing for future engagements. There are several counters to these arguments:
  - Repeat engagement is a hallmark of expertise.
  - Fiduciary duties, independent counsel, and active judicial oversight serve as structural checks.
  - Companies with independents may be more likely to end up insolvent and without recoveries available to unsecured creditors.
- The NYSE and Nasdaq independence standards do not treat prior professional relationships as per se disqualifying. The inquiry is whether the relationship would "interfere with the exercise of independent judgment" (Nasdaq Rule 5605(a)(2)) or create a "material relationship" (NYSE § 303A.02).

Special Committees

Overview

- A special committee is a sub-group of directors, advised by professionals, organized by a company's board to carry out a specific goal.
- In the restructuring setting, a special committee, among other things, typically reviews past transactions and/or current restructuring proposals to determine how the company should react to these events.
- A board can form a special committee by issuing a delegation; for example, the board can delegate certain powers and duties to a sub-board, and, to preserve the independence of the sub-board, such delegation is non-revocable.

Special Committees

Who comprises the special restructuring committee?

- Special committees often include independent directors.
- Special committees are advised by counsel and other advisors with no prior role in the conduct under review.

Special Committees

What does a special committee do?

- General Governance: A special committee can perform any task delegated to it by the board, including governance functions for debtors in possession.
- Considering Insider Transactions: The committee provides an independent analysis of insider proposals to buy the company, provide financing to the company, purchase assets from the company, or any other insider transaction.
- Investigating Claims Against Insiders: A special restructuring committee can review and analyze the strength of potential claims, including against insiders based on recent transactions with insiders, including significant divestments, distributions of dividends, or in cases where insiders participated in restructuring negotiations with the company's creditors. They often recommend whether releases should be granted.

Special Committees

Why do companies use special committees?

- Whether the special committee is formed to review a prepetition transaction or a postpetition transaction, the committee's independent review helps to protect the integrity of the transaction.
- Because of the special committee's independence and unbiased review, the transaction can enjoy the deference afforded to a corporate decision pursuant to the business judgment rule (instead of higher standard such as entire fairness).
- Special committees often evaluate releases of company claims as part of a restructuring transaction, including insiders (officers and directors) and private equity sponsors.
- Over time, the purpose and scope of special committees have expanded to often include a delegation of authority over all restructuring related transactions and expansive decision-making power over a chapter 11 proceeding.

Special Committees

Why do companies use special committees?

- One of the important uses of a special restructuring committee—reviewing a sale to an insider or potential legal claims against an insider—requires the court to apply higher standards of proof when the proposed transaction was negotiated by insiders against insiders.
- Using a special committee protects the company's access to the deferential business judgment legal standard.
- The potential uses of special committees are nearly endless:
  - For example, a special committee can be formed for the specific purpose of protecting a foreign board from potential liability under non-U.S. law.
  - A special committee could be used for the simple purpose of adding credibility and professionalism to a closely held small business, although this may come at significant cost.

Investigations by Independent Directors/Special Committees

Scope is critical

- Written scope that outlines the boundaries and expectations of the investigation

- Types of investigations
  - Investigation of estate claims against Directors & Officer
  - Investigation of intercompany/related party claim
  - Investigation of claims against third parties

- Determination of the timeline is important

Investigations by Independent Directors/Special Committees

Documentation of the Investigation

- Document Requests to Debtor, Related Parties and Third Parties
- Interviews
- Additional requests

Final Work Product

- Full written report
- PowerPoint presentation
- Oral presentation

Investigations by Independent Directors/Special Committees

Privilege

- Special committee holds its own privilege and controls when it is disclosed.
  - *United States Sec. & Exch. Comm'n v. Leibowitz*, 2025 WL 3763814, at *9 (S.D.N.Y. Dec. 30, 2025); *In re BCE West, L.P.*, 2000 WL 1239117, at *2 (S.D.N.Y. Aug. 31, 2000); *In re Vioxx Prods. Liability Litig*., 2007 WL 854251, at *4 (E.D. La. Mar. 6, 2007) (finding that materials underlying a publicly-disclosed report from counsel to a special committee constituted protected attorney work product).

- Rationale for separate privilege is that special committees are typically formed because one or more directors has a conflict of interest or an interest adverse to the corporation and are tasked with mandates such as negotiating an interested transaction or conducting an internal investigation.
  - See, e.g., *In re CBS Corp. Stockholder Class Action & Derivative Litig.*, 2021 WL 268779, at *39 (Del. Ch. Jan. 27, 2021); *City of Tamarac Firefighters' Pension Tr. Fund v. Corvi*, 2019 WL 549938, at *2 (Del. Ch. Feb. 12, 2019).

Investigations by Independent Directors/Special Committees

Privilege

- Communications between a board and the independent committee (or its counsel) ***may*** be privileged.
  - *BCE West, L.P.*, 2000 WL 1239117, at *2; *see also In re Vioxx Prods. Liability Litig*., 2007 WL 854251, at *4 (E.D. La. Mar. 6, 2007) (finding that materials underlying a publicly-disclosed report from counsel to a special committee constituted protected attorney work product)
  - *Ryan v. Gifford,* 2008 WL 43699 (Del. Ch. Jan. 2, 2008) (special committee waived its attorney-client privilege when it disclosed its detailed findings in a meeting attended by the full board of directors)
  - *In Re Rhodium Encore LLC and Air HP LLC*, No. 24-90448 (ARP) (Bankr. S.D. Tex.) (parties seeking discovery regarding a special committee's investigation into potential estate causes of action "get to discover all of the facts that [the special committee] relied on and their conclusions, but the legal analysis as to how they got from the facts to the conclusion, that generally is privileged.")

Investigations by Independent Directors/Special Committees

Testimony by Independent Directors

- Credibility is key
- Disclosure of the investigation
- Discussions with counsel
- Recommendation – timing in the process is important