

**VOLUME 2: CHAPTER 7 CASE ADMINISTRATION**

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**VOLUME 2: CHAPTER 7 CASE ADMINISTRATION****CHAPTER 2-1: THE TRUSTEE PANEL AND TRUSTEE APPOINTMENTS****2-1.1 ESTABLISHMENT OF THE CHAPTER 7 PANEL**

The United States Trustee<sup>1</sup> is authorized by law to establish a panel of private trustees. 28 U.S.C. § 586. Members of the panel are appointed by the United States Trustee to serve as interim trustees in chapter 7 cases. 11 U.S.C. § 701(a)(1)<sup>2</sup>.

The United States Trustee determines the composition of the panel and may change the size of the panel. In determining the optimum size, the United States Trustee should consider the primary goals of ensuring the prompt, competent, and complete administration of chapter 7 cases and the fair and equitable distribution of case assignments. The United States Trustee, contemporaneously with the reappointment of panel members, should examine the panel and determine if a change in size and composition of the panel is warranted.

The size of the panel is largely determined by the number of chapter 7 filings in an area, but geography and other local factors can also influence panel size. The United States Trustee should make every reasonable effort to ensure panel size allows each trustee adequate time to comply with the trustee's duties in each case. The United States Trustee should also maintain the panel in a reasonable size to allow proper supervision with our limited resources. The case load should be of a size to motivate the trustee and encourage the liquidation of assets. The United States Trustee should avoid any appearance that membership is being limited simply to guarantee the trustees' level of compensation. Providing increased diversity among the panel is also a valid consideration in determining panel size. The United States Trustee should periodically review the size of the panel and the filing statistics to see if a change is warranted.

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<sup>1</sup>All references to the United States Trustee shall include the United States Trustee's designee, unless otherwise indicated.

<sup>2</sup>All statutory references herein refer to the Bankruptcy Code, 11 U.S.C. § 101 et seq., unless otherwise indicated.

2-1.2

**RECRUITMENT AND ADVERTISEMENT**

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The United States Trustee maintains and conducts an open system for the solicitation of persons interested in serving on the panel of trustees. The United States Trustee should actively encourage broad representation among trustees. To accomplish this goal, the United States Trustee should meet and speak with culturally diverse organizations and community groups to remove real or perceived barriers to participating in the bankruptcy process and to broaden the awareness of opportunities the system affords.

To fill a vacancy on the panel or to expand the panel, the United States Trustee should forward an advertisement and solicitation package to the Office of Review and Oversight. The solicitation package includes a proposed notice, a list of non-traditional contacts or sources in the community, and a description of proposed outreach efforts to encourage a diverse pool of applicants. The Program has adopted standard public vacancy notices to attract a diverse pool of qualified applicants. All advertisements must conform to these notices, which may be obtained from the Office of Review and Oversight. See Appendix 2-1 for the current version (7/27/99) of the vacancy notice.

The United States Trustee sends a copy of the advertisement along with a list of proposed publications to the Office of Review and Oversight for review and suggestions. Upon a determination by the United States Trustee and after review by the Office of Review and Oversight, the Administrative Officer, or such other person as the United States Trustee shall designate, will place the advertisement with the various publications. The Office of Review and Oversight will also send a copy of the vacancy announcement to various national organizations. Local posting of announcements is handled by the United States Trustee. The United States Trustee will also provide information concerning the vacancy to any local professional groups for notice to their membership where possible. All appointments for panel membership are to be advertised for a reasonable period of time.

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The United States Trustee must follow the advertising policy set forth herein and avoid making a selection without fully advertising and noticing the opening. If a new vacancy occurs within a reasonably short period of time after the advertisement and posting of a vacancy, the United States Trustee may use that notice to replace the additional vacancy, provided that the information of the previous notice is accurate for the new vacancy. If more than twelve (12) months have passed, the United States Trustee must re-advertise the vacancy. The United States Trustee may re-advertise sooner, if deemed necessary.

### 2-1.3 **QUALIFICATIONS FOR CHAPTER 7 PANEL MEMBERSHIP**

The United States Trustee should actively encourage talented, qualified persons, who need not be attorneys, to apply for panel membership. Particular efforts should be made to appoint qualified female and minority applicants. The applicant must possess all of the qualifications established by the Attorney General of the United States under 28 U.S.C. § 586(d) and published at 28 C.F.R. § 58.3. Panel members must also be able to satisfy the eligibility requirements of § 321 for serving in a case. Anyone who was employed by the United States Trustee Program within the preceding one-year period is not eligible for appointment. 28 C.F.R § 58.3. Prior to appointment, each person must be interviewed and informed of the performance expected, as well as the method by which that person will be assigned cases.

#### 2-1.3.1 **Qualifications for Panel Membership, 28 C.F.R. § 58.3**

The minimum qualifications for membership on the panel are set forth in 28 C.F.R. § 58.3.

To qualify for panel membership, the applicant must:

1. possess integrity and good moral character;
2. be physically and mentally able to satisfactorily perform a trustee's duties;
3. be courteous and accessible to all parties with reasonable inquiries or comments about a case for which such individual is serving as trustee;
4. be free of prejudices against any individual, entity, or group of individuals which would interfere with unbiased performance of a trustee's duties;
5. not be related by affinity or consanguinity within the degree of first cousin to any employee of the Executive Office or to any employee of the Office of the United States Trustee for the district in which he/she is applying;
6. be either:
  - a. a member in good standing of the bar of the highest court of a state or of the District of Columbia;
  - b. a certified public accountant;



- c. a college graduate with a bachelor's degree from a full four year course of study (or the equivalent) of an accredited college or university (accredited as described in Part II, Section III of Handbook X118 promulgated by the U.S. Office of Personnel Management), with a major in a business-related field of study or at least 20 semester hours of business-related courses, or hold a master's degree or doctorate degree in a business-related field of study from a college or university of the type described above; or
  - d. a senior law student or candidate for a master's degree in business administration recommended by the relevant law school or business school dean and working under the direct supervision of:
    - (1) a member of a law school faculty;
    - (2) a member of the panel of private trustees; or
    - (3) a member of a program established by the local bar association to provide clinical experience as deemed acceptable by the United States Trustee.
7. be willing to provide reports as required by the United States Trustee; and
8. have submitted an application under oath, in the form prescribed by the Director of Executive Office for United States Trustees, to the United States Trustee for the district in which appointment is to be made.

### 2-1.3.2 **Eligibility to Serve in a Case, § 321**

In addition to considering qualifications for panel membership, the United States Trustee should ascertain a candidate's general eligibility to serve in cases. Eligibility requirements are set forth in § 321. Specifically, a trustee must be (1) competent to perform the duties of a chapter 7 trustee, (2) reside or have an office in the district where the cases are pending or in an adjacent district, and (3) be an individual or a corporation authorized by corporate charter or by-laws to act as a trustee.

While corporations are eligible under § 321 for appointment as interim trustees in specific cases, each individual in a corporation who performs the duties of a trustee must individually satisfy the requirements of 28 C.F.R. § 58.3. In view of the fiduciary duties of the trustee, the responsibility of the individual trustee to

preside at section 341 meetings, possible complications as to coverage under blanket or separate bonds, and possible increases in expenses imposed on estates, corporate entities are rarely appointed. The regulation provides that no professional corporation, partnership, or similar entity organized for the practice of law or accounting is eligible for appointment as a chapter 7 trustee.

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## 2-1.4

### **APPOINTMENT TO THE PANEL**

#### 2-1.4.1

##### **The Initial Appointment**

When the United States Trustee selects a person for appointment to the panel, a security package must be completed and forwarded by facsimile or overnight mail to the Office of Review and Oversight for initial review. After the United States Trustee has confirmed with the Executive Office that the applicant's background investigation package is complete and suitable<sup>3</sup>, the appointment is prepared by the United States Trustee in the form prescribed by the Executive Office for United States Trustees. See Appendix 2-2 for the current (7/27/99) initial appointment form. If the United States Trustee cannot issue the appointment because of a conflict, the appointment will be issued by the Executive Office and signed by the Deputy Director.

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The Office of Review and Oversight retains a copy of all applications and maintains a roster of all panel members. That office must be notified of any change of name or address of a panel member and of any resignation, removal, or suspension of a member. This information is used to update the Program's web site as well the chapter 7 trustee master database.

#### 2-1.4.2

##### **Security Clearances**

The appointment of a panel trustee is subject to completion of a satisfactory background investigation, which includes a name and fingerprint check and a report on credit history. The proposed appointee must submit an employment application, Form SF-85P (Questionnaire for Public Trust Positions), Form DOJ-488B (Tax Check Waiver), two sets of Form USDOJEOTZ (Fingerprint Cards), Form I-9 (Employment Eligibility Verification), and Form DOJ-555(a) (Disclosure and Authorization pertaining to Consumer Reports Pursuant to the Fair Credit Reporting Act, 15 U.S.C. § 1681) to the United States Trustee. After

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<sup>3</sup> In most cases the trustee is appointed without waiting for the results of the background check, which may take months to complete.

the United States Trustee has reviewed the documents for completeness and accuracy, they should be transmitted to the Office of Review and Oversight for final processing. Upon acceptance of the forms, the applicant may be appointed, conditioned on the completion of a satisfactory background investigation. The Office of Review and Oversight will notify the United States Trustee of any background information that requires additional clarification by the trustee. The resolution of questionable information may require an affidavit by the applicant or other clarification.

Panel trustees are subject to reinvestigation every five years or the United States Trustee may request a reinvestigation earlier, if there is a valid reason.

#### 2-1.4.3 **Term of Appointment**

All panel members are generally appointed for one-year renewable terms. The appointment may be for less than one year. Short-term appointments are often used to adjust a trustee's renewal appointment date or as a compliance measure. Service during the term and the renewal of the appointment are at the discretion of the United States Trustee, subject to the "Procedures for Suspension and Removal of Panel Trustees and Standing Trustees" 28 C.F.R. § 58.6 ("Administrative Procedures"). See Appendix 2-5.

#### 2-1.4.4 **Renewal of Appointment**

At least sixty (60) days before the expiration of the trustee's term, the United States Trustee should review the trustee's performance and other factors in determining whether to reappoint the trustee. If the United States Trustee decides to renew the appointment, the United States Trustee will provide written notice of the decision to reappoint to the Assistant Director for Review and Oversight, by facsimile or overnight mail, at least a week prior to the expiration of the trustee's appointment. If a performance review has not been sent to the Office of Review and Oversight within the preceding twenty-four (24) months, the United States Trustee should also include the summary and conclusion pages of the most recent trustee performance review or the entire performance review, if it contains any "adequate, except for" or "inadequate" ratings. If no concerns are raised or no response is transmitted by the Office of Review and Oversight within five business days of receipt, the United States Trustee may forward the renewal appointment to the trustee. A copy of the appointment should be sent to the Assistant Director.

The renewal appointment is prepared by the United States Trustee in the form prescribed by the Executive Office for United States Trustees. See Appendix 2-3 for the current (7/27/99) renewal appointment form. If the United States Trustee cannot issue the appointment because of a conflict, the appointment will be issued by the Executive Office and signed by the Deputy Director.

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The trustee performance review does not have to be prepared in conjunction with the reappointment process. The United States Trustee may use a performance review completed within the twenty-four (24) month period preceding the renewal appointment. See USTM 2-3.17 for information on the performance review process. The United States Trustee must comply with the Administrative Procedures in the event a decision is made not to reappoint the trustee. The assignment of cases shall continue until terminated under the Administrative Procedures.

#### 2-1.4.5 **Non-Reappointment**

The United States Trustee shall notify the panel trustee in writing of any decision not to renew the trustee's appointment. The notice shall state the reasons for the decision and should refer to, or be accompanied by copies of, pertinent materials upon which the United States Trustee has relied and any prior communications in which the United States Trustee has advised the trustee of the potential action. The notice must be sent to the office of the trustee by overnight courier, for delivery the next business day. The United States Trustee should review the Administrative Procedures and consult with the Assistant Director for Review and Oversight before taking this action to make sure that the notice and reasons are in compliance. The trustee's appeal rights upon notice of non-renewal may extend the trustee's case assignments unless an interim directive is issued by the United States Trustee.

#### 2-1.4.6 **Training**

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The United States Trustee should develop a training program for new trustees and provide training to all new panel trustees. New trustees should receive thorough training on the *Handbook for Chapter 7 Trustees* ("Handbook") and be familiar with the duties of a trustee and the United States Trustee's reporting requirements before being assigned cases. Assigning a mentor for new trustees and allowing a new trustee to observe and talk to panel veterans will aid in acclimating the new trustee. As part of the training process, the United States Trustee should make every effort to attend the trustee's first section 341 meetings to provide onsite training and assistance. The United States Trustee should consider assigning the

new trustee a reduced case load during the initial learning process. The United States Trustee should meet with a new trustee periodically during the first year to review case administration, reporting, internal controls, and other matters of concern to the United States Trustee or the trustee.

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The United States Trustee also should provide ongoing training for trustees in the following areas:

1. United States Trustee policies and procedures, e.g., preparation of no-asset reports, final reports, final accounts, and 180-day reports;
2. bankruptcy fraud and abuse to include the identification and reporting of potential bankruptcy crimes;
3. bond and bank depository requirements;
4. internal accounting controls and the prevention of defalcation of estate funds;
5. legal issues encountered by trustees;
6. securing and liquidating assets;
7. conducting a section 341 meeting;
8. ethical standards for trustees, including conflicts of interest and the appropriate declination of cases;
9. diversity; and
10. other requirements of the Handbook.

The United States Trustee should have at least four hours of training per year for panel trustees in one or more sessions. This training often qualifies for continuing education credit, and the United States Trustee may wish to investigate this possibility. In conducting this training, outside presenters and trustees may provide practical information and are usually well received.

#### 2-1.5

#### **APPOINTMENT AND QUALIFICATION OF INTERIM TRUSTEES**

Section 701 of the Bankruptcy Code mandates that the United States Trustee appoint one disinterested panel member to serve as interim trustee in a chapter 7

case immediately after the order for relief. § 701(a). See USTM 2-1.6.5 regarding the appointment of an interim trustee in an involuntary case.

To qualify to serve, the trustee must furnish a bond in favor of the United States that is conditioned on the faithful performance of the trustee's duties. § 322. Unless the United States Trustee directs otherwise, a panel trustee covered by a regional or district blanket bond does not have to file a separate bond in each case. See USTM 2-3.10 for bonding requirements.

The interim trustee serves until a trustee is elected under § 702 and qualifies under § 322. If no trustee is elected, then the interim trustee becomes the trustee under § 702(d). The interim trustee has all the duties and powers of a permanent trustee. See USTM 2-1.6.8 for Trustee Elections.

## 2-1.6 **ASSIGNMENT OF CASES**

### 2-1.6.1 **Blind Rotation**

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The United States Trustee Program seeks to appoint panel members to chapter 7 cases in a fair and equitable basis by utilizing a single, blind rotation system that includes all asset and no-asset cases. As cases are filed, they should be assigned to panel members in a manner predetermined by the United States Trustee.

A system of blind rotation avoids the appearance of favoritism and eliminates the need to make individual judgments about case assignments. Over a reasonable period of time, this system normally results in asset cases being fairly and equally distributed among the panel. Because the order of assignment is not available to the public, the "blind" rotation also reduces the likelihood that debtors can engage in "trustee shopping" – that is, timing the filing of a petition in order to have a specific trustee appointed in the case. The United States Trustee reviews the processing of chapter 7 cases periodically to evaluate the efficiency and fairness of assignment procedures.

### 2-1.6.2 **Exceptions to Rotation**

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Exceptions to the blind rotation system may be warranted on occasion. Reasons that warrant such exceptions include:

1. the unique characteristics of a specific case;

2. the goal of achieving equity in the assignment of cases among panel members;
3. suspension of a trustee from case assignments;
4. previous service in a reopened or converted case;
5. geographic considerations; and
6. training for new panel members.

Any exception from the rotation system must be documented in the appropriate file and approved by the United States Trustee. The documentation of the exceptions to the blind rotation is made available for review upon request by a trustee or any interested party or member of the public. A suggested method of recording exceptions is for each office to keep a log of the exceptions to rotation, in addition to any memoranda regarding the individual cases.

### 2-1.6.3 **Notice and Acceptance of the Appointment**

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Interim trustees are sent a notice of appointment. A panel member who is covered by a regional or district blanket bond is deemed to have accepted the appointment unless the appointment is rejected within five days after receipt of the notice. If a trustee cannot accept the appointment, e.g., where the trustee has a conflict of interest or was an examiner in the case, then the trustee must expressly reject the appointment. Fed. R. Bankr. P. 2008.

A trustee is expected to accept all cases assigned, unless there is a conflict of interest or other extraordinary circumstance.

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If the person selected is not covered by a regional or district blanket bond<sup>4</sup>, the trustee shall notify the court and the United States Trustee in writing of acceptance within five days after receipt of the notice of selection or shall be deemed to have rejected the appointment. If applicable, a copy of the trustee's acceptance of appointment should accompany the notice of appointment, so that the form can be filed in the clerk's office.

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<sup>4</sup>Usually the panel trustees will be covered by the regional or district blanket bond, and this may only apply to elected trustees. However, there are other circumstances in which a trustee may not be covered by the regional or district blanket bond, such as a non-panel trustee who was serving in a converted case and is appointed to serve as the chapter 7 trustee.

#### 2-1.6.4 **Non-Panel Trustees in Converted Cases**

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When a case converts to chapter 7, the trustee administering the case immediately prior to conversion may be appointed by the United States Trustee to serve as the interim trustee, regardless of whether the person is a member of the chapter 7 panel. § 701(a)(1). Upon conversion of a chapter 11 case in which a trustee was serving, the United States Trustee will assess the advisability of reappointing the chapter 11 trustee to serve as the chapter 7 trustee. The United States Trustee should consider the trustee's performance as the chapter 11 trustee, including compliance with the reporting requirements, and the trustee's ability to carry out the duties of a chapter 7 trustee in the case. Appointing the chapter 11 trustee to serve in the chapter 7 case does not relieve the trustee of the reporting requirements under Fed. R. Bankr. P. 1019, and the United States Trustee should ensure that the trustee complies with this rule.

#### 2-1.6.5 **Involuntary Chapter 7 Cases**

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The United States Trustee should not appoint an interim trustee in an involuntary chapter 7 case until the order for relief is entered. However, if the court orders the appointment of a trustee pursuant to § 303(g), the United States Trustee should appoint an interim trustee in accordance with § 701. If it appears that assets are being dissipated and that an order for relief will be entered, the United States Trustee should consider moving for the appointment of an interim trustee under § 303(g), if the creditors do not.

#### 2-1.6.6 **Conflicts of Interest**

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A trustee must be knowledgeable of §§ 701(a)(1), 101(14), and 101(31), as well as any other applicable law or rules, and must decline any appointment in which the trustee has a conflict of interest or lacks disinterestedness. A trustee should have in place a procedure to screen new cases for possible conflicts of interest or lack of disinterestedness immediately upon being appointed.

If a trustee discovers an actual conflict of interest or a lack of disinterestedness after accepting the appointment, the trustee should immediately file a notice of resignation in the case. Conflict waivers by either the debtor or creditor are not effective to obviate the trustee's duty to resign.

The trustee must advise the United States Trustee immediately of any potential conflict or lack of disinterestedness so that a determination can be made as to whether the appointment of a successor trustee is necessary. The trustee should



also advise the United States Trustee immediately of any circumstances which might give rise to the appearance of impropriety.

In order to address conflicts of interest and lack of disinterestedness, the trustee must:

1. review each case assigned as soon as possible after appointment, but in any event prior to the section 341 meeting, for actual or potential conflicts and lack of disinterestedness;
2. immediately advise the United States Trustee in writing of any such actual or potential conflicts or lack of disinterestedness;
3. disclose any potential conflicts on the court record or at the section 341 meeting, or both on the court record and at the section 341 meeting; and
4. decline any appointment or immediately resign if there is an actual conflict or lack of disinterestedness.

While it is not possible to list all situations presenting an actual or potential conflict of interest or lack of disinterestedness, a non-exclusive list of examples follows:

1. Trustee represents or has represented the debtor, a creditor, an equity security holder, or an insider in other matters;
2. Debtor or creditor is an employee of the trustee or of a professional providing services to the trustee in the case;
3. Trustee is appointed to serve as trustee for a corporate debtor and for a debtor who is an insider, officer, director or guarantor of the corporate debtor;
4. The estate has a potential cause of action against the trustee, an employee of the trustee, a client of the trustee or the trustee's firm or other person or entity with whom the trustee has a business or family relationship;
5. Trustee was an officer, director, or employee of the debtor or of the debtor's investment banker within two years before the commencement of the case;

6. Trustee is a creditor or an equity security holder of the debtor;
7. Trustee had been an investment banker for a security of the debtor within three years before the commencement of the case or the trustee has represented such an investment banker in connection with the offer, sale, or issuance of a security of the debtor.

Several courts have addressed the issue of whether an actual or potential conflict of interest or lack of disinterestedness of a trustee's partner or associate may be imputed to the trustee. Therefore, the trustee should disclose to the United States Trustee all situations presenting an actual or potential conflict of interest or lack of disinterestedness for his partners or his firm.

Fed. R. Bankr. P. 2008 allows the appointment of one trustee in jointly administered cases. The existence of interdebtor claims in jointly administered cases must be examined closely because such claims do not automatically disqualify the trustee. *See, e.g., In re BH & P Inc.*, 949 F.2d 1300 (3rd Cir. 1991). However, these cases should be monitored because conflicts can develop and require the appointment of separate trustees.

In districts in which the standing chapter 13 trustee is also a panel trustee, appointment of the chapter 7 trustee in cases converted from chapter 13 should be monitored so that the chapter 13 trustee is not appointed as the chapter 7 trustee.

#### 2-1.6.7

#### **United States Trustee Serving as Case Trustee**

The provisions of 28 U.S.C. § 586(a)(2) and 11 U.S.C. § 701(a)(2) authorize the United States Trustee to serve in a case where no panel member is willing to serve. This situation should rarely occur because the *1998 Chapter 7 Initiatives* and the Handbook provide that a trustee is not to decline appointments, except for conflicts or other extraordinary circumstances. However, there may be instances, such as a trustee's resignation or possible embezzlement, in which the United States Trustee would need to serve.

If the United States Trustee serves as the case trustee, no bond is required. § 322(b)(1). Any compensation to which the United States Trustee is entitled will be paid to the clerk of the bankruptcy court and then paid into the United States Trustee System Fund. § 330(d).

## 2-1.6.8 **Election of Trustees**

### 2-1.6.8.1 **Eligibility to Request an Election and to Vote**

Creditors in a chapter 7 case may request the opportunity to elect a trustee at the section 341 meeting. The election is properly requested if creditors having 20 percent in amount of the eligible claims request the election. To request an election and to vote in an election, a creditor:

1. must hold an allowable, undisputed, fixed, liquidated, non-priority unsecured claim of a kind entitled to distribution under §§ 726(a)(2)-(4), 752(a), 766(h), or 766(i);<sup>5</sup>
2. must not have an interest materially adverse, other than an equity interest that is not substantial in relation to the creditor's interest as a creditor, to the interest of creditors entitled to distribution;
3. must not be an insider; and
4. must have "filed a proof of claim or a writing setting forth facts evidencing a right to vote pursuant to § 702(a) unless objection is made to the claim or the proof of claim is insufficient on its face." Fed. R. Bankr. P. 2003.

A candidate for trustee is elected if the candidate receives the votes of creditors holding the majority in amount of those claims voted. See § 702 and Fed. R. Bankr. P. 2003.

### 2-1.6.8.2 **Trustee Election Procedure**

If an election is requested the United States Trustee presides over the election. This eliminates the possible conflict of the interim trustee presiding while having an interest in the outcome of the election. Neither the Bankruptcy Code or Rules requires creditors to provide any advance notice of an intent to request an election.

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<sup>5</sup>Undersecured creditors may bifurcate their secured and unsecured claims for purposes of requesting an election and voting under § 702. Similarly, creditors with both liquidated and unliquidated claims may assert the liquidated portion of their claims for purposes of determining eligibility to vote for a chapter 7 trustee. See In re Klein, 119 B.R. 971, 981-82 (N.D. Ill. 1990), appeal dismissed, 940 F.2d 1075 (7<sup>th</sup> Cir. 1991).

If the creditors move to elect a trustee during the section 341 meeting without prior notice, the interim trustee adjourns the meeting and notifies the United States Trustee, who shall preside over the election then or at a later date. If the clerk of the bankruptcy court has notified creditors that no proof of claim is required in the case pursuant to Fed. R. Bankr. P. 2002(e), the United States Trustee should consider continuing the section 341 meeting and notifying the creditors of the requested election and of the need to file a proof of claim in order to participate in the election.

The following procedure is recommended. The presiding officer should note for the record:

1. the name of the case;
2. the case number;
3. the date;
4. the names of the creditors requesting an election;
5. the amount of each requesting creditor's claim, whether the claim is documented by a proof of claim or other writing, and whether a written or oral objection has been made to the claim;
6. any individual(s) representing a requesting party;
7. each nomination for trustee; and
8. whether there are any objections to the election, identifying the objector and the reason for each objection.

The next critical step is to determine the total amount of general unsecured claims eligible to vote.<sup>6</sup> For this purpose, the total amount of "Unsecured Claims Without Priority" set forth on the summary page of the debtor's schedules should

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<sup>6</sup>There is a difference of opinion as to the determination of the 20 percent threshold. One view is that only 20 percent of the claims which have actually been filed are needed. In re Lake States, 173 B.R. 642 (Bankr. N.D. Ill. 1994) leave to appeal denied, Michael v. Fisher, 185 B.R. 259 (N.D. Ill. 1995). Other cases hold there must be 20 percent of the eligible claims, regardless of whether filed at the time of election. In re Oxborrow, 104 B.R. 356 (E.D. Wash.1989), aff'd, 913 F.2d 751 (9th Cir. 1990). The United States Trustee should be familiar with the case law of the district in which the election is held.

be used. Unless an objection is raised, this total should be the basis from which to determine the 20 percent required for an election. In the absence of schedules, the debtor should provide, under oath, the amount of non-priority, unsecured claims eligible to vote.

In computing the 20 percent quorum, the United States Trustee should give due consideration to information provided by the debtor and creditors as to the unsecured portions of partially secured debts that are to be included, and to unsecured debts that must be excluded from the computation as disputed, unliquidated, due to insiders, or to one having an interest materially adverse to other creditors, as required by § 702. In any event, the methodology used in determining the total should be reported, along with any objections.

The next step in determining whether the necessary 20 percent of claims has requested an election is to identify each party requesting the election, the amount of the claims represented, and if other persons' claims are represented, assuring that an appropriate affidavit pursuant to Fed. R. Bankr. P. 2006 and supporting proxies are presented. If the presiding officer determines that the 20 percent requisite is not met, the parties are to be informed of that determination. The election process will continue so that the court will have a full report of what transpired or what would have transpired had the 20 percent requisite been met.

If there are objections or disputes that are not resolved by agreement of the parties, the parties should be informed that the election will be held subject to the right of creditors to seek resolution of the underlying dispute by the court.

The presiding officer should then proceed with the election, soliciting from the parties the names of the candidates they wish to nominate. After the nominations, the presiding officer shall hold a vote for the election of a trustee. The candidate who receives the votes of creditors holding a majority in amount of the claims voted is the elected trustee. The number of creditors voting for or against a candidate is irrelevant, because only the dollar amount of the claims is counted for voting purposes.

The final step is to report the name of the candidate receiving the most votes and to announce that the interim trustee will remain in office until the expiration of the objection period in Fed. R. Bankr. P. 2003(d) and the elected trustee has qualified. If there are any disputes or objections raised, the presiding officer should announce that the report of the United States Trustee will be delivered to the court as soon as possible following the election. Parties should also be advised that those who complete a sign-up sheet will be provided notice of the United States Trustee's report and that creditors may move, within ten days after the report is

filed<sup>7</sup>, for resolution of any election dispute by the court, as provided by Fed. R. Bankr. P. 2003(d).

The parties should also be informed that if no motion is made to resolve a dispute within the time allowed by Fed. R. Bankr. P. 2003(d), the interim trustee will become the trustee by operation of law.

When the election is concluded, the interim trustee or the United States Trustee may still examine the debtor or allow the creditors to examine the debtor. However, the United States Trustee should consider continuing the examination of the debtor until the election report is filed and any election dispute is resolved, so that the elected trustee may conduct the examination. Once all parties in interest have had an opportunity to examine the debtor, the meeting should be concluded.

#### 2-1.6.8.3 Voting by Proxy

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Voting by proxy at a section 341 meeting is permitted, provided the authority of the agent, attorney or proxy is evidenced by a power of attorney executed pursuant to Fed. R. Bankr. P. 9010(c). A proxy is a written power of attorney authorizing any entity to vote the claim or otherwise act as the owner's attorney in fact in connection with the administration of the estate. Fed. R. Bankr. P. 2006(c) states that a proxy may be solicited only in writing, and only by:

1. A creditor holding an allowable unsecured claim against the estate on the date of the filing of the petition;
2. A committee elected pursuant to § 705;
3. A committee of creditors selected by a majority in number and amount in claims of creditors (a) whose claims are not contingent or unliquidated; (b) who are not disqualified from voting under § 702(a), and (c) who were present or represented at the meeting of which all creditors having claims of over \$500 or the 100 creditors having the largest claims had at least five days notice in writing and of which meeting written minutes were kept and are available reporting the names of the creditors present or represented and voting and the amounts of their claims; or

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<sup>7</sup>A change in Fed. R. Bankr. P. 2003(c), effective 12/1/99, revised the requirement from ten days of the meeting to ten days after the election report is filed.

4. A bona fide trade or credit association, but such association may solicit only creditors who were its members or subscribers in good standing and had allowable unsecured claims on the date of the filing of the petition.

Fed. R. Bankr. P. 2006(d) prohibits solicitation (1) in any interest other than that of general creditors; (2) by or on behalf of any custodian; (3) by the interim trustee or by or on behalf of any entity not qualified to vote under § 702(a); (4) by or on behalf of an attorney at law; or (5) by or on behalf of a transferee of a claim for collection only.

Before the voting commences at the section 341 meeting, or at any other time as the court may direct, a holder of two or more proxies must file and transmit to the United States Trustee a verified list of the proxies to be voted and the verified statement required by Fed. R. Bankr. P. 2006(e) discussing the facts and circumstances surrounding the execution and delivery of each proxy. On motion of any party in interest or on its own initiative, the court may determine whether there has been a failure to comply with the provisions of Fed. R. Bankr. P. 2006 or any other impropriety in connection with the solicitation or voting of a proxy. After notice and a hearing, the court may reject any proxy for cause, vacate any order entered in consequence of the voting of any proxy which should have been rejected, or take any other appropriate action.

#### 2-1.6.8.4 Election Reports

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Whether or not there is an objection to an election, an election report must be prepared by the United States Trustee and filed with the court as soon as possible after the election. Fed. R. Bankr. P. 2003(d). If the election is undisputed, the United States Trustee should file a report of undisputed election and notify the elected trustee of his or her selection and how to qualify for office by posting the requisite bond.

If the election is disputed, the United States Trustee must file with the court a report of disputed election. The United States Trustee cannot resolve any dispute in the election process. Although Fed. R. Bankr. P. 2003(d) does not specify what facts should be contained in the report other than the fact that a dispute exists, Fed. R. Bankr. P. 2003(b)(3) states that “in the event of an objection to the amount or allowability of a claim for the purpose of voting, unless the court orders otherwise, the United States trustee shall tabulate the votes for each alternative presented by the dispute and, if resolution of such dispute is necessary to determine the result of the election, the tabulations for each alternative shall be reported to the court.” Fed. R. Bankr. P. 2007.1(b)(3)(B), which is applicable to

chapter 11 disputed elections, is instructive concerning the format of a chapter 7 report and provides that the report should inform the “court of the nature of the dispute, and listing the name and address of any candidate elected under any alternative presented by the dispute.” The report of election should be concise and objective, and all relevant documents received at the meeting should be attached as exhibits to the report.

#### 2-1.6.8.5 Disputed Elections

\_\_\_\_\_ The United States Trustee cannot resolve any dispute in the election process. The United States Trustee, as the presiding officer, must promptly inform the court in writing that a dispute exists. Pending the resolution of the dispute, the interim trustee shall continue to serve. If no motion for resolution of such election dispute is made within 10 days after the election report is filed, the interim trustee shall serve as the trustee in the case. Fed. R. Bankr. P. 2003(d).

#### 2-1.6.8.6 Qualification of Elected Trustees

\_\_\_\_\_ The elected trustee is considered qualified once the trustee has returned a notice of acceptance of election, accompanied by a bond. See § 322. Fed. R. Bankr. P. 2008 requires the United States Trustee to notify the person elected concerning how to qualify and the amount of the bond.

#### 2-1.6.8.7 Duties and Responsibilities of Elected Trustees

\_\_\_\_\_ The statutory duties of an elected trustee are the same as the duties of an interim trustee who becomes trustee by operation of § 702(d). An elected trustee must also comply with the requirements of the United States Trustee and will be requested to submit to a background investigation. If the trustee refuses to submit to a background investigation, the United States Trustee should contact the Assistant Director for Review and Oversight.

The United States Trustee may wish to provide the Handbook to the elected trustee, with a letter advising the trustee of the United States Trustee’s reporting and other requirements.

#### 2-1.7 SUCCESSOR TRUSTEES

\_\_\_\_\_ When a trustee dies, resigns, fails to qualify under § 322, or is removed from a case under § 324, the creditors have a right to elect, in the manner specified in § 702, a person to serve as successor trustee. In the event an election is requested,



the United States Trustee should call a special meeting of creditors for the purpose of electing a successor trustee. Fed. R. Bankr. P. 2003(f). Only creditors holding eligible claims may request and vote in the election. See USTM 2-1.6.8.1. The procedures set forth in § 702 must be strictly observed when electing a successor trustee. See USTM 2-1.6.8.2. Any person elected by the creditors must be eligible under § 321 to serve as trustee.

Pending the election of a successor trustee, the United States Trustee should appoint an interim trustee under § 703(b) to preserve or prevent loss to the estate. The interim trustee must be a disinterested person who is a member of the panel of private trustees established under 28 U.S.C. § 586(a)(1).

Section 703(c) provides that if creditors do not elect a successor trustee, or if a trustee is needed in a case reopened under § 350, the United States Trustee shall appoint one disinterested person that is a member of the panel of private trustees established under 28 U.S.C. § 586(a)(1) to serve as trustee in the case. This section appears to apply only if the United States Trustee has not appointed an interim trustee under § 703(b). If creditors do not elect a successor trustee *in the manner specified in § 702*, the interim trustee appointed under § 703(b) should serve as successor trustee by operation of § 702(d). If creditors elect a successor trustee under § 703(a), the services of an interim trustee appointed under § 703(b) terminate when the successor trustee qualifies under § 322.

#### 2-1.7.1 **Death of a Trustee**

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In the event a trustee dies, the United States Trustee should:

1. Appoint a successor trustee for each of the estates of the decedent trustee, § 703.
2. Ensure that the successor trustee contacts the representative of the decedent trustee's estate.
3. Ensure that the successor trustee obtains any and all books, records, and files of the decedent trustee and files a report of the administration of the estate by the decedent trustee.
4. Verify that an appropriate and timely application is made for the award of compensation and expenses to the decedent trustee's estate, and compensation and expenses to the professionals retained by the deceased trustee. See § 326(c) which limits the aggregate compensation to that

available to a single trustee. The United States Trustee should ensure that the division is fair and equitable to both the decedent trustee's estate and to the successor trustee.

5. Ensure that the successor trustee reasonably cooperates with the representative of the decedent trustee's estate.

## 2-1.8 **REOPENED CASES**

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The United States Trustee should not appoint a trustee in a reopened case unless ordered by the court. Fed. R. Bankr. P. 5010. The United States Trustee may move for the appointment or reappointment of a trustee in the reopened case if it appears necessary.

In a reopened case, the United States Trustee may appoint the successor trustee through the blind rotation, but appointing the trustee who previously served in the case is a reason for departing from the blind rotation. If the previous trustee served well in the case, the United States Trustee may wish to reappoint that person as trustee. On the other hand, if the previous trustee was not aggressive in locating assets or if there is a concern about reappointing the previous trustee, the United States Trustee may choose to use the blind rotation to appoint a trustee.

## **CHAPTER 2-2: ADMINISTRATION OF CHAPTER 7 ESTATES**

### 2-2.1 **INTRODUCTION**

Pursuant to 28 U.S.C. § 586(a), the United States Trustee must supervise the actions of trustees in the performance of their responsibilities. The principal duty of the trustee is to collect and liquidate the property of the estate and to distribute the proceeds to creditors. The trustee is a fiduciary charged with protecting the interests of the various parties in the estate.

A chapter 7 case should be administered to maximize and expedite dividends to creditors and facilitate a fresh start for the debtors entitled to a discharge. A trustee should not administer an estate or an asset in an estate where the proceeds of liquidation will primarily benefit the trustee or the professionals, or unduly delay the resolution of the case. Chapter 7 trustees must be guided by this fundamental principle when acting as trustee. Accordingly, the United States Trustee must verify that a trustee considers whether sufficient funds will be generated to make a meaningful distribution to creditors before administering a case as an asset case.

## 2-2.2

**STATUTORY DUTIES UNDER § 704**

The specific statutory duties of a trustee are set forth at § 704. The trustee shall:

1. collect and reduce to money the property of the estate and close the estate as expeditiously as is compatible with the best interests of parties in interest;
2. be accountable for all property received;
3. ensure that the debtor performs his intentions as to the retention or surrender of property of the estate that secures consumer debts;
4. investigate the financial affairs of the debtor;
5. if a purpose would be served, examine proofs of claims and object to the allowance of any claim that is improper;
6. if advisable, oppose the discharge of the debtor (but not the discharge of a particular debt since only the creditor to whom it is owed may do so);
7. unless the court orders otherwise, furnish such information concerning the estate and the estate's administration as is requested by a party in interest;
8. if the business of the debtor is authorized to be operated, file with the court and with any governmental unit charged with the responsibility for collection or determination of any tax arising out of such operations, periodic reports and summaries of the operation of such business, including a statement of receipts and disbursements, and such other information as the court or the United States Trustee requires; and
9. make a final report (TFR) and file a final account (TDR) of the administration of the estate with the United States Trustee and the court.

Section 323(a) makes the chapter 7 trustee the representative of the bankruptcy estate. The trustee is a fiduciary charged with protecting the interests of all estate beneficiaries, i.e., all classes of creditors, including those holding secured, administrative, priority, and non-priority unsecured claims, as well as the debtor's interest in exempt property and surplus property, if any. The trustee's duties enumerated under § 704 are specific, but not exhaustive. To properly represent the estate, the trustee must secure for the estate all assets properly obtainable

under applicable provisions of the Bankruptcy Code, object to the debtor's discharge where appropriate, defend the estate against improper claims or other adverse interests, and liquidate the estate as expeditiously as possible for distribution to creditors.

#### 2-2.2.1 **Collection and Liquidation of Assets, § 704(1)**

A trustee has a duty to ensure that a debtor files all schedules and statements required under § 521 and Fed. R. Bankr. P. 1007. A trustee must also ensure that a debtor surrenders non-exempt property of the estate to the trustee, and that records and books are properly turned over to the trustee.

The trustee should be familiar with the definition of property of the estate as set forth in § 541. Under § 541, all legal and equitable interests of the debtor, wherever located and by whomever held, are property of the estate. Property of the estate also includes any property that the debtor acquires or becomes entitled to acquire within 180 days after the petition date by way of inheritance, property settlement or divorce decree, or life insurance.

Property of the estate is defined more broadly in chapter 13 cases under § 1306 to include property and earnings acquired postpetition. However, if a chapter 13 case is converted to a chapter 7 case, the § 1306 definition does not apply. Upon conversion, property of the chapter 7 estate consists of property of the estate, as of the date of the chapter 13 petition, that remains in the possession of or is under the control of the debtor on the date of conversion, unless the case was converted in bad faith. § 348(f).

In reviewing the schedules, the trustee should make a preliminary determination as to whether there appear to be assets in the case or areas warranting further inquiry at the section 341 meeting. The trustee should not rely upon the designation by the clerk of the bankruptcy court as to whether the case is an asset or no-asset case. The trustee should conduct an independent investigation to make this determination. A trustee should refrain from administering an estate where the proceeds of liquidation will solely benefit the trustee and the trustee's professionals, i.e., the trustee should consider whether sufficient funds will be generated to make a meaningful distribution to creditors, prior to administering the case as an asset case.

A trustee performs the duty of collecting and reducing to money property of the estate in a variety of ways. For example, the trustee may object to improper exemptions, seek disgorgement of unreasonable attorney fees paid to the debtor's

counsel, compel the turnover of non-exempt property, and use the avoidance powers of § 544, *et seq.*, to recover assets. After a trustee has collected all assets of an estate, the assets must be reduced to cash for eventual distribution to creditors under § 726.

#### 2-2.2.2 Accountability of the Trustee, § 704(2)

Section 704(2) requires the trustee to be accountable for all property received, and Fed. R. Bankr. P. 2015 imposes a duty on a trustee to keep records, make reports, and give notice of a case to persons holding property of the estate. It is incumbent on the United States Trustee to ensure that these duties are, in fact, performed.

##### 2-2.2.2.1 Control and Preservation of Property

The trustee has the duty and responsibility to insure and safeguard all estate property and property that comes into the trustee's hands by virtue of his appointment. In those cases where the property appears to have value for the estate, the trustee should obtain control over the property (which may include changing locks at the premises, hiring guards, etc.) and determine the extent and value of the property. The trustee also should immediately obtain insurance in an amount sufficient to protect the estate property (which may include insurance against fire, theft, vandalism, liability and other possible hazards) and take any other steps which may be reasonably necessary to preserve the assets. The trustee should request proof of insurance from the debtor and should ensure that it is continued for the benefit of the estate.

If there is no insurance and there are no estate funds available, the trustee should contact the secured creditor immediately, so that the secured creditor can obtain insurance or otherwise protect its own interest in the property. When the uninsured property has value, the trustee may consider seeking (a) an agreement with the secured creditor to fund the expense of insurance and provide proper safeguarding under § 506(c); or (b) a court order allowing the trustee to insure or safeguard the property at the expense of the secured creditor pursuant to § 506(c). Where the property is not or cannot be insured, the trustee should liquidate the property as quickly as possible in a reasonable manner. Under these circumstances, the trustee is strongly encouraged to file a motion to reduce the time within which objections may be filed to the proposed sale.

When the property is fully secured and of nominal value to the estate, the trustee should contact the secured creditor immediately so that the secured creditor can obtain insurance or otherwise protect its own interest in the property. The trustee

should immediately abandon fully secured property or uninsured property of no value to the estate. Note that an order granting relief from stay does not automatically constitute an abandonment.

If a loss occurs as a result of the trustee's failure to insure or protect estate property, the trustee could be subject to liability including a surcharge.

#### 2-2.2.2.2 Inventory of Estate Property

Pursuant to Fed. R. Bankr. P. 2015(a)(1), a trustee must file a complete inventory of the debtor's property within 30 days after qualifying as a trustee, unless such inventory has already been filed. The nature and extent of the inventory depends upon the type and value of the debtor's assets. The inventory should be sufficient to enable the trustee to later verify whether an auctioneer or other liquidator has accounted for all property turned over for sale.

Generally, the debtor's schedules A and B will satisfy the requirements of Fed. R. Bankr. P. 2015(a)(1) as long as the trustee is able to verify at the section 341 meeting that the debtor's inventory, as shown on Schedules A and B or other documents, is complete and satisfactory. The Form 1<sup>8</sup> maintained by the trustee, may provide a sufficient inventory of the debtor's assets. Nonetheless, there may be instances when the trustee will need to obtain a more detailed inventory in order to properly administer the assets. For example, if the debtor has listed Furs and Jewelry at \$10,000 in the schedules, the trustee will need to obtain a detailed list of the items. In addition to the written list, the trustee should consider using other methods to document the assets, such as videotaping the assets.

#### 2-2.2.2.3 Environmental Issues

The United States Trustee should verify that the trustee takes necessary and appropriate action to abate or prevent environmental contamination by or to estate property. If property of the estate has no value and may be hazardous to the health or safety of the general public, the trustee should give immediate consideration to abandoning property under § 554(a). Before abandoning the property, however, the trustee should take all precautions possible in light of the available assets of the estate and consult with appropriate federal, state and local authorities.

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<sup>8</sup>See USTM 2-3.7.1.1 for a full description of Form 1, the Individual Estate Property Record and Report.

### 2-2.2.3 **Examining the Debtor's Exemptions and Statement of Intention, § 704(3)**

#### 2-2.2.3.1 **Initial Review of Exemptions**

The trustee must object to improper debtor exemptions within 30 days after the conclusion of the section 341 meeting or the filing of any amendment to the list or supplemental schedules, unless, within such period, further time is granted by the court. Fed. R. Bankr. P. 4003(b). If the trustee does not file a timely objection to an exemption, it is deemed allowed. See Taylor v. Freeland and Krantz, 503 U.S. 638 (1992).

#### 2-2.2.3.2 **Review of Statement of Intention**

Section 521(2) requires an individual debtor to file a statement within 30 days of the filing of the bankruptcy petition disclosing his intention with respect to the retention or surrender of property of the estate securing consumer debts, and further, to perform such intention within 45 days of the filing of the notice of intent. The trustee must ensure the performance of such intentions and should examine the statement of intention early in the case and seek the debtor's verification at the section 341 meeting that the intentions have been performed.

### 2-2.2.4 **Investigate the Financial Affairs of the Debtor, § 704(4)**

The trustee investigates the debtor's financial affairs in the following ways:

1. reviews the debtor's schedules of assets and liabilities, statement of financial affairs, and schedules of current income and expenditures which the debtor must file pursuant to § 521 and Fed. R. Bankr. P. 1007 (see USTM 2-2.3)
2. examines the debtor at the section 341 meeting (see USTM 2-2.4); and
3. conducts such other investigation as necessary, such as following up on tips about unscheduled assets.

### 2-2.2.5 **Examine Proofs of Claim, § 704(5)**

Section 704(5) requires a trustee to examine proofs of claim and object to the allowance of any claim that is improper, if a purpose would be served by doing so. For example, if it is clear that there are only sufficient assets to pay priority

creditors, then no purpose would be served by examining or objecting to general unsecured claims. See USTM 2-2.5.11.

#### 2-2.2.6 Oppose the Discharge of the Debtor, § 704(6)

The trustee has a duty under § 704 to object to the debtor's discharge if advisable. Whenever appropriate, the trustee should examine the acts and conduct of the debtor to determine whether grounds exist for denial of discharge. § 727(c).

Section 727(a) provides that the court shall grant a discharge unless the debtor:

1. is not an individual (corporations and partnerships do not receive a discharge under chapter 7);
2. conceals property with intent to defraud;
3. fails to preserve or conceals financial records;
4. makes a false oath or account; presents or uses a false claim; gives, offers, receives money, property, or advantage for acting or forbearing to act; or withholds books and records;
5. fails to explain satisfactorily the loss or deficiency of assets;
6. refuses to obey an order of the court or to testify after being granted immunity;
7. commits any of the acts in a through f above within one year of the date of the filing of the petition or during the case, in connection with another case concerning an insider;
8. receives a chapter 7 or chapter 11 discharge in a case commenced within the previous six years;
9. receives a chapter 12 or chapter 13 discharge in a case commenced within the past six years under certain circumstances; or
10. submits a written waiver of discharge approved by the court.

A complaint objecting to discharge must be filed within 60 days of the date first set for the section 341 meeting. Fed. R. Bankr. P. 4004(a). The court may extend



this time but the motion for extension must be filed before expiration of the 60 day period. Fed. R. Bankr. P. 4004(b). An order granting a creditor's motion to extend the time to file an objection does not necessarily amount to an extension of time for the trustee. The trustee must obtain a separate extension.

A discharge can be revoked within one year after it was granted if the discharge was obtained by fraud and the requesting party was not aware of it until after the discharge was granted. § 727(d)(1) and (e)(1). Alternately, pursuant to § 727(d)(2) and (3) and (e)(2), before the later of one year after the granting of a discharge or the date the bankruptcy case is closed, the discharge may be revoked on the following grounds:

1. the debtor acquired or became entitled to property that would be property of the estate and knowingly and fraudulently concealed it from the trustee; or
2. the debtor refused to obey a court order or to respond to a material question after a grant of immunity if the privilege against self-incrimination was invoked.

Section 727 also authorizes the United States Trustee to object to the discharge of a debtor or to seek revocation of the discharge. If the trustee has information that would support an objection to discharge but deems such an action inadvisable, the trustee should promptly bring such facts to the attention of the United States Trustee. The United States Trustee, in addition to ensuring that the trustee complies with the duty to object to discharges under § 704, may bring such actions. Fed. R. Bankr. P. 7041 states that a complaint objecting to the debtor's discharge shall not be dismissed at the plaintiff's insistence without notice to the United States Trustee.

#### 2-2.2.7 **Furnish Information Concerning the Estate, § 704(7)**

The trustee should reply in an expeditious manner to inquiries from creditors and other parties in interest.

#### 2-2.2.8 **Operating Reports, § 704(8)**

Where the trustee is operating a business under § 721, the trustee must meet report filing requirements as described in USTM 2-3.7.2.

### 2-2.2.9 **Final Report and Final Account of the Estate, § 704(9)**

After liquidating all estate assets, converting those assets to cash, and properly investing the cash pending an examination of claims and complete performance of other duties under § 704, the trustee must make a final report and file a final account of the administration of the estate with the United States Trustee and the court. These requirements are more fully discussed in USTM 2-3.3.

## 2-2.3 **REVIEW OF PETITION, SCHEDULES, AND STATEMENTS**

### 2-2.3.1 **Review of Petition and Schedules**

The trustee is responsible for reviewing the sufficiency of the petition, matrix (list of creditors' names and addresses) and statements and schedules.

The debtor's petition must include the debtor's name, social security number, employer's tax identification number and all other names used by the debtor within six years prior to the filing. Fed. R. Bankr. P. 1005.

In addition to the petition, the following schedules and statements must be filed:

- Schedule A - Real Property
- Schedule B - Personal Property
- Schedule C - Property Claimed as Exempt
- Schedule D - Creditors Holding Secured Claims
- Schedule E - Creditors Holding Unsecured Priority Claims
- Schedule F - Creditors Holding Unsecured Non-priority Claims
- Schedule G - Executory Contracts and Unexpired Leases
- Schedule H - Co-Debtor
- Schedule I - Current Income of Individual Debtor(s)
- Schedule J - Current Expenditures of Individual Debtor(s)
- Statement of Financial Affairs

If the schedules and statements do not accompany the petition, the petition should, at a minimum, be submitted with a list containing the names and addresses of all the debtor's creditors. If such a list is filed, the debtor is given fifteen days from the filing to supply complete schedules and statement(s) of affairs. Fed. R. Bankr. P. 1007(c). The trustee must receive notice of any request for an extension of time to file documents. Fed. R. Bankr. P. 1007(a)(4) & (c).

An individual debtor also must file a statement of intention with respect to the retention or surrender of property securing consumer debts. § 521. In addition, the attorney or the petition preparer for the debtor must disclose any fees received or promised in connection with the bankruptcy proceeding. See § 110(h)(1); Fed. R. Bankr. P. 2016(b). The trustee must verify submission of the above-referenced documents and taking action in the event of non-compliance.

The trustee must also be aware of the following issues of special concern:

1. only a husband and wife can file a joint petition, pursuant § 302;
2. in a filing by a corporation, the petition should be accompanied by a copy of the resolution authorizing the filing;
3. in a partnership case, if fewer than all general partners of a partnership consent to the petition for relief on behalf of the partnership, it is an involuntary petition under § 303(b)(3); and
4. upon conversion of a chapter 11, chapter 12 or chapter 13 case to a chapter 7 case, unless otherwise ordered by the court, the previously filed statements and schedules are deemed filed in the chapter 7. If the case is converted from chapter 13, the debtor must file a statement of intention. In addition, the debtor in possession or the superseded trustee must file the final report and account and schedule of postpetition debts.

If there is no individual who is performing the duties of the corporate or partnership debtor, the trustee should request the bankruptcy court to designate a party (officer, director, partner, or person in control) to perform the duties of the debtor. Fed. R. Bankr. P. 9001(5). The person who is the subject of the designation should be given notice of the trustee's application to the court.

#### 2-2.3.2

#### **Review of Debtor's Attorney Fees**

The debtor's attorney in a bankruptcy case, whether or not the attorney intends to apply for compensation postpetition, must file a statement in compliance with § 329(a) and Fed. R. Bankr. P. 2016(b) setting forth the amount of compensation paid or agreed to be paid for services in connection with the case. This statement must be filed within 15 days after the order for relief, or as otherwise ordered. The trustee should review this disclosure of compensation and make an independent determination whether the fee paid or agreed to be paid is excessive. If the fee is questionable, the trustee or the United States Trustee should move,

pursuant to § 329 and Fed. R. Bankr. P. 2017(a), to have the court review the fee for reasonableness. To the extent the fee is excessive, the court may order cancellation of the fee agreement or the return of all or any portion of the fee.

Claims for unpaid attorney fees for prepetition services provided to the debtor generally will be discharged in a chapter 7 case. The trustee should advise the United States Trustee if a debtor's attorney attempts to collect fees from the debtor for prepetition services.

Some courts hold that a chapter 7 debtor's attorney may not be compensated for postpetition services from estate assets in light of a 1994 revision to § 330 which eliminated chapter 7 debtors' attorneys from the list of professionals who may be awarded compensation pursuant to that section. See, e.g., Inglesby, Falligant, Horne, Courington & Nash, P.C. v. Moore (In re American Steel Products, Inc.), 197 F.3d 1354 (11th Cir. 1999); Andrews & Kurth L.L.P. v. Family Snacks, Inc. (In re Pro-Snax Distributors, Inc.), 157 F.3d 414 (5th Cir. 1998). Contra U.S. Trustee v. Garvey, Schubert & Barer (In re Century Cleaning Services, Inc.), 195 F.3d 1053 (9th Cir. 1999).

The trustee should be alert for retainers held by debtors' attorneys. While courts generally hold that an unearned retainer on hand at the commencement of a case constitutes estate property, the trustee may have to initiate action to obtain the balance of the retainer.

### 2-2.3.3 **Review for Petition Preparers**

In 1994, Congress enacted legislation to regulate the conduct of lay persons who assist debtors in preparing bankruptcy petitions. Section 110 requires bankruptcy petition preparers to disclose their name, address, social security number, and fee. It prohibits preparers from signing documents for debtors, from collecting fees if court fees have not been paid, and from using the word "legal" or similar terms in advertisements. It requires preparers to provide a copy of the bankruptcy documents to the debtor at least by the time that documents are presented for the debtor's signature. The section also authorizes the court to order the return of excessive fees. The court may impose fines of up to \$500 for each statutory violation.

Section 110 also provides remedies to address certain petition preparer abuses. Damages include the debtor's actual damages, the greater of \$2,000 or twice the amount the debtor paid for the preparer's service, and reasonable attorney fees and

costs. The trustee can pursue actions under § 110 and may receive an additional \$1,000 plus reasonable attorney's fees and costs.

Section 110 also authorizes injunctive relief against preparers under certain circumstances. If a case is dismissed as the result of a preparer's knowing attempt to disregard bankruptcy requirements, the preparer may be subject to criminal liability under 18 U.S.C. § 156.

Section 110 in no way permits the unauthorized practice of law.

Trustees should report potential violations of § 110 to the United States Trustee. The United States Trustee should also conduct a review for potential violations.

#### 2-2.3.4 **Review for Substantial Abuse Under § 707(b)**

Schedules, statements of affairs, and statements of current income and expenses are reviewed for any evidence of substantial abuse that may provide the basis for a motion to dismiss pursuant to § 707(b). Such evidence may also arise or be confirmed at the section 341 meeting. If such evidence exists, the trustee notifies the United States Trustee. The United States Trustee must then independently determine whether to move for the dismissal of the case under § 707(b).

The trustee must review each case for substantial abuse. The United States Trustee must review cases for substantial abuse as well; however, the percentage of cases reviewed is within the discretion of the United States Trustee.

The following guidelines should be used in determining whether a case involves substantial abuse.

##### 2-2.3.4.1 **Determination of "Primarily Consumer Debt"**

Consumer Debt:

Section 707(b) applies only to a case filed by an individual with debts incurred primarily for personal, family, or household purposes.

Credit card debts may not in all instances constitute consumer debts. When the credit transaction involves a profit motive, it is outside the definition of a consumer credit transaction. Mortgage debt is considered a consumer debt, In re Kelly, 841 F.2d 908 (9th Cir. 1988), unless the proceeds are used for a business purpose. In re Funk, 146 B.R. 118 (D.N.J. 1992).

### Primarily Consumer Debt:

The term “primarily consumer debt” is not defined in the Bankruptcy Code. One court has held that a debtor’s obligations may be adjudged primarily consumer debts not only by the aggregate amount, but by their relative number as well. Other courts have concluded, however, that it is appropriate to give more weight to the aggregate amount than the number of debts. The United States Trustee should alert trustees to any decisions on this point within the trustee’s judicial district.

#### 2-2.3.4.2 Determining Substantial Abuse

The precise meaning of “substantial abuse” is presently left to judicial interpretation. The following factors have been considered by the courts in determining if there is substantial abuse under § 707(b) and should, therefore, be considered:

##### Ability to Repay Debts:

The statement of financial affairs and statement of income and expenses of the debtor should be examined for any evidence indicating that the debtor could pay a meaningful percentage of debts owed to creditors over a period of time. The Ninth Circuit Court of Appeals, in In re Kelly, 841 F. 2d 908, 915 (9th Cir. 1988), held that “a finding that a debtor is able to pay his debts, standing alone, supports a conclusion of substantial abuse,” justifying dismissal under § 707(b).

In addition, several other courts have indicated that the primary factor to be considered in determining the existence of substantial abuse is whether the debtor would have sufficient disposable income to repay a meaningful part of the debtor’s debts within the context of a chapter 11 or chapter 13 plan.

In analyzing the ability to repay debts, the debtor’s statement of income and expenditures should be reviewed for reasonableness and accuracy. The future earnings potential of the debtor also should be considered, even if the earnings arise from an exempt source. To the extent possible, consideration should be given to the debtor’s experience, education, background, skills, health, and aptitude.

In determining disposable income, § 1325(b)(2) offers guidance in that it defines “disposable income” as income which is received by the debtor and which is not reasonably necessary for the maintenance or support of the debtor or a dependent of the debtor.

The Fourth Circuit, however, has held that an ability to repay standing alone will not support a finding of substantial abuse. In re Green, 934 F.2d 568 (4th Cir. 1991).

#### Motivation and Factors Surrounding Filing:

Some courts have also sustained a finding of substantial abuse if the debtor’s motivation for filing evidences a lack of honesty. One leading case stated:

Substantial abuse can be predicated upon either lack of honesty or want of need.

It is not possible, of course, to list all the factors that may be relevant to ascertaining a debtor’s honesty. Counted among them, however, would surely be the debtor’s good faith and candor in filing schedules and other documents, whether he has engaged in “eve of bankruptcy purchases,” and whether he was forced into Chapter 7 by unforeseen or catastrophic events.

In re Krohn, 886 F.2d 123, 126 (6th Cir. 1989). Accord, First USA v. Lamanna (In re Lamanna), 153 F.3d 1 (1st Cir. 1998).

#### 2-2.3.4.3 Timing

The trustee should notify the United States Trustee of any reasonable basis for a motion to dismiss pursuant to § 707(b) as soon as possible. If the United States Trustee decides to bring an action, it must be filed within 60 days of the date originally scheduled for the first meeting of creditors, not the date on which the meeting was actually held. Fed. R. Bankr. P. 1017(e)(1).

The trustee should also refer cases which appear to be abusive, but do not meet the criteria for § 707(b), to the United States Trustee for consideration under § 707(a).

## 2-2.4 **SECTION 341 MEETING**

### 2-2.4.1 **Duty to Preside at Meeting**

Section 341(a) states that the United States Trustee shall preside at the meeting of creditors. The meeting of creditors provided for in § 341(a) is the official forum where the debtor must appear and answer under oath questions from the trustee, creditors, and other parties in interest regarding the estate. The trustee is the presiding officer at the section 341 meeting as designee of the United States Trustee. The trustee may not delegate the duty to preside at the section 341 meeting. The trustee must seek prior approval, confirmed in writing, from the United States Trustee if the trustee is unable to preside at a scheduled meeting. If the United States Trustee designates another to serve at the section 341 meeting, the trustee is responsible for ensuring that the designated presiding officer is qualified and trained to conduct the meeting.

The section 341 meeting is held for the benefit of creditors and parties in interest. It is their opportunity to question the debtor regarding the debts and assets of the estate. It also provides them with the chance to learn about the debtor's financial situation in greater detail through questioning by other creditors. Prior to the section 341 meeting, the trustee can ask the debtor to provide documents to corroborate the information contained in the petition, statements, and schedules. See § 521(4). Such documents may include, but are not limited to: tax returns, financial statements, loan documents, trust deeds, titles, insurance policies, and wage and bank statements.

The United States Trustee should confirm the trustee's compliance with procedures for approving a debtor's alternative appearance at a creditors' meeting when extenuating circumstances prevents the debtor from appearing in person. Extenuating circumstances may include military service, terminal illness, or incarceration. In such instances, a debtor's appearance at a section 341 meeting may be secured by alternative means, such as a telephonic meeting under oath. A trustee may not unilaterally waive a debtor's appearance at the creditors' meeting.

The United States Trustee should also confirm that, when a trustee becomes aware of a debtor's disability, including hearing impairment, the trustee notifies the United States Trustee immediately so that reasonable accommodation can be made. The United States Trustee should have procedures in place to address the special needs of debtors.



There is no statutory obligation to provide language interpreters at section 341 meetings. However, the trustee should attempt to communicate with a non-English speaking debtor by seeking the assistance of third parties present such as attorneys and family members. All parties who offer to interpret must be placed under oath. If a non-English speaking debtor is unable to communicate with the trustee, or the trustee plans to take any adverse action against a non-English speaking debtor, the trustee should consult with the United States Trustee.

#### 2-2.4.2 **Conducting the Meeting**

The trustee must conduct the meeting in an orderly, yet flexible manner, and provide for questioning of the debtor as to matters affecting the debtor's financial affairs and conduct. The trustee's demeanor toward all parties should be appropriate and professional.

The trustee should examine the debtor to the extent appropriate to determine the existence of estate assets, transfers, exemptions, prior filings, possible fraud, abuse, and other matters. Paraprofessionals, such as a paralegal or a petition preparer, may not sit next to the debtor at the table, advise the debtor, or stand-in for the debtor's attorney at the meeting. Representatives of the media are permitted to be present, but no one is permitted to televise, photograph, or electronically record the proceedings (other than certified court reporters). Questions by creditors and other parties in interest are allowed. Individuals who represent creditors but who are not attorneys may be present at the meeting. Generally, the trustee should permit these persons to examine the debtor. Some jurisdictions, however, may view this as the unauthorized practice of law. The United States Trustee should instruct the trustee regarding local practices.

The United States Trustee should verify that the trustee refrains from answering questions seeking legal advice during the section 341 meeting, and avoids actions that would result in the perception that the trustee is a judge or has judicial power. If an election is requested, the trustee should follow the procedures set forth in USTM 2-1.6.8.

The United States Trustee should also verify that the trustee exercises appropriate control over the demeanor of the debtors, attorneys, and creditors during the course of the section 341 meeting. Uncooperative or recalcitrant debtors should be reminded by the trustee of their duties under § 521 and Fed. R. Bankr. P. 4002, especially the duty to cooperate with the trustee in the administration of the estate. Questioning should not be allowed to deteriorate to a level constituting harassment or to focus exclusively on the dischargeability of a particular debt.

All section 341 meetings must be electronically recorded. The trustee is responsible for ensuring that the recording equipment is operating properly. The trustee should announce that testimony is being recorded on a tape recorder and must require parties to speak clearly. The spelling of the names of any parties formally entering their appearance on the record should be obtained in case a transcript is requested at a later date. The trustee must provide the tape recording to the United States Trustee upon conclusion of the day's meetings. The recording must be retained by the United States Trustee for a period of two years. Fed. R. Bankr. P. 2003(c).

The trustee must administer the oath to each debtor individually, not to the debtors collectively. Pursuant to § 341(d), the trustee must establish on the record that the debtor acknowledges an awareness of:

1. the potential consequences of seeking a discharge in bankruptcy, including the effects that this action may have on the debtor's credit history;
2. the ability to file a bankruptcy petition under a different chapter of the Bankruptcy Code;
3. the effect of receiving a discharge of debts under chapter 7 of the Bankruptcy Code; and
4. the effect of reaffirming a debt, including the debtor's knowledge of the provisions of § 524(d).

This information is contained in the information sheet furnished by the United States Trustee. The trustee must verify on the record that the debtor has received and read the information sheet. If the debtor responds in the negative, the trustee must provide a copy of the information sheet and adjourn the meeting to the end of the calendar or another appropriate time. The meeting cannot be concluded until the information has been conveyed.

If a debtor asserts the Fifth Amendment privilege in response to a particular question, the trustee should proceed with the meeting and continue to question the debtor. At the conclusion of the questioning, the trustee should adjourn or continue the meeting and immediately notify the United States Trustee. The United States Trustee will, if appropriate, advise the United States Attorney who may take appropriate action to seek a grant of immunity. If the claim of privilege is not well founded, the trustee should seek an order from the court compelling

testimony or granting such other relief as may be appropriate, such as dismissal or denial of discharge.

#### 2-2.4.3 **Rescheduling and Continuances**

Continuances of section 341 meetings are not mandated by the Bankruptcy Code and should be granted only under exceptional circumstances. The United States Trustee should instruct trustees regarding the local rules and practices governing debtor rescheduling requests and continuances.

The trustee should not routinely continue section 341 meetings when the debtor appears. If a trustee must continue the meeting, however, the trustee must, if at all possible, announce the continued date to all parties present at the initial meeting, and advise the United States Trustee and, if necessary, the clerk of the bankruptcy court, of the continued date.

Any continued or rescheduled meeting should be held before the time for objection to discharge has expired unless the trustee has obtained an extension of time to object to the debtor's discharge. If the debtor does not appear at a continued or rescheduled meeting, the trustee should ensure that action is taken for dismissal, unless dismissal would not be in the best interest of the estate.

#### 2-2.4.4 **Non-Attendance by Attorneys**

When the debtor's attorney fails to appear, the trustee should advise the debtor of the right to proceed without an attorney or to request a continuance to ensure the debtor is represented by an attorney. The trustee should consider filing a motion under § 329(b) to compel turnover or refund of the fees received by an attorney who unjustifiably fails to appear.

#### 2-2.4.5 **Non-Attendance by Debtors**

The debtor or, in a case of a partnership or corporation, a designated representative of the partnership or corporation must attend the section 341 meeting. When spouses have filed jointly, the Code requires both debtors to be present at the section 341 meeting. The United States Trustee should verify the trustee's use of the following remedies for a debtor's failure to appear:

1. Continuing the section 341 meeting to another calendar date and notifying the United States Trustee and, if necessary, the clerk of the bankruptcy court, of the new date;

2. Filing a motion to dismiss the case; or
3. Filing an application to designate an individual to perform the duties of the debtor if the debtor is not a natural person. Fed. R. Bankr. P. 9001(5). If that individual fails to appear at the section 341 meeting, the trustee should seek an order to compel attendance.

In any event, in an individual debtor case, if the availability of these remedies extends beyond the date fixed for objecting to the discharge of the debtor or the time to file a motion pursuant to § 707(b), then the trustee should:

1. obtain a consensual order extending the deadlines;
2. file a motion to extend the trustee's time to object to discharge; or
3. notify the United States Trustee of the need to file a motion to extend the time to move to dismiss.

## 2-2.5 **ADMINISTRATION OF A CASE**

### 2-2.5.1 **Determination and Administration of No-Asset Cases**

Prior to administering a case as an asset case, the trustee must consider whether sufficient funds will be generated to make a meaningful distribution to creditors. If the trustee determines after the section 341 meeting that the case is a no-asset case, then the trustee must timely execute and file a Report of No Distribution (NDR).

The purpose of the NDR is to close administration of the case. An NDR certifies that the trustee has reviewed the schedules, investigated the facts, and determined that there are no assets to liquidate for the benefit of creditors. It also certifies that the trustee has examined the debtor's claimed exemptions and concluded that there is no purpose served to object to their allowance, and that all security interests and liens against non-exempt property are properly documented, perfected, and not subject to attack as preferences or otherwise voidable. See USTM 2-2.5.7.4.

If assets are subsequently discovered, the NDR should be withdrawn in writing and the case should be re-opened to administer the assets. See USTM 2-2.10. The trustee should seek to deny or revoke the debtor's discharge if the debtor failed to disclose the assets. See USTM 2-2.2.6.

### 2-2.5.2 **Claims Bar Date**

In most districts, a notice of insufficient assets to pay dividends is provided to creditors as part of the section 341 meeting notice. Fed. R. Bankr. P. 2002(e). Promptly upon determination that the administration of a case will generate funds to pay creditors, the trustee must ensure that the clerk of the bankruptcy court provides notice to creditors to file proof of claims on or before a certain date. Fed. R. Bankr. P. 3002(c)(5).

### 2-2.5.3 **Exemptions**

A debtor must list property claimed as exempt on the schedule of assets filed with the court. Fed. R. Bankr. P. 4003(a). Only individuals may claim exemptions; corporations and partnerships may not. The trustee must object to improper debtor exemptions within 30 days after the conclusion of the section 341 meeting or the filing of any amendment to the list or supplemental schedules, unless, within such period, further time is granted by the court. Fed. R. Bankr. P. 4003(b); see Taylor v. Freeland and Kronz, 503 U.S. 638 (1992). The objecting party has the burden of proving that the exemptions are not properly claimed. If an objection is not filed in a timely manner, the exemption will be allowed by the court.

The trustee should object to a claimed exemption if to do so benefits the estate. The trustee may use the section 341 meeting to gain information on the debtor's claimed exemptions. The debtor is allowed to amend the bankruptcy schedules as a matter of course at any time before the case is closed. Fed. R. Bankr. P. 1009.

The debtor must give notice of the amendment to the trustee and to any entity affected thereby. Thus, where the debtor has incorrectly exempted assets that would be exempt under another section if claimed properly, or has exempted assets that provide no equity for the estate after accounting for secured claims and properly claimed exemptions, the trustee probably would not want to object. However, if allowing the improperly claimed exemption would remove assets from the estate that should be available for payment of creditor claims, the trustee must object.

### 2-2.5.4 **Abandonments**

Abandonments of property are governed by § 554. A trustee should abandon any estate property that is burdensome or of inconsequential value to the estate.

Property should be abandoned when the total amount to be realized would not result in a meaningful distribution to creditors or would redound primarily to the benefit of the trustee and professionals.

In determining whether property has consequential value to the estate, the trustee should consider a number of issues, including:

1. The amount, validity and perfection of purported security interests against such property. Since the trustee has a duty to use the trustee's avoidance powers under §§ 544, 545, 547, and 548, to the extent a purported lien is invalid or could be avoided by the trustee, the property should not be abandoned if the value thereof without the lien would benefit the estate.
2. The value of the property. Value can be determined in various ways. The trustee can consult with the debtor and the debtor's attorney, have the secured party provide documentation as well as the pay-off statement, obtain price lists, conduct physical inspections or appraisals, and use common sense. The precision with which value is determined often depends on the margin between the lien or encumbrance and the estimated value of the property.
3. Tax considerations, including any § 724(b) issues.
4. Administrative expenses and litigation costs to be borne by the estate resulting from the recovery and sale of the property.

The trustee should be able to justify the decision to abandon estate property. Any documentation in support of this decision should be kept in the estate file. Scheduled property that is not administered before the case is closed is deemed abandoned upon entry of the order closing the estate. § 554(c). However, the trustee should not rely on the deemed abandonment provisions of § 554(c) where property may expose the estate to some type of liability. An order granting relief from stay does not remove property from the estate. The trustee should immediately abandon fully secured property or uninsured property of no value to the estate. Immediate consideration should be given to property of no value to the estate which may be hazardous to the health or safety of the general public. Such property should be abandoned after consultation with appropriate federal, state, and local authorities.

Creditors are entitled to notice of a proposed abandonment of assets. § 554(a). A notice of abandonment should identify each asset to be abandoned by reference

to the description provided in the debtor's schedules and any unlisted assets should be clearly described. The notice should also provide such additional information as is needed to demonstrate the basis upon which the decision to abandon was made, such as (a) the amount of secured claims exceeds the value of the asset; (b) the costs of recovering and/or liquidating the asset are estimated to exceed its value to the estate; (c) the expenses of preserving the asset are estimated to exceed its value to the estate; and (d) any other information that would assist creditors in evaluating the proposed action of the trustee.

The United States Trustee should review notices of abandonment and final reports to determine whether the decision to abandon or not to administer an asset was in the estate's best interest. If no determination can be made on the basis of information supplied, the United States Trustee should require additional information in the notice or final report. The United States Trustee should review abandonments at the earliest opportunity, and, if it appears that the decision to abandon or not administer an asset was not in the estate's best interest, object or take other appropriate action.

#### 2-2.5.5 **Turnover Demands**

When assets in which there is equity are in the possession or control of the debtor or third parties, the trustee should seek to gain control of those assets as soon as possible. Normally, the assets will be delivered to the trustee voluntarily and without court order. The request for the turnover of property from the debtor can be made on the record at the section 341 meeting. In most cases, the trustee should put requests for turnover in writing, designating a time limit for compliance.

If the initial requests do not produce results, the trustee should seek a court ruling requiring the debtor or third party to give up possession to the trustee. An action against the debtor is commenced by motion. An action against a third party must be commenced as an adversary proceeding. Fed. R. Bankr. P. 7001(1). If there is a danger that the assets are wasting in the hands of the debtor or third party, the trustee should request a hearing forthwith or a temporary restraining order.

Sections 542 and 543 govern the turnover of property. Section 542(a) contains the general requirement that estate property be delivered to the trustee. Section 542(e) allows the court to order a person holding papers or other recorded information about the debtor's property or financial affairs to turn over the property rather than just disclose the information. Section 543 addresses the turnover of property by a custodian.

In chapter 11 or chapter 13 cases that are converted to chapter 7, any debtor or trustee must turn over to the chapter 7 trustee all records or property of the estate in his possession or control. Fed. R. Bankr. P. 1019(4).

#### 2-2.5.6 **Executory Contracts and Unexpired Leases**

Section 365 provides that the trustee may assume or reject unexpired leases or executory contracts. This authority is subject to court approval. It is also subject to limitations set forth in § 365(b), (c), and (d).

A proceeding to assume, reject, or assign an executory contract or unexpired lease is a contested matter. See Fed. R. Bankr. P. 6006(a). The assumption or rejection of an executory contract or unexpired lease must be sought within 60 days of the filing of the petition. An extension may be requested from the court, for cause, but must be obtained within the original 60-day period. The contract or lease is deemed rejected if a motion for assumption is not filed within the time limitations, pursuant to § 365(d)(1).

The trustee should promptly evaluate unexpired leases and executory contracts for potential value or detriment to the estate. The trustee's failure to timely reject may result in the accrual of administrative expense liability to the estate. See, e.g., § 365(d)(3) which requires the trustee to timely perform the obligations of the debtor, such as payment of rent, with respect to an unexpired lease of nonresidential real property up until the time of assumption or rejection.

Assumption of unexpired leases or executory contracts may be desirable for favorable leases or contracts which the trustee can assume and then contemporaneously assign for consideration. The trustee must cure, or provide adequate assurance of a prompt cure of, any default in an unexpired lease or executory contract to assume the lease or contract. The trustee also is required to compensate or provide adequate assurance of prompt compensation to non-debtor parties for pecuniary loss resulting from the default and to provide adequate assurance of future performance under such lease or contract.

The trustee may encounter a situation in which business property needs to be used for a period of time to secure inventory or provide a sale location. The trustee should negotiate with the landlord for short-term use of the facilities with rental cost to be treated as an administrative expense to be paid from the sale proceeds. This falls short of assuming the debtor's lease or contract for purchase.



### 2-2.5.7 Avoidance Powers

A fundamental goal of the Bankruptcy Code is to ensure equality of distribution among creditors of the same class. The trustee is provided with various avoiding powers in §§ 544-553 as tools to be used to avoid unequal treatment among creditors of the same class or other parties in interest. The trustee should be familiar with these Bankruptcy Code sections and alert to their application in individual cases.

Generally, any action brought by the trustee to recover money or property pursuant to the trustee's avoiding powers must be brought as an adversary proceeding. Fed. R. Bankr. P. 7001. The trustee does not need court approval to prosecute such an action. Fed. R. Bankr. P. 6009.

#### 2-2.5.7.1 Section 544 - General Power

Section 544 vests the trustee with the powers of a hypothetical judicial lien creditor or bona fide purchaser of real property under state law. The effect is to empower the trustee to avoid unperfected and secret liens, even if the debtor or trustee has knowledge of these liens. This section also allows a trustee to exercise the rights of actual unsecured creditors to avoid liens under state fraudulent and preferential conveyance laws, to avoid defective bulk transfers, and to employ state equitable remedies such as the marshaling of assets.

#### 2-2.5.7.2 Section 545 - Statutory Liens

Section 545 empowers the trustee to avoid certain statutory liens, such as landlord liens, against the debtor's property within the terms and conditions set out in the section. The term "statutory lien" is defined in § 101(53).

#### 2-2.5.7.3 Section 546 - Limitations

Section 546 places limitations on the trustee's power. Limits are specified as to:

1. statute of limitations, the later of two years after the entry of the order for relief or one year after the appointment or election of the first trustee, or the time the case is closed or dismissed, whichever occurs first;
2. postpetition perfection authorized by non-bankruptcy law;
3. reclamation - statutory or common law;

4. producers of grain or fishermen; and
5. payments regarding settlement or margin accounts, repurchase agreements or swap agreements.

#### 2-2.5.7.4 Section 547 - Preferences

Section 547 deals with preferential transfers. It is probably the most important and most frequently used avoiding power of the trustee. The trustee may avoid any transfer of an interest of the debtor in property:

1. to or for the benefit of a creditor;
2. for or on account of an antecedent debt owed by the debtor before the transfer was made;
3. made while the debtor was insolvent;
4. made on or within 90 days of the date the petition was filed; and
5. which enables the creditor to receive more than the creditor would have received if the case was a case under chapter 7 and the transfer had not been made.

All five of the conditions must be present to avoid the transfer. The 90-day time period is extended to one year if the transfer is to an “insider” as defined in § 101(31). The transfer in question can be the granting or perfection of a lien or security interest as to property of the debtor.

The trustee should become familiar with the provisions of § 547(c) which define transfers that the trustee cannot avoid. A transferee will most likely raise a provision of § 547(c) as a defense to an avoidance action brought by the trustee.

#### 2-2.5.7.5 Section 548 - Fraudulent Transfers

Section 548 allows the trustee to avoid transfers that are different in nature than the preferential transfers described above. While preferential transfers are most often made to creditors, fraudulent transfers are most frequently made to family or friends. The trustee may avoid a transfer or obligation made or incurred within one year before the date of the filing when:

1. the transfer or obligation involved an actual intent to hinder, delay, or defraud creditors, without regard to the solvency or insolvency of the debtor; or
2. the debtor received “less than a reasonable equivalent value” in exchange for the transfer where:
  - a. the debtor was or became insolvent as a result of the transfer;
  - b. the debtor was left with unreasonably small capital for his business; or
  - c. the debtor intended to incur debts beyond his ability to pay them as they mature.

The trustee should be aware of state fraudulent conveyance laws which may allow avoidance of transfers beyond the one year period, through application of § 544(b).

#### 2-2.5.7.6 Section 549 - Postpetition Transfers

Section 549 recognizes the trustee’s right to avoid any transfer of property made after the commencement of the case that is not specifically authorized by the Bankruptcy Code or by the court. If such a transfer was made voluntarily, the trustee should notify the United States Trustee who should make a referral to the United States Attorney if it appears that there may have been a violation of 18 U.S.C. § 152. If the transfer was involuntary, the trustee may bring contempt proceedings against the transferee for violating the automatic stay and request damages for any diminution of estate funds resulting from the unauthorized transfer.

#### 2-2.5.7.7 Section 553 - Setoff

Section 553 recognizes the right to offset for mutual, prepetition, allowed claims and takes such transactions out of the preference category. The section places limits on the right of the offset as to claims to which the creditor became entitled to within 90 days of the filing of the petition.

2-2.5.7.8      Section 724(a) - Fines, Penalties, or Forfeitures

Section 724(a) authorizes the trustee to avoid liens that secure claims for fines, penalties, forfeitures, or multiple, exemplary, or punitive damages, to the extent such claims are not compensation for actual pecuniary losses.

2-2.5.8      Contested Matters and Adversary Proceedings

Rule 9014 provides that, in a “contested matter,” relief shall be requested by motion and reasonable notice and opportunity for hearing shall be afforded the party against whom relief is sought. Fed. R. Bankr. P. 9014. Unless the court orders otherwise, no response to a motion is required. However, local rules may require a response. In essence, contested matters are disputes not designated as adversary proceedings in Fed. R. Bankr. P. 7001.

Adversary proceedings are lawsuits commenced by a complaint. The types of actions that must be brought as adversary proceedings include:

1. To recover money or property, except a proceeding to compel the debtor to deliver property to the trustee or a proceeding under § 554(b), § 725, or Fed. R. Bankr. P. 2017 or 6002;
2. To determine the validity, priority, and extent of a lien or other interest in property;
3. To approve the sale of both the estate’s interest and a co-owner’s interest in property;
4. To object to or revoke a discharge;
5. To revoke an order of confirmation of a chapter 11, chapter 12 or chapter 13 plan;
6. To determine the dischargeability of a debt;
7. To obtain an injunction or other equitable relief;
8. To subordinate any allowed claim or interest except in chapter 9, chapter 11, chapter 12 or chapter 13 plans;
9. To obtain a declaratory judgment, or

10. To determine a claim or cause of action removed to a bankruptcy court.

Fed. R. Bankr. P. 7001. Fed. R. Bankr. P. 7001-7087 specify the procedures applicable to adversary proceedings. These rules incorporate many of the Federal Rules of Civil Procedure.

#### 2-2.5.9 **Operating the Debtor's Business**

Under § 721, the court may authorize a trustee to operate the business of a debtor for a limited period of time. In order for the court to grant such a request, two basic requirements must be met. First, operation of the debtor's business must be in the best interest of the estate. Second, such operation must be consistent with the liquidation of the estate.

Section 721 adds the ability for a trustee to sell the business as a going concern. Unlike a chapter 11 case, in a chapter 7, only the trustee and not the debtor may be authorized to operate the debtor's business. Such authorization might be appropriate, for example, for the interim operation of the debtor's business to complete work in process if the final product will realize a net return greater than would be the value of the component parts sold individually. Similarly, continued operation of the debtor's business may be authorized when it appears that the debtor's business can be sold for a greater price as a going concern or when sudden termination of the business would cause great hardship to the general public or innocent third parties, such as patients in a nursing home. The trustee should consider the following factors in determining whether continued operation is in the best interests of the estate:

1. whether operating the business will result in an operating loss;
2. the tax consequences of operating the business;
3. the costs necessary to bring the business within compliance of local laws to the extent local laws do not conflict with the Bankruptcy Code;
4. potential liabilities and claims against the estate and the trustee which may arise from the operation of the business; and
5. the length of time the business will be operated.

Even when the court finds operation of a business will increase the estate's value without endangering the estate assets, the trustee should seek to operate the

business for the shortest practical period. The trustee should either close the case, liquidate the business, or convert the case to chapter 11 within a reasonable time, normally not to exceed one year from entry of the order authorizing operation of the business.

Pursuant to § 721, the trustee must obtain a court order approving and authorizing operation of the debtor's business. Prior to seeking authority to operate a business, the trustee must consult with the United States Trustee to discuss the nature of the operation, cash management controls, and to obtain the appropriate monthly operating report form required pursuant to § 704 (8). Note that the format of the operating report may vary from district to district.

The trustee's regional or district blanket bond may not cover the trustee's operation of a business in a chapter 7 case. The United States Trustee should discuss with the trustee whether it is necessary for the trustee to acquire a separate bond.

Having a general duty to maintain and preserve property of the estate, the trustee of an operating business should ensure that the estate's assets are insured against all normal business risks including general liability, property damage, and workmen's compensation, as well as all other types of insurance that may be required for a particular operation. A trustee who exceeds his or her granted authority, or is guilty of a breach of his or her fiduciary duty, is subject to personal liability for any loss to the estate.

The trustee may not use cash collateral to continue the operation without first obtaining an order of the court, unless the creditor consents. When the trustee operates the debtor's business, the ability of the trustee to use, sell, or lease property of the estate in connection therewith, or to obtain credit or incur debt, is governed by §§ 363 and 364. The trustee may, however, sell or lease property in the ordinary course of the business without notice or a hearing, and may use property of the estate in the ordinary course of business without notice or hearing, except that the trustee may not use cash collateral without a court order or the creditor's consent.

The trustee operating a business may obtain unsecured credit and incur unsecured debt in the ordinary course of the business without notice or hearing or other court authority, and the debts incurred become an administrative expense. The trustee may not, however, borrow money or incur unsecured credit other than in the ordinary course of business without court approval after notice and hearing.

If the business has employees, the trustee must withhold income, social security, and other applicable taxes from any wages paid, as well as file employment tax returns and remit the amounts withheld, plus the employer portion of the taxes, to the appropriate taxing authority. For further information, the trustee should consult IRS Circular E (Employer's Tax Guide).

The trustee also must comply with other laws applicable in the state(s) in which the business operates. See 28 U.S.C. § 959(b).

If it is apparent that the estate would benefit from an extended period of operation, the United States Trustee should encourage the trustee to file a motion seeking conversion of the case to chapter 11 under § 706(b), and requesting the appointment of a chapter 11 trustee pursuant to § 1104(a). The trustee should determine whether a proposed plan of liquidation could satisfy the requirements of confirmation under § 1129. If the trustee fails to request conversion of the case and the appointment of a chapter 11 trustee, the United States Trustee should take appropriate action to do so.

If the trustee fails to maintain an adequate bond, or fails to file the requisite operating reports, or the reports demonstrate a loss to the estate, and the efforts of the United States Trustee to persuade the trustee to remedy these deficiencies or any others affecting the integrity of the administration of the case are not successful, then the United States Trustee should seek an order terminating the trustee's authority to operate the business or seek removal of the trustee if continued operation is in the estate's best interest.

#### 2-2.5.10 **Sale of Assets**

##### 2-2.5.10.1 **General Standards**

Section 363(b) permits a trustee to use, sell or lease property of the estate only after notice to creditors and a hearing. The only exception to the notice requirement is when the contemplated transaction is in the ordinary course of the debtor's business. The liquidation of estate assets by a chapter 7 trustee rarely falls within the "ordinary course of business exception" because the debtor's operations cease upon the filing of the chapter 7 case. A trustee, therefore, must comply with the notice and hearing requirements of § 363(b) before liquidating an estate asset.

Generally, the trustee begins liquidating estate assets after the section 341 meeting. Exigent circumstances, however, may require liquidation of assets immediately after the case is filed.

A trustee should only sell assets that will generate sufficient proceeds to ensure a distribution to unsecured creditors, priority or general. In evaluating whether an asset has equity, the trustee must determine whether there are valid liens against the asset and whether the value of the asset exceeds the liens. The trustee must also consider whether the cost of administration or tax consequences of any sale would significantly erode or exhaust the estate's equity interest in the asset. If the sale of an asset would result in little or no equity to the estate for the benefit of unsecured creditors, the trustee should abandon the asset.

It is a violation of federal criminal law for a trustee or officer of the court to purchase directly or indirectly or otherwise deal in property of the estate for which the trustee serves. 18 U.S.C. § 154. While a trustee is not specifically prohibited from purchasing assets from an estate administered by another trustee, the practice should be avoided to eliminate any appearance of impropriety. Similarly, sales to professionals regularly retained by a trustee should be avoided. A trustee or a professional regularly employed by the case trustee, including the auctioneer, a family member of the trustee or professional, or an employee of the trustee or professional, are not permitted to bid or to buy property at a private sale or at an estate sale conducted by the auctioneer. The United States Trustee will object to any proposed sale of estate property to either a trustee or a professional person regularly employed by the case trustee, a family member of the trustee, or an employee of the trustee. If the trustee becomes aware of any indications of sales to insiders or of collusion in bidding, the sale should be stopped immediately, and the matter reported to the United States Trustee.

Creditors must receive 20 days notice of a proposed sale of estate property. Fed. R. Bankr. P. 2002(a)(2) and 6004(a). The court, for cause, may order a shorter notice period. Fed. R. Bankr. P. 6004(d) provides that when all non-exempt assets of the estate have an aggregate gross value of less than \$2,500, it is sufficient to give a general notice of the trustee's intent to sell. The notice does not have to conform to the requirements of Rule 2002(c). Fed. R. Bankr. P. 6004(d).

A hearing on the sale or an order authorizing or confirming the sale is not required by Fed. R. Bankr. P. 6004, unless an objection is filed. However, in some jurisdictions, the trustee may be required to file a motion and obtain a court order to sell property.



Objections to the sale must be filed within 15 days from the mailing of the notice or within the time fixed by the court. Unless the court orders otherwise, objections to a sale must be filed and served five days before the date set for the proposed action. Fed. R. Bankr. P. 6004(b). An objection to sale is deemed a request for a hearing and the matter proceeds as a contested matter. Fed. R. Bankr. P. 9014.

Notice of a proposed use, sale, or lease of property of the estate must be provided to the clerk of the bankruptcy court, debtor, United States Trustee, and all creditors. The following information should be included in the notice:

1. Type of sale (private, auction, etc.);
2. Location, date, and time of public sale;
3. Description of assets;
4. Terms and conditions of sale;
5. Factors used to establish value (appraisal, book value, etc.) in a private sale;
6. Procedure and time period for filing objections;
7. Amount of liens and identity of lien holders; and,
8. In a private sale, identity of purchaser and relationship, if any, to any creditor or party in interest.

Generally, all sales should be paid for in cash equivalents, such as certified checks, cashier's checks, and money orders. The trustee normally should not accept a promissory note or installment payments. See USTM 2-2.5.10.6 regarding periodic payments.

#### 2-2.5.10.2 Sale Free and Clear of Liens

Section 363(f) allows a trustee to sell property of the estate free and clear of an interest of an entity other than the estate, only if:

1. applicable non-bankruptcy law would permit a sale of such property free of the interest;

2. the entity consents;
3. the interest is a lien and the sale price is greater than the aggregate value of all liens on the property;
4. the interest is in bona fide dispute; or
5. the entity could be compelled in a legal or equitable proceeding to accept a money satisfaction of its interest.

The bankruptcy court may approve a sale over objections of a lien holder or any entity with an interest in the property, with liens attaching to the proceeds.

A lien holder cannot be charged with general expenses of administration, or the expenses of the case, and preservation of the property, except as incurred for the lien holder's benefit. If the trustee can establish that the sale was necessary to the preservation of the lien holder's interest in the collateral, the trustee may be able to recover sale expenses under § 506(c).

#### 2-2.5.10.3 Sale of Jointly Owned Property

Section 363(h) allows a trustee to sell both the estate's interest and the interest of any co-owner in property in which the debtor had, at the time of the commencement of the case, an undivided interest as a tenant in common, joint tenant, or tenant by the entirety, if specific conditions are met. An action to obtain approval pursuant to § 363(h) to sell jointly owned property must be brought by the trustee as an adversary proceeding. Fed. R. Bankr. P. 7001.

#### 2-2.5.10.4 Sale of Secured Property

Generally, a trustee should not sell property subject to a security interest unless the sale generates funds for the benefit of unsecured creditors. A secured creditor can protect its own interests in the collateral subject to the security interest. In certain limited circumstances, however, a trustee may properly sell secured property that would generate no proceeds for the benefit of unsecured creditors ("fully secured property"). For example, a trustee may be able to satisfy in full a blanket security interest on multiple units of property by selling only one unit. Similarly, a trustee may be able to obtain a higher price from an aggregate sale of assets than from selling the assets individually. In a case with funds otherwise available for unsecured creditors, a trustee also may sell fully secured property to

eliminate a deficiency, if the secured creditor agrees to waive any unsecured claim for a deficiency in the event the sale does not fully satisfy the security interest.

In determining whether the sale of secured property is appropriate, the trustee must consider possible adverse tax consequences resulting from the sale and the sale's effect on the trustee's ability to otherwise administer and close the case as expeditiously as possible. Administering fully secured property should always be viewed as the exception taking into account the particular circumstances of each case.

When selling fully secured property, the trustee must administer the sale to avoid a diminution of funds otherwise available for unsecured creditors. The trustee should obtain an agreement in writing from the secured creditor to recover the costs of sale from the collateral pursuant to § 506(c). The trustee must disclose the terms of any agreement between the trustee and the secured creditor at the outset, for example, in the notice of proposed sale, and in the trustee's final report and request for compensation and reimbursement of expenses. Any sums recovered from the collateral under § 506(c) is property of the estate and must be deposited in the estate account.

#### 2-2.5.10.5 Conduct of Sales

Sales of estate property must conform to the requirements of Fed. R. Bankr. P. 6004. Upon completion of the sale, an itemized statement of the property sold, the names of the purchasers, and the price received for each item should be transmitted to the United States Trustee and filed with the clerk of the bankruptcy court. If the property is sold by an auctioneer, the auctioneer must file the statement. If the property is not sold by an auctioneer, the trustee must file the statement. Fed. R. Bankr. P. 6004(f)(1).

#### 2-2.5.10.6 Periodic Payments

Estate assets in the form of periodic, future payments due to extend beyond one year require special consideration. This type of asset may be part of the debtor's estate (e.g., note or mortgage receivable) or may arise when a trustee accepts periodic payments to sell an asset.

Generally, the trustee should avoid sales of estate assets involving buyer payments which will extend beyond one year. However, there may be instances, such as the need for periodic payments which do not delay case closing, when it is

in the best interest of the estate to sell an estate asset in this manner. When the purchase price will be paid in installments, the trustee also should obtain and perfect a security interest in the estate assets sold and take other suitable precautions to protect the estate against default.

When an asset comes into the estate that involves future payments, the trustee should attempt to discount the future income stream to an appropriate present value and liquidate the asset as expeditiously as possible. If the discounted payments cannot be liquidated, or the asset cannot otherwise be assigned for the benefit of creditors, the trustee should consider interim distributions to creditors as funds become available, provided that claims are resolved and sufficient funds are reserved to administer the estate.

#### 2-2.5.11 **Review of Claims**

A trustee should commence the claims review process after it is certain that there will be a distribution to creditors and as soon as possible following the expiration of the bar date for filing claims. In no event should the final report be filed prior to completion of the claims examination and determination process.

##### 2-2.5.11.1 **Objections to Claims**

Section 704(5) requires a trustee to examine proofs of claim and object to the allowance of any claim that is improper. The trustee should consider the following issues when reviewing claims:

1. If a claim is filed as secured, there should be appropriate documentation, e.g., security agreement and UCC-1 financing statement. The trustee should review this documentation to determine whether the secured creditor's lien is subject to avoidance pursuant to § 544. The trustee should verify that the claim was properly perfected at least 90 days prior to the filing (one year for insiders). The trustee may be able to avoid a lien perfected within 90 days (or one year) pursuant to § 547. It should be noted that a secured creditor is not required to file a proof of claim. Fed. R. Bankr. P. 3002(a). Therefore, prior to selling estate assets, the trustee ordinarily should perform a lien search to verify that all liens have been identified.

2. Tax claims should be verified. In most instances, a taxing entity will file only one claim which may include liens as well as priority and general unsecured taxes. In some instances, the liens may be subordinated to other classes of claims.
3. Unsecured claims should be reviewed for appropriate documentation, accuracy and timeliness.
4. Judgments and liens listed in the schedules should be compared to claims that are filed.

A trustee should file objections to allowance of claims, if appropriate. Fed. R. Bankr. P. 3007. Possible reasons for objecting to a claim include:

1. Sufficient documentation was not provided;
2. The claim amount is in error;
3. The claim has been previously paid;
4. The claim is not owed;
5. The claim is a duplicate of another claim; or
6. The claim is filed late.

Other grounds for objection may be found in § 502.

The trustee should perform a second review for new, tardy, and/or amended claims prior to distribution. See § 726(a)(1) regarding tardily filed priority claims.

#### 2-2.5.11.2 Unpaid Quarterly Fees

When a chapter 11 case is converted to a case under chapter 7 there may be unpaid fees due to the United States Trustee pursuant to 28 U.S.C. § 1930(a)(6). The United States Trustee should file a proof of claim or request for payment with the clerk of the bankruptcy court for the period(s) when appropriate payments were not made by the debtor. In appropriate cases, the United States Trustee should ask the trustee to review the debtor's books and records to determine the appropriate amount of unpaid fees.

## 2-2.5.12 Subordination of Claims

The Bankruptcy Code empowers the trustee to obtain a court order subordinating certain claims to other claims for purposes of distribution.

### 2-2.5.12.1 Section 510(a) - Agreements

Section 510(a) empowers the trustee to enforce subordination agreements to the extent they are enforceable under non-bankruptcy law.

### 2-2.5.12.2 Section 510(b) - Purchase or Sale of Stock

Section 510(b) subordinates claims arising from rescission of a purchase or sale of stock, or the purchase or sale of stock, to all claims or interests that are senior or equal to the claim or interest represented by such security.

### 2-2.5.12.3 Section 510(c) - Equitable Subordination

Section 510(c) empowers the trustee to seek subordination of a claim under principles of equitable subordination. Generally, equitable subordination requires misconduct on the part of the creditor that has injured the debtor or conferred an unfair advantage on the creditor.

### 2-2.5.12.4 Section 724(b) - Subordination of Tax Liens

Section 724(b) allows the trustee to subordinate tax liens to § 507(a)(1)-(7) priority claims up to the amount of the tax liens. Under this section, the proceeds received from property subject to tax liens are distributed as follows:

1. First, to the holders of liens senior to the tax liens;
2. Second, to the holders of unsecured priority claims senior to priority tax claims, but only up to the amount of the tax lien claim;
3. Third, to the holder of the tax lien to the extent that the amount of the tax lien exceeds the amount distributed under the previous paragraph;
4. Fourth, to the holders of liens that are junior to the tax lien;

5. Fifth, to the holder of the tax lien, to the extent the tax lien has not been paid under the third paragraph above; and
6. Sixth, to the estate.

### 2-2.5.13 **Redemption**

Under § 722, an individual debtor may redeem tangible personal property (intended primarily for personal, family, or household use) from a lien securing a consumer debt. “Consumer debt” means debt incurred by an individual primarily for personal, family, or household purposes. § 101(8). Because § 722 applies only to personalty, a consumer debt for purposes of § 722 does not include a debt to the extent that it is secured by real property. The debt secured by the lien must also be dischargeable.

Redemption was intended by Congress to protect debtors against ill-advised reaffirmations and the high replacement cost of consumer goods. Section 722 allows debtors to retain necessary property, such as furniture, clothing, cooking utensils, and other household items, and thereby avoid the high replacement cost that might be required if the secured creditor repossessed the collateral. See H.R.Rep. No. 595, 95th Cong., 1st Sess. 127 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6088. Debtors may redeem collateral securing a debt by paying the creditor the amount of the secured claim or the fair market value of the collateral, whichever is less, in exchange for a release or satisfaction of the lien. Redemption of property cannot be waived and applies only if a debtor’s interest in the property is exempt under § 522 or has been abandoned pursuant to § 554.

Fed. R. Bankr. P. 6008, which implements the provisions of § 722, specifically provides that “the court may authorize redemption of property from a lien or from a sale to enforce a lien in accordance with applicable law” when requested by a debtor, trustee, or debtor in possession. Fed. R. Bankr. P. 6008. Recent cases hold that redemption agreements require bankruptcy court approval under Fed. R. Bankr. P. 6008, notwithstanding the fact that the debtor and secured creditor may agree on the redemption price and value of the collateral. See, e.g., In re White, 231 B.R. 551 (Bankr. D. Vt. 1999); In re Spivey, 230 B.R. 484 (Bankr. E.D.N.Y. 1999); In re Lopez, 224 B.R. 439 (Bankr. C.D. Cal. 1998). Any dispute as to the amount of the claim or value of the collateral must be resolved as a contested matter. Fed. R. Bankr. P. 6008; 9014. The right to redeem extends to the whole of the property, not just the debtor’s exempt interest in it. In re Fitzgerald, 20 B.R. 27 (Bankr. N.D.N.Y. 1982). The majority of courts hold that, unless the creditor agrees otherwise, the redemption amount must be paid in a lump sum

rather than installments. See, e.g., In re Bell, 700 F.2d 1053 (6<sup>th</sup> Cir. 1983); In re Polk, 76 B.R. 148 (B.A.P. 9<sup>th</sup> Cir. 1987). Debtors who are unable or unwilling to redeem property under § 722 may, under § 524(c) and (d), negotiate an agreement with the creditor to reaffirm the debt and retain possession of the collateral.

#### 2-2.5.14 **Reaffirmation**

A debt that is properly reaffirmed will not be discharged and, under § 524(c) and (d), may be enforced even after a discharge is granted to the debtor.

Reaffirmation agreements are strictly construed to protect a debtor from overreaching by a creditor. To be enforceable, a reaffirmation agreement must: (1) be entered into before the granting of a discharge; (2) contain a clear and conspicuous statement concerning the debtor's right to rescind the agreement at any time before discharge or within sixty days after the agreement is filed with the court, whichever is later; (3) be filed with the court; and (4) not have been rescinded by the debtor. § 524(c). If applicable, the agreement must be accompanied by a declaration or affidavit of the attorney who represented the debtor during the course of negotiating the agreement. The affidavit or declaration must state that (1) the agreement represents an informed, voluntary agreement by the debtor; (2) it does not impose an undue hardship on the debtor or the debtor's dependents; and (3) the attorney fully advised the debtor of the legal effect and consequences of the reaffirmation agreement and any default thereunder. § 524(c)(3).

When an individual debtor is not represented by an attorney in the course of negotiating the reaffirmation agreement, the court must hold a hearing, which the debtor must attend, to determine whether the agreement imposes an undue hardship on the debtor and the debtor's dependents, and whether the agreement is in the debtor's best interests. §§ 524(c)(6)(A) and (d). Such a hearing is normally triggered by the filing of a motion for approval of the reaffirmation agreement. Section 524(c)(6)(A) does not apply to the extent that a debt is a consumer debt secured by real property. § 524(c)(6)(B).

Only the debtor has standing to seek approval of a reaffirmation agreement. Fed. R. Bankr. P. 4008. A reaffirmation agreement that fails to comply with § 524(c) and (d) is void and unenforceable. Courts have declined to approve reaffirmation agreements where there is evidence that the debtor will not be able to make the payments required by the agreement, the security agreement is invalid, or the secured debt exceeds the value of the collateral. See, e.g., In re Carlos, 215 B.R. 52 (Bankr. C.D. Cal. 1997); In re Bryant, 43 B.R. 189 (Bankr. E.D. Mich. 1984); In re Delano, 7 B.R. 72 (Bankr. D. Me. 1980). Reaffirmation should rarely be



recommended by an attorney or approved by the court if the sole reason for the reaffirmation is the debtor's desire to repay a discharged debt. The debtor has an absolute right to voluntarily repay such a debt notwithstanding a discharge of indebtedness. See In re Berkich, 7 B.R. 483 (Bankr. E.D. Pa. 1980).

To combat abuses in the reaffirmation process, the United States Trustee should:

1. Post signs in section 341 meeting rooms notifying debtors concerning the effect of reaffirmation. Example: "Notice: Any agreements to repay debts ARE NOT VALID unless filed with the Bankruptcy Court. Repayment agreements signed by debtors who do not have attorneys ARE NOT VALID unless filed with and approved by the Bankruptcy Court."
2. Verify that the trustees are orally examining debtors at creditors' meetings as required by § 341(d) to ensure that debtors are aware of, among other things, the effect of reaffirming a debt and the requirements of § 524(d).
3. Have the trustees inquire at the section 341 meeting about any reaffirmations and inform the debtor that reaffirmation is not required and that any reaffirmation can be rescinded.
4. Prohibit creditors from soliciting reaffirmations, redemptions or the surrender of property "off the record" in the section 341 meeting room. This would not, however, prohibit the trustee from ensuring that the debtor carried out their stated intentions under § 521(2)(B).
5. Seek a disgorgement of fees when debtors' attorneys fail to fulfill their duties under § 524(c). To prevent creating a disincentive to contesting dischargeability actions and to discourage debtors' attorneys from encouraging reaffirmations to avoid the litigation, the United States Trustee should recognize the attorney's right to a reasonable fee for defending dischargeability complaints.

These steps will enable the United States Trustee to exercise greater control over section 341 meetings, reduce the potential for reaffirmation abuse, and increase the likelihood that debtors will understand the reaffirmation process and the effect of reaffirmation as required by § 341(d).

## 2-2.6 **TAX CONSIDERATIONS**

### 2-2.6.1 **Overview**

Sections 346 and 728 of the Bankruptcy Code, as well as § 1398 and § 1399 of the Internal Revenue Code, 26 U.S.C. § 1, *et. seq.*, set forth special tax provisions with which the trustee should be familiar. These sections generally provide that the trustee must prepare and file appropriate income tax returns for any estate income earned during the administration of the estate. (If the debtor has not already done so, the trustee also may consider filing prepetition tax returns, especially where it appears the estate would be entitled to a refund. The trustee cannot sign an individual tax return for a period that ended before the bankruptcy filing. If the debtor will not sign the return, the trustee can have the returns prepared and then ask the taxing authority to file the return.)

In preparing estate tax returns, the trustee should review the debtor's prior year returns. If the debtor is unwilling or unable to provide copies of these returns, the trustee can request copies from the IRS using Form 4506. Such requests should be directed to the Service Center where the debtor's tax returns were filed. 26 U.S.C. § 6103(e)(4)-(5).

Under certain limited circumstances, the IRS may grant the trustee relief from filing a particular estate tax return. The trustee should consult the IRS Special Procedures Unit for further information. *See* Rev.Rul. 84-123, 1984-2 Cum. Bull. 244 and Rev. Proc. 84-59, 1984-2 Cum. Bull. 504.

### 2-2.6.2 **Individual Chapter 7 Debtors**

For both federal and state tax purposes, the individual and the bankruptcy estate are treated as separate taxable entities, and a separate tax identification number is required for the estate. If a husband and wife file a joint petition under § 302, absent substantive consolidation, two separate estates and two separate taxable entities are created. Each estate obtains its own tax identification number and files its own tax returns.

The trustee must file a federal income tax return in an individual chapter 7 case for any year in which gross income of the estate equals or exceeds the exemption amount under 26 U.S.C. § 151(a) plus the basic standard deduction under 26 U.S.C. § 63(c)(2)(D) for a taxpayer filing as married filing separately. (For example, the filing threshold for 1997 is \$6,100.) The trustee also must file state income tax returns if the estate of an individual debtor has net taxable

income for the entire period after the order for relief during which the case is pending. § 728(b).

The trustee files a return for an individual's estate using Form 1041 (U.S. Income Tax Return for Estates and Trusts) as a transmittal form with a Form 1040 (U.S. Individual Income Tax Return) together with appropriate forms and schedules. The tax to the estate is computed generally in the same manner as for an individual and the rate schedules used are those for married individuals filing separate returns under 26 U.S.C. § 1(d), pursuant to 26 U.S.C. § 1398(c). For joint debtors, a separate Form 1041 and the related attachments are filed for each spouse's estate.

The gain on the sale of an individual chapter 7 debtor's residence is excluded from gross income of the debtor's bankruptcy estate to the extent provided by 26 U.S.C. § 121. The estate succeeds to the holding period and character of the property under 26 U.S.C. § 1398(g)(6), and the estate is treated as the debtor with respect to such asset under 26 U.S.C. § 1398(f)(1). See In re Bradley, 222 B.R. 313, 318 (Bankr. M.D. Tenn. 1998); In re Popa, 218 B.R. 420, 428 (Bankr. N.D. Ill. 1998), aff'd sub nom. Popa v. Peterson, 238 B.R. 395 (N.D. Ill. 1999).

The estate is entitled to deduct administrative expenses allowed under § 503 and any fees and charges assessed by the court as itemized deductions to the extent such deductions are not otherwise disallowed by other provisions of the Internal Revenue Code. 26 U.S.C. § 1398(h).

The debtor's tax attributes are transferred to the estate upon commencement of the case. The attributes are determined as of the first day of the taxable year in which the petition is filed, generally this is January 1<sup>st</sup> of the year of filing, but if the debtor makes a short-year election, the attributes are determined as of the date of filing. The debtor's discharge may affect the use of tax attributes by the estate. Consideration should be given to the effects of 26 U.S.C. § 108 on the debtor's tax attributes.

The debtor in an asset case can make a short-year election which terminates the debtor's taxable year on the date before the petition is filed and begins a second taxable year on the date of filing. 26 U.S.C. § 1398(g)(2). If the debtor makes this election, any tax owing for the prepetition short year is treated as a priority tax claim against the estate.

The trustee has the option to follow the individual debtor's taxable year (usually the calendar year) or adopt a fiscal taxable year. 26 U.S.C. § 1398(j)(1). The

trustee also is permitted to change the estate's annual accounting period once without the approval of the Secretary of the Treasury, as otherwise required. These options enable the trustee to do some tax planning to minimize any tax liability and to expedite closure of the case.

The trustee must disclose to the debtor all information contained in the estate tax returns that can affect the debtor's future or past returns since the debtor acquires the tax attributes of the estate upon its closing.

### 2-2.6.3 **Partnership and Corporate Chapter 7 Debtors**

(Note: Limited liability corporations (LLCs) and limited liability partnerships (LLPs) are treated the same as partnerships.)

The filing of a bankruptcy petition by a partnership or corporation does not create a separate taxable entity. There is no break in the accounting period of the partnership or corporation and the return, filed under the debtor's tax identification number, must reflect the pre- and postpetition income and deductions. The trustee files a corporate income tax return using Form 1120 (U.S. Corporate Income Tax Return) or Form 1120S (U.S. Income Tax Return for an S Corporation) and a partnership tax return on Form 1065 (U.S. Partnership Income Tax Return), with appropriate forms and schedules attached to each.

Unless a corporation is exempt from income tax under 26 U.S.C. § 501(a), corporate returns must be filed by the trustee regardless of whether the corporation has income. 26 U.S.C. § 6012(a). The trustee must file state income tax returns for a corporation unless the corporate debtor lacks postpetition net taxable income for the entire period after the order for relief during which the case is pending. § 728(b). Upon application to the IRS District Director, the IRS may waive the requirement to file federal returns if the corporate debtor has ceased business operations and has neither assets nor income. See Rev. Rul. 84-123, 1984-2 Cum. Bull. 244 and Rev. Proc. 84-59, 1984-2 Cum. Bull. 504.

For partnership cases, the chapter 7 trustee must file the federal and state tax returns regardless of the amount of gross income.

### 2-2.6.4 **Employment Taxes and Other Tax Forms**

If the debtor was an employer, the trustee must file any Form 941 (Employer's Quarterly Federal Tax Return), for withheld federal income and FICA taxes, or Form 940 (Employer's Annual Federal Unemployment Tax Return), for

unemployment taxes, that was not filed by the debtor before commencement of the bankruptcy case. A failure to file these returns may lead to the imposition of penalties against the trustee or the estate.

In addition, the trustee must withhold all applicable federal and state income, social security, and medicare taxes from any wage claims paid by the estate. The taxes must be properly and timely deposited with a financial institution or paid with the return. Further, depending upon the business the debtor conducted, the trustee may need to file sales, excise and other tax returns in order to establish the amount of the taxing authority's claim.

The trustee may also have to file information returns (Form 1099 series) if certain payments are made. For example, Form 1099-INT must be supplied to the payee and to the IRS when a trustee makes a payment of interest aggregating \$10 or more. 26 U.S.C. § 6049. Similarly, the trustee may be required to file Form 1099-MISC when \$600 or more in fees are paid to attorneys, accountants and other professionals for their work in assisting in the administration of the estate. Payments made to an attorney where the attorney's fee cannot be determined (such as payment of a settlement) must be reported to the IRS and the attorney without application of the \$600 limitation.

#### 2-2.6.5 **Employee W-2 Forms**

If the trustee pays wages, including prepetition wage claims, the trustee is responsible for preparing and filing W-2 forms for the wages paid and for sending copies to the employees. For those cases in which the trustee does not pay any wages, but wages were paid by the debtor during the calendar year of the bankruptcy petition, the trustee will receive requests from the employees for wage withholding information in order to complete their personal income tax returns. In these circumstances, the trustee may complete W-2 forms to give to the employees based on the corporate records or may make those records available to the former employer or former employees to assist them in reconstructing the information. In any event, if an employee is unable to obtain Form W-2 for wages paid by the debtor prepetition, the employee should be instructed to secure Form 4852 from the IRS and attach it to Form 1040 in order to obtain credit for the estimated amount of taxes withheld. For further information, the trustee should consult IRS Circular E (The Employer's Tax Guide).

### 2-2.6.6 **Sales and Abandonments**

When estate property is sold, the estate recognizes a taxable gain or loss. Any resulting tax liability is treated as an administrative expense. As previously noted, the gain on the sale of an individual chapter 7 debtor's residence is excluded from gross income of the debtor's bankruptcy estate to the extent provided by 26 U.S.C. § 121. The estate succeeds to the holding period and character of the property under 26 U.S.C. § 1398(g)(6), and the estate is treated as the debtor with respect to such asset under 26 U.S.C. § 1398(f)(1). See USTM 2-2.6.2.

The trustee should abandon assets that will not generate net proceeds sufficient to pay any tax liability generated by the sale. For example, the estate is liable for any tax gain upon the sale of property, even if the proceeds are abandoned. See In re Bentley, 916 F.2d 431 (8<sup>th</sup> Cir. 1990). In an individual case, the estate also is liable for any taxable gain from foreclosure after relief from the automatic stay is granted if the property is not abandoned before the foreclosure sale.

Some courts have held that when a trustee abandons property of an individual's chapter 7 estate, whether during the bankruptcy under § 554(a) or at the close of the case under § 554(c), the abandonment is a tax-free transaction and any tax liabilities resulting from the subsequent disposition of the property are borne by the individual. Thus, if an asset is sold or foreclosed upon after abandonment, any tax liabilities as a result of the sale or foreclosure are the responsibility of the debtor, not the trustee. For the minority view, see In re A.J. Lane & Co., Inc. 133 B.R. 264 (Bankr. D. Mass. 1991); In re Rubin, 154 B.R. 897 (Bankr. D. Md. 1992). The abandonment of or failure to abandon property by the trustee in a corporate or partnership case does not affect the tax consequences to the estate of a subsequent sale or foreclosure.

### 2-2.6.7 **Failure to Pay**

The trustee should be mindful of the obligation to file appropriate returns and to pay tax liabilities on behalf of the estate. See generally, Howard, *An Overview of the State and Federal Tax Responsibilities of Bankruptcy Trustees and Debtors*, 93 Com. L.J. 43 (1988). A trustee who fails to comply with the federal withholding provisions runs the risk of being held personally liable for trust fund taxes not collected and paid over to the government. Similarly, the trustee may be held personally liable when an estate does not have sufficient funds to pay the taxes due from the sale of estate assets. See, e.g., In re San Juan Hotel Corp., 847 F.2d 931 (1<sup>st</sup> Cir. 1988) (trustee surcharged interest and penalties incurred by the estate for failing to seek out and pay estate taxes where sufficient funds

existed to pay them); In re Sapphire Steamship Lines, 762 F.2d 13 (2d Cir. 1985) (non-operating trustee of a corporate debtor's estate required to make estimated quarterly payments).

In some circumstances, the trustee can seek relief under 26 U.S.C. § 6658 from having penalties imposed under 26 U.S.C. §§ 6651, 6654, or 6655 for failure to pay certain taxes. Such relief is conditioned on showing that (a) the failure to pay taxes incurred by the estate resulted from a court order finding probable insufficiency of funds or (b) the tax was incurred by the debtor prepetition, and either the petition was filed prior to the tax return due date or the penalty was imposed after the petition was filed. 26 U.S.C. § 6658(a). However, relief under this section is not available for cases involving the failure to pay employment taxes. 26 U.S.C. § 6658(b).

#### 2-2.6.8

#### **Quick Audits**

Under § 505(b), the trustee may request determination of unpaid estate liabilities for any taxes incurred during the administration of the case by filing the tax return and requesting that determination from the appropriate tax agency. The procedure, which is known as the “quick audit,” allows the trustee to wind-up the administration of the case expeditiously.

In the case of federal taxes, the trustee must file a written application with the IRS District Director for the district where the bankruptcy case is pending. The application must be submitted in duplicate and executed under penalty of perjury. The application must be accompanied with an exact copy of the return(s) filed by the trustee and a statement as to where the original return(s) were filed. Any tax shown owing on the return must have been paid. The envelope should be marked: “For the Personal Attention of the Special Procedures Function. DO NOT OPEN IN MAILROOM.”

The agency must give notice within 60 days that the return has been selected for audit and has a total of 180 days to complete the examination unless an extension of time is granted by the court. If the agency does not give notice or complete its examination within the applicable time limits, the trustee is discharged from liability, absent fraud or a material misrepresentation in the return. The trustee also is discharged upon paying the tax determined to be due by the agency or by the court upon completion of the quick audit.

Revenue Procedure 81-17, 1981-1 Cum. Bull. 688 should be consulted for the quick audit procedures applicable to federal taxes.

## 2-2.7

**EMPLOYMENT AND SUPERVISION OF PROFESSIONALS**

Under § 327, a chapter 7 trustee may employ professionals, including attorneys, accountants, appraisers or auctioneers to “represent or assist the trustee” in performing trustee duties under title 11. Those professionals may be awarded compensation for actual and necessary services and reimbursement for actual and necessary expenses, pursuant to § 330.

The employment of professionals must be approved by the court. Court approval should be sought prior to the rendering of any services. Issues such as disinterestedness and necessity of employment are more appropriately addressed when court approval is sought and obtained prior to work by the professional. Generally, courts do not authorize compensation for services rendered prior to court-ordered employment. However, some courts permit retroactive or *nunc pro tunc* orders of employment in special circumstances, but even where permitted, such orders should be rarely sought.

## 2-2.7.1

**Definition of Professionals**

The list of “professional persons” provided by § 327(a) – attorneys, accountants, appraisers, auctioneers – is not exhaustive. A trustee must seek court approval only if the person sought to be employed is a “professional person” within the scope of § 327(a). A trustee may find it necessary to employ brokers, underwriters, farm managers, private investigators, etc. If an issue arises regarding the need to obtain court approval of the employment, the following factors should be considered:

- Does the person play a central role in the administration of the estate?
- Does the person possess discretion or autonomy over some part of the estate?
- Does the person have special knowledge or skill usually achieved by study and educational attainments?
- Does the person operate under a license or governmental regulation?

Trustees should be advised to err on the side of caution and seek court approval of the employment. To obtain compensation from the estate, a “professional person” must be employed with court approval.



### 2-2.7.2 **Employment Standards**

The threshold question for the employment of any professional is the necessity of employment. Although many trustees may be attorneys or accountants, the allowance of statutory compensation for a trustee does not contemplate the trustee rendering legal or accounting services to the estate. Conversely, professionals are not to do ministerial work or perform the duties of a trustee.

Accounting services normally are required when the debtor is a corporation or an individual engaged in business, or when a trustee liquidates assets which generate tax consequences and require the filing of a tax return on behalf of the estate. Common accounting services include reviewing the debtor's books and records for preferences and fraudulent transfers, preparing and filing tax returns, and determining whether a tax refund is due to the estate.

The United States Trustee should scrutinize employment applications to determine whether the services of a professional are needed and whether the cost is warranted. The United States Trustee should also determine at the outset the level of professional work required and the estimated costs and benefits associated with the work.

As a general rule, professional persons employed by a trustee must be disinterested and must not have an interest adverse to the estate. §§ 327(a) and 101(14). There are some exceptions. If a trustee is authorized to operate the debtor's business under § 721, and if the debtor has regularly employed professional persons on salary, the trustee may retain or replace such professional persons. § 327(b). Representation of a creditor does not disqualify a person from representing the trustee, unless there is an objection from another creditor or the United States Trustee and the court finds there is an actual conflict of interest. § 327(c). The trustee may retain an attorney for a "specified special purpose," even though the attorney previously represented the debtor, if the attorney does not hold or represent an adverse interest to the debtor or the estate with respect to the subject matter of the employment. § 327(e).

The employment of a professional with a conflict of interest can result in denial of compensation to the professional under § 328(c) and to the trustee under § 326(d).

The trustee may not employ a person who has served as an examiner in the case. § 327(f).

### 2-2.7.3 **Employment Procedures**

Section 327 does not require notice and hearing procedures to hire professionals, only court approval. The trustee must provide a copy of the employment application to the United States Trustee, Fed. R. Bankr. P. 2014(a), and the United States Trustee should review the application and order before they are approved by the court.

The form of applications for employment are governed by Rules 2014 and 6005 of the Federal Rules of Bankruptcy Procedure. An employment application must:

1. the specific facts necessitating employment;
2. the name of the person employed;
3. the reasons for selecting the firm or individual;
4. the professional services to be rendered;
5. the proposed arrangements for compensation; and
6. the professional's connections with the trustee, debtor, creditors, and other parties in interest.

Fed. R. Bankr. P. 2014. The application should be accompanied by a verified statement of the person to be employed setting forth the person's connections with the debtor, creditors, any other party in interest, including the trustee, their respective attorneys and accountants, the United States Trustee, or any person employed by the United States Trustee. Fed. R. Bankr. P. 2014(a).

Fee sharing arrangements are prohibited. § 504. The United States Trustee should object to an employment application providing insufficient justification for employment of a professional. If there is any question as to the necessity for legal or accounting services, the United States Trustee should object to the application.

### 2-2.7.4 **Supervision of Professionals**

The trustee is a fiduciary and representative of the estate. Trustees cannot avoid or abdicate their responsibilities by employing professionals and delegating to them certain tasks. It is critical that the trustee oversees the work performed by professionals and exercises appropriate business judgment on all key decisions.

The trustee must actively supervise estate professionals to ensure prompt and appropriate execution of duties, compliance with required procedures and reasonable and necessary fees and expenses.

The trustee is advised to pay particular attention to the activities of professionals who are not closely regulated by state authorities or who take physical possession of estate property and funds, such as auctioneers, liquidators, brokers, collection agents and property managers. The general standards for supervising auctioneers apply equally to other professionals who take possession of estate funds and property. See USTM 2-2.7.6.1.

#### 2-2.7.5

#### **Trustee as Attorney or Accountant for the Estate**

A trustee, with court approval, may act as an attorney or accountant for the estate if such employment is in the best interest of the estate. § 327(d). Routine matters may be handled quickly and economically by this kind of representation. However, a trustee should be sensitive to the best interest of each individual estate and the conflict of interest problems that may be posed by acting as an attorney or accountant for the estate. The trustee should not be employed as counsel to provide services that a trustee could perform without the assistance of counsel. If there is any question as to the necessity for legal or accounting services, the United States Trustee should object to the employment application. A form application to employ the trustee as a professional in every case without specifying the necessity for the services to be provided is subject to an objection by the United States Trustee.

If a trustee acts as attorney or accountant, detailed time records of the tasks performed as trustee and as attorney or accountant must be maintained. A trustee acting as an attorney or accountant under § 327(d) may receive compensation only for services performed in that capacity and not for the performance of regular trustee duties. § 328(b).

The importance of distinguishing trustee duties from attorney or accountant for trustee functions cannot be overemphasized. The demarcation of the roles of the trustee and the professional is made to ensure that an estate incurs only appropriate costs for administration. It also serves to ensure that the trustee and the trustee's attorney or accountant keep to their respective functions in administering a bankruptcy case. The law imposes upon the trustee the primary responsibility to administer the estate and provides a mechanism for compensating the trustee, pursuant to §§ 326 and 330, in return for carrying out these responsibilities. The cost of administration and its financial effect upon

creditors demands careful scrutiny of the trustee's application to employ themselves or others. The question of necessity is best addressed *prior* to services being rendered. Applications that do not sufficiently justify employment of an attorney or accountant should prompt objections. Abuses in the process of a trustee serving dually as attorney or accountant may be the basis for suspension or removal from the panel. Requiring a dual capacity trustee to keep time and service entries as professional *and* trustee aids in maintaining the distinction between the trustee and the employed professional.

Attorneys and accountants may not be compensated for performing the statutory duties of the trustee. See § 704, Fed. R. Bankr. P. 2015(a). The following list includes examples of services considered to fall within the duties of a trustee:

1. preparing for and examining the debtor at the section 341 meeting in order to verify factual matters;
2. examining proofs of claim to eliminate duplicate claims and to identify those that are in addition to or differ in amounts from claims listed on the debtor's schedules;
3. investigating the financial affairs of the debtor;
4. furnishing information to parties in interest on factual matters;
5. collecting and liquidating assets of the estate by employing auctioneers or other agents and soliciting offers;
5. preparing required reports;
6. performing banking functions; and
7. supervising professionals.

The aforementioned trustee duties are not compensable as legal or accounting services unless sufficiently documented to show that special circumstances exist.

## 2-2.7.6 Retention of Auctioneers

### 2-2.7.6.1 General Standards

The trustee may employ auctioneers as professional persons pursuant to §§ 327(a) and 328(a) to sell property of the estate. All auction sales must be noticed pursuant to Rule 6004(a). Fed. R. Bankr. P. 6004(a).

The trustee must actively supervise the activities of the auctioneers to ensure that estate property is protected against loss, that property is sold for reasonable prices to independent buyers, that auction proceeds are promptly and fully remitted, that auctioneers timely submit accurate sale reports, and that auctioneer expenses are actual and necessary and paid in accordance with legal requirements. Methods by which a trustee can supervise auctioneers include personally attending auction sales, thoroughly reviewing auctioneer reports, and independently verifying reported information. The trustee should advise the United States Trustee of concerns with respect to auctioneers and must report situations which could result in a loss to the estate. Failure to appropriately supervise auctioneers may result in claims against the trustee individually.

A representative of the United States Trustee should periodically attend auctions to ensure that the sales are conducted in a proper manner and are free from coercion or other irregularities.

### 2-2.7.6.2 Compensation

An auctioneer's compensation must be approved by order of the court. § 328, Fed. R. Bankr. P. 6005. Any buyer's premium must be fully disclosed in the employment application and considered in determining the reasonableness of the total compensation.

Although auctioneers, outside of a bankruptcy context, usually deduct their commissions and expenses from the sales proceeds and remit a net amount to the seller, this practice may not be employed with regard to bankruptcy estate funds, unless it is specifically authorized by order of the court. However, the order authorizing the employment may specify the percentage fee to be charged by the auctioneer and authorize the deduction of the commission and the costs of sale from the sales proceeds, with the effect of the auctioneer remitting the net sales proceeds to the trustee. In those cases, the auctioneer must present an affidavit or declaration listing all costs and expenses incurred with the report of sale.

### 2-2.7.6.3 Bonding and Insurance

The trustee must ensure that auctioneers are adequately bonded, prior to taking possession of estate property, in an amount that is sufficient to cover all receipts from the sale. The bond should be in favor of the United States of America and is distinct from any other auctioneer's bond required under state law. The amount of the bond will be established by local bankruptcy rule or the United States Trustee. The trustee should contact the United States Trustee to ensure that the auctioneer is bonded in an appropriate amount to cover all estates in which the particular auctioneer has been employed. All original bonds should be forwarded to the United States Trustee. See USTM 2-3.10.7.

The trustee also should determine if the auctioneer maintains insurance for lost or stolen property, since the trustee may wish to make a claim against the insurer for any such losses.

When the auctioneer assumes control over estate property for a period of time prior to sale, the trustee should keep an inventory of the items stored and periodically verify that the assets still exist and are in good condition. Insurance claims for lost or stolen property should be made promptly, and the trustee should inform the United States Trustee of such claims.

The United States Trustee should object to any application to employ an auctioneer if the trustee fails to comply with the foregoing.

### 2-2.7.6.4 Turnover of Proceeds

The auctioneer must not commingle auction proceeds with business, personal or other accounts.

Whenever possible, the auctioneer should immediately turn over auction proceeds to the trustee. In any event, all proceeds must be turned over within thirty (30) days of the auction. If an auctioneer fails to account for or to turnover auction proceeds within thirty (30) days, the trustee should promptly notify the United States Trustee and take immediate action to recover the funds, including initiating a proceeding against the auctioneer's bond.

### 2-2.7.6.5 Auctioneer's Report

The auctioneer must submit an itemized statement of the property sold, the name of each purchaser, and the price received for each item, lot, or for the property as a

whole if sold in bulk. Fed. R. Bankr. P. 6004(f). The trustee must ensure that the auctioneer's report is promptly submitted upon completion of the auction. If the report has not been provided within thirty (30) days after the auction, the trustee should request a copy and ensure that it has been filed with the court and United States Trustee, or as otherwise provided by local rules and practices.

The trustee must compare the auctioneer's report to the initial inventory and obtain an explanation for any discrepancies. The trustee also should scrutinize items marked 'stolen' or 'missing.' As noted earlier, the trustee should attempt to recover the value of lost or stolen items by filing a claim with the auctioneer's insurer or by initiating a proceeding against the auctioneer's bond, as appropriate.

#### 2-2.7.7 **Retention of Appraisers**

A trustee may require the services of an appraiser to ascertain the value of property of an estate. For economy of administration, trustees may use alternative means of valuation if feasible, but the basis for the evaluation must be documented. Alternative evaluation means include the NADA book for automobiles; information acquired from real estate agents, as well as county records regarding recent sales of comparable real property; or advertisements for the sale of like goods.

#### 2-2.8 **COMPENSATION OF TRUSTEES AND PROFESSIONALS**

Pursuant to 28 U.S.C. § 586(a)(3), as amended, the United States Trustee reviews applications for compensation and reimbursement of expenses filed by trustees and professionals in accordance with the procedural guidelines adopted by the Executive Office for United States Trustees. See 28 C.F.R. Part 58 Appendix A. These Fee Guidelines are included with this Manual at Appendix 2-8.

The United States Trustee objects to requested fees and expenses as appropriate. Objections to fee applications should not be solely based on the Fee Guidelines, but rather upon the Bankruptcy Code and Rules or applicable case law.

#### 2-2.8.1 **Compensation of Trustees**

Trustee compensation is governed by § 330, subject to the limitations set forth in § 326. The maximum compensation allowable set forth in § 326 consists of varying percentages of all moneys disbursed or turned over in the case by the trustee to parties in interest, excluding the debtor, but including holders of secured claims. In a joint case consisting of two separate estates, the limitation applies to

the entire case, not to each estate separately. In addition, trustee duties performed by a paraprofessional employed by the trustee are also subject to the § 326(a) limit on trustee compensation. Boldt v. United States Trustee (In re Jenkins), 130 F.3d 1335, 1342 (9<sup>th</sup> Cir. 1997).

A court may award a trustee less than the statutory maximum based upon the considerations in § 330, but may not exceed the compensation ceiling in § 326(a). The trustee also receives a portion of the filing fee when administration of the case is complete. The trustee should keep time records in every asset case as evidence of the services performed. However, local rules and practices sometimes provide that time records need not be submitted if the compensation request is under a specified amount.

#### 2-2.8.2 **Interim Compensation of Trustees**

Section 331 permits a trustee to apply to the court for interim compensation or reimbursement of expenses pursuant to § 330. Section 326(a) provides a cap to the trustee's compensation based upon all funds disbursed by the trustee. A literal reading of § 326 requires that a trustee receive compensation only after a disbursement to parties in interest. Nonetheless, a line of cases has developed, allowing interim reasonable compensation to trustees in certain circumstances, although distribution may not have been made to any creditor. The United States Trustee should carefully examine a trustee's request for interim compensation and object as warranted.

The United States Trustee should ordinarily object to a trustee's application for interim compensation unless the application is linked to an interim distribution to creditors. However, when a trustee is heavily engaged in the administration of a case over an extended period of time and the trustee is providing substantial services to the estate, those factors may present good cause for interim compensation to the trustee.

#### 2-2.8.3 **Compensation of Professionals**

Section 330(a) authorizes professionals employed by the trustee under § 327(a) to be compensated from the estate for actual services rendered that are necessary to the administration of a case or beneficial at the time at which the service was rendered toward completion of the case. Professionals should not be compensated for performing work that the trustee can do without professional assistance. In re Spungen, 168 B.R. 373 (N.D. Ind. 1993). Particular care must be taken to avoid



“double-dipping” when the trustee also serves as an attorney or accountant in a case.

Reasonable and necessary legal services are those which require professional legal skills and expertise beyond the knowledge and skills of a trustee. In re Knapp, 930 F.2d 386 (4<sup>th</sup> Cir. 1991); In re Braswell Motor Freight Lines, Inc., 630 F.2d 348, 350 (5<sup>th</sup> Cir. 1980); In re Meade Land & Dev. Co., 527 F.2d 280 (3d Cir. 1985). See also In re Gary Fairbanks, Inc., 111 B.R. 809, 811 (Bankr. N.D. Iowa 1990); In re King, 88 B.R. 768 (Bankr. E.D. Va. 1988); In re Shades of Beauty, Inc., 56 B.R. (Bankr. E.D.N.Y. 1986).

#### 2-2.8.4 **Applications for Compensation**

Pursuant to § 330, after notice and a hearing, and subject to §§ 326, 328, and 329, the court may award the trustee or a professional person employed pursuant to § 327 reasonable compensation for actual, necessary services. Section 330 also allows the recovery of actual, necessary expenses. Overhead expenses of a trustee or professional are not reimbursable from the estate. See Sousa v. Miguel (In re U.S. Trustee) 32 F.3d 1370 (9<sup>th</sup> Cir. 1994).

Unless otherwise permitted by the court, the professional may make application for interim compensation and reimbursement of expenses not more than once every 120 days. § 331. The trustee has a fiduciary obligation to review professional fee applications and to object when appropriate.

In determining the amount of reasonable compensation under § 330, the court considers the nature, extent and value of the professional’s services, taking into account all relevant factors, including:

1. the time spent on such services;
2. the rates charged for such services;
3. whether the services were necessary to the administration of the case, or beneficial at the time at which the service was rendered toward the completion of the case;
4. whether the services were performed within a reasonable amount of time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed; and

5. whether the compensation is reasonable based on the customary compensation charged by comparably skilled practitioners in cases other than cases under Title 11.

Each application for interim or final fees and expenses must include:

1. a detailed statement of services rendered, time expended, and expenses incurred;
2. a statement of the amount of fees and expenses requested;
3. a statement of payments received or promised for services rendered or to be rendered in any capacity in connection with the case;
4. a statement of the source of compensation paid or promised; and
5. a statement of whether an agreement or understanding exists for the sharing of compensation received or to be received.

Fed. R. Bankr. P. 2016. Unless otherwise ordered by the court, all creditors and parties in interest must receive notice of all fee applications over \$500.

## 2-2.9 **DISMISSALS AND CONVERSIONS**

### 2-2.9.1 **Dismissals or Conversions of a Chapter 7 Case**

Chapter 7 cases may be dismissed pursuant to § 707. The trustee should review proposed dismissals and object to dismissals which would not be in the best interest of creditors. Unless the court orders otherwise, the trustee in a dismissed case must pay any funds on hand in the case and return any property to the person or entity from whom the funds and property were obtained. See § 349(b). Generally, this will mean that the trustee will return the funds and property to the debtor, unless the court directs that the funds and property be distributed to creditors.

Chapter 7 cases also may be converted to a different chapter pursuant to § 706. The court may not convert a chapter 7 case to a chapter 12 or chapter 13 case unless the debtor requests the conversion. § 706(c). While the right of a chapter 7 debtor to convert to another chapter is generally viewed as absolute absent prior conversion of the case, see § 706(a), a trustee may be able to challenge conversion if the debtor has engaged in fraudulent conduct. Upon conversion of a chapter 7

case to another chapter, the trustee should pay any funds on hand and deliver any property to the successor trustee or debtor, as appropriate.

The trustee must file a final report after a case has been dismissed, converted, or reassigned. See § 704(9). If the case was an asset case or the trustee collected any funds, the trustee must attach Forms 1 and 2 to the final report and transmit any original bank statements and canceled checks to the United States Trustee with the final report. The final report should be submitted after a zero bank balance is attained.

### 2-2.9.2 **Conversion of Cases From Another Chapter to Chapter 7**

Cases filed under chapters 11, 12, or 13 may be converted to chapter 7. The former debtor in possession or trustee must, forthwith, turnover to the chapter 7 trustee all records and property of the estate, unless the court orders otherwise. Fed. R. Bankr. P. 1019(4). The lists, inventories, schedules, and statements of financial affairs filed in the previous case are deemed filed in the chapter 7 case unless the court orders otherwise. Fed. R. Bankr. P. 1019(1). New time periods for filing claims and objecting to discharge are established if the case was not previously a chapter 7 case. Fed. R. Bankr. P. 1019(2).

Unless the court orders otherwise, the debtor in possession or former trustee must file a schedule of unpaid debts within 15 days and a final report within 30 days following conversion. Fed. R. Bankr. P. 1019(5). Generally, the United States Trustee should schedule a section 341 meeting when a case converts to chapter 7 from another chapter. §§ 341 and 348.

Appointment of the chapter 11 trustee to the chapter 7 case does not relieve the trustee of the reporting obligations under Fed. R. Bankr. P. 1019. The chapter 11 trustee must file a final report within 30 days of conversion pursuant to Fed. R. Bankr. P. 1019(5) and promptly turnover the records and property of the estate to the successor trustee, unless otherwise ordered. Fed. R. Bankr. P. 1019(4). The chapter 11 books and records must be closed as of the conversion date, and new books and records must be opened for chapter 7. These requirements apply even in the event that the chapter 11 trustee serves as the chapter 7 trustee.

Section 348 addresses the effects of case conversion. The trustee should be aware of the limitations on bringing avoidance actions in converted cases. § 546.

## 2-2.10 **REOPENING CLOSED CASES**

Occasions may arise when a closed case has to be reopened to administer unreported or recently discovered assets. The filing of a final report or a final account by a trustee does not close a case; it can only be closed by court order. If a new asset is discovered before a case is closed, the trustee may notify the United States Trustee and the clerk of the bankruptcy court and amend the final report and the final account. However, if the court has officially closed a case, the trustee, United States Trustee, or other party in interest, will have to file a motion to reopen the case, state the reasons for reopening, and pay any required filing fee.

If a case is reopened, a trustee is appointed only upon order of the bankruptcy court. Fed. R. Bankr. P. 5010. If the court orders appointment of a trustee, the United States Trustee may or may not reappoint the original trustee to the case.

Once administration is completed, a new final report and a new final account will be required from the trustee.

## 2-2.11 **REFERRAL OF POTENTIAL BANKRUPTCY CRIMES**

Section 3057 of title 18 requires trustees and judges to report suspected violations of federal criminal law to the appropriate United States Attorney. Section 586 of title 28 confers a similar duty on the United States Trustee to refer any matter that may constitute a violation of criminal law to the United States Attorney and, upon request, to assist the United States Attorney in prosecuting the matter.

### 2-2.11.1 **Detecting Criminal Activity**

The trustee is often in the best position to initially identify fraud or criminal activity in chapter 7 cases. When criminal activity is suspected, the trustee should notify the United States Trustee immediately.

The initial review of bankruptcy schedules may alert the trustee to potential crimes. Schedules and statements may indicate sham or fraudulent transactions, such as creation of false secured creditors, gross undervaluation of assets, sudden depletion of inventory, fraudulent transfers to fictitious entities (e.g., affiliates), or incurrence of significant trade debt shortly before the filing.

Creditors and other parties may contact the trustee with allegations of fraud. For example, former employees may have knowledge of undisclosed assets that the debtor failed to list on the schedules (e.g., assets transferred on the eve of

bankruptcy). Ex-spouses or trade creditors may disclose information about assets which the debtor failed to list on the bankruptcy schedules.

The section 341(a) examination of the debtor is an important opportunity to discover potential criminal activity. During this meeting, and while the debtor is under oath, the trustee may acquire or develop facts that may indicate a potential bankruptcy related crime. For example, debtors may lie during questioning on recent repayments of debts, gifts or transfers to insiders. In all cases where the trustee suspects criminal activity after questioning at the section 341 meeting, the trustee should immediately notify the United States Trustee so that the section 341 meeting tape may be properly secured and stored to preserve its later use in a criminal proceeding.

The trustee may also discover potential criminal violations through the review of records such as financial statements and records, UCC filings and title searches, insurance records, divorce files, bank loan files, proofs of claim and tax returns. It is not infrequent to discover gross discrepancies between assets identified in these documents and the debtor's documentation on the bankruptcy schedules and statements.

#### 2-2.11.2 **Types of Criminal Conduct**

The most common bankruptcy crimes are set forth in § 152 of title 18. Section 152 makes it a crime for any individual to “knowingly and fraudulently”:

- 1) conceal property of the estate;
- 2) make a false oath or account in relation to a bankruptcy case;
- 3) make a false declaration, certification, verification or statement in relation to a bankruptcy case;
- 4) make a false proof of claim;
- 5) receive a material amount of property from the debtor with intent to defeat the Bankruptcy Code;
- 6) give, offer, receive or attempt to obtain money, property, reward or advantage for acting or forbearing to act in a bankruptcy case;
- 7) transfer or conceal property with the intent to defeat the Bankruptcy Code;
- 8) conceal, destroy, mutilate or falsify documents relating to the debtor's property or affairs; or
- 9) withhold documents related to the debtor's property or financial affairs from a trustee or other officer of the court.

Persons other than the debtor may commit bankruptcy crimes. During the course of the administration of the estate, the trustee also may become aware of potential theft or embezzlement by professionals (e.g., appraisers, auctioneers, attorneys) or by trustee employees.

Sections 153 and 154 of title 18 are specifically directed to trustees and other officers of the court. Section 153 relates to the knowing and fraudulent misappropriation, embezzlement or transfer of property, or destruction of any estate document, by the trustee or other officer of the court. The Bankruptcy Reform Act of 1994 broadened the scope of those affected by this statute to include an agent, employee or other person engaged by the trustee or officer of the court. 18 U.S.C. §§ 153, 154.

Section 154 of title 18 prohibits a trustee or other officer of the court from knowingly purchasing, directly or indirectly, any property of the estate of which such person is a trustee or officer; or the knowing refusal to permit a reasonable opportunity for the inspection of estate documents or accounts when directed by the court to do so. It also specifically identifies the United States Trustee as the only party in interest who does not require a court order directing the trustee or court officer to permit a reasonable opportunity for inspection. 18 U.S.C. § 154(3).

Section 155 of title 18 makes it a crime for any party in interest or its attorney to knowingly and fraudulently enter into an agreement with another party in interest or its attorney, for the purpose of fixing the fee or compensation to be paid to them for services rendered in connection therewith, from assets of the estate. 18 U.S.C. § 155

The Bankruptcy Reform Act of 1994 added 18 U.S.C. § 156, “Knowing Disregard of Bankruptcy Law or Rule,” and 18 U.S.C. § 157, “Bankruptcy Fraud.” A “bankruptcy petition preparer” is guilty of a misdemeanor if its knowing attempt to disregard in any manner the requirements of the Bankruptcy Code or Rules causes a bankruptcy case or related proceeding to be dismissed. § 156. A bankruptcy petition preparer does not include a debtor’s attorney or an employee of such attorney, but applies to a person who prepares for compensation a document for filing by a debtor in bankruptcy or district court.

Section 157 is similar to the federal mail fraud and wire fraud statutes in that it requires a person to devise or intend to devise a scheme or artifice to defraud. A person, not only a debtor, commits bankruptcy fraud if, for the purpose of executing or concealing this scheme or artifice to defraud, that person:

1. files a petition under title 11;
2. files a document in a proceeding under title 11; or

3. makes a false or fraudulent representation, claim, or promise concerning or in relation to a proceeding under title 11, at any time before or after the filing of the petition, or in relation to a proceeding falsely asserted to be pending under such title.

18 U.S.C. § 157. If a person falsely claims to be in bankruptcy, this is a violation of § 157.

There are several other criminal statutes that may be relevant to bankruptcy related crimes including those relating to bank fraud, tax fraud, mail and wire fraud, and money laundering. The United States Trustee should provide information and training to the trustees on these statutes.

### 2-2.11.3 **Compliance With the Trustee's Duty to Report Criminal Conduct**

Section 3057 of title 18 of the United States Code requires the trustee to report suspected violations of federal criminal law to the appropriate United States Attorney. Section 586 of title 28 imposes a similar duty on the United States Trustee to refer any matter that may constitute a violation of criminal law to the United States Attorney and, upon request, to assist the United States Attorney in prosecuting the matter.

It is important that the chapter 7 trustee and the United States Trustee coordinate their efforts in the criminal referral process. Upon determining that there are reasonable grounds to believe that a crime has been committed, the trustee is required to refer the matter to the United States Attorney. Depending upon local practice, the trustee should submit the referral through the United States Trustee or furnish a copy to the United States Trustee. The mechanics of this referral should be discussed with the United States Trustee, the Assistant United States Trustee, or the Criminal Referral Coordinator for the particular region, as they may have developed specific procedures with the local offices of the United States Attorney and the Federal Bureau of Investigation.

In making a criminal referral it is important to provide as much specific factual and documentary information as possible. At a minimum, the referral should include:

1. the bankruptcy case name, file number and chapter;
2. a chronological summary including dates and specific facts related to the who, what, where, when and how of the suspected crime;

3. a brief narrative of what occurred in relation to each allegation referring to copies of relevant documents;
4. an estimate of the amount of loss involved;
5. names, addresses, phone numbers, titles, and descriptions of likely witnesses;
6. a copy of all written documents relevant to the allegations; and
7. a statement of other related referrals made to law enforcement agencies.

Additional information regarding bankruptcy crimes and the referral process is set forth in USTM Volume 5.

## **CHAPTER 2-3: TRUSTEE SUPERVISION**

### **2-3.1 ROLE OF THE UNITED STATES TRUSTEE**

The primary functions of the United States Trustee in chapter 7 cases are the establishment, maintenance, and supervision of panels of trustees, and the monitoring and supervision of the administration of cases under chapter 7 of the Bankruptcy Code. Accordingly, the goal of the United States Trustee in chapter 7 cases is to establish a system that will allow for the complete, economical, equitable and expeditious administration of cases, while allowing the trustee to exercise appropriate business and professional judgment in performing the trustee's fiduciary duty.

Trustee supervision is an ongoing process. It requires monitoring the trustee's case load and the trustee's service as a fiduciary in each case. Effective supervision begins when a trustee is assigned to a case and continues throughout the administration of the case. A trustee's performance in each case provides the framework for evaluating the administration of the entire case load. An effective trustee monitoring system collects, integrates and analyzes information from a variety of sources. This information can then be used to evaluate the trustee's competency, commitment and integrity in discharging of the trustee's fiduciary obligations.



The United States Trustee has identified a number of important areas which are reviewed on an ongoing basis. The trustee's performance is routinely documented in correspondence to the trustee and memos to the file, and summarized in the trustee's performance review. See USTM 2-3.17 and Appendix 2-4. The United States Trustee's responsibilities in each of these areas are described in the following sections:

1. Reports in No-Asset Cases (No-Distribution Reports or NDRs)
2. Trustee Final Reports (TFRs) and Trustee Final Accounts (Trustee Distribution Reports or TDRs)
3. Section 341(a) Meetings
4. Securing Estate Property
5. Legal Administration
6. 180-Day and Operating Chapter 7 Reports
7. Case Progress
8. Banking
9. Bonding
9. Distributions to Creditors
10. Response to Audits
11. Response to USTs
12. Investigation of and Response to Fraud and Abuse
13. Response to Public Complaints
14. Retention and Compensation of Professionals

#### 2-3.1.1 **Memorandum of Understanding**

The United States Trustee Program and the Administrative Office of the United States Courts have entered into an Amended Memorandum of Understanding (dated April 1, 1999) ("AMOU") which delineates the respective responsibilities of the clerk of the bankruptcy court, the trustee and the United States Trustee in the case closing process, as well as other matters. See Appendix 2-9. The United States Trustee must review a trustee's reports of no-distribution, final reports and final accounts in a manner that conforms to the requirements of the AMOU.

Pursuant to the AMOU, a trustee is to submit a report of no-distribution, final report and proposed distribution (pre-distribution report), as well as the trustee's final account (post-distribution report), to the United States Trustee.

### 2-3.2 **REPORTS IN NO-ASSET CASES (NDRs)**

If a trustee determines that no funds for the benefit of creditors can be derived from a liquidation of the debtor's assets, a report of no-distribution (NDR) is to be filed timely with the court and the United States Trustee. § 704(9). Pursuant to the AMOU, the trustee shall submit the NDR to the United States Trustee and the court within 60 days of the section 341 meeting. If the trustee submitted the original NDR to the United States Trustee, then the United States Trustee shall file the NDR with the court within five days of receipt.

Pursuant to Fed. R. Bankr. P. 5009, a trustee's NDR must contain a certification that the trustee has fully administered the case. The NDR certifies that the trustee has reviewed the schedules, investigated the facts and determined there are no assets to liquidate for the benefit of creditors. It also certifies the trustee has reviewed the exemptions and concluded there is no purpose to be served by objecting to their allowance and that all security interests and liens against non-exempt property are properly documented, perfected and not subject to attack as preferences or are otherwise voidable. All copies of NDRs received by the United States Trustee should immediately be date-stamped and entered into the ACMS System.

The United States Trustee should evaluate a random sample of cases in which the trustee has filed an NDR to determine whether the trustee adequately examined the assets, exemptions and claims and whether the trustee had an unreasonably high dollar threshold for pursuing assets in a case, including causes of action. The statements and schedules, as well as the claims, should be reviewed by the United States Trustee to make that determination. Generally, all NDRs from non-panel trustees should be reviewed.

All reviews must be completed so that objections to the NDR may be filed within 30 days of the filing of the NDR. AMOU. Therefore, the United States Trustee should develop a procedure to complete the NDR reviews within this 30-day time frame, to minimize the need to reopen a closed case. The review should include an examination of United States Trustee case files for any indication of funds that the trustee may have received, such as a report or notice of sale, copies of correspondence concerning the turnover of funds, or a report from a previous chapter 12 or 13 standing trustee indicating the turnover of funds to the chapter 7 trustee in a converted case. Schedules and other pleadings must also be examined to determine that all assets listed were properly exempted or were of no value to the estate. The reviewer must be familiar with the appropriate federal and/or state exemptions. Although the time to object to improper exemptions

may have expired, it is important from the standpoint of reviewing the trustee to note a pattern of missed exemptions. In addition, a verification letter should be sent to the debtors in the sampled cases as a further substantiation that assets were not turned over to the trustee. AMOU. If the debtor was represented by counsel, the verification letter must be sent to counsel and not the debtor. The United States Trustee should retain the listing of cases reviewed and a record of any discrepancies and their resolution. The listing and record should be maintained by the United States Trustee and retained in the trustee's oversight file.

The trustee's fee under § 330(b) (per each no-asset case) will not be paid by the clerk of the court until the NDR is filed, the discharge order is entered, and the case closed by the court.

If assets are subsequently discovered, the trustee should (1) seek to have the case reopened and (2) withdraw the NDR in writing to administer the assets. The procedures as set out in the Handbook at pp. 8-1 and 8-36 should be followed.

It should be noted that a trustee's failure to timely and properly file NDRs should be addressed by an appropriate remedial action.

### 2-3.3 **REPORTS FOR CLOSING ASSET CASES: FINAL REPORTS (TFRs) and FINAL ACCOUNTS (TRUSTEE DISTRIBUTION REPORTS or TDRs)**

#### 2-3.3.1 **Final Reports (Pre-Distribution)**

When a case is ready to be closed, a chapter 7 trustee must prepare and file a final report (TFR) with the United States Trustee for review before filing it with the court. The TFR must be signed by the trustee under penalty of perjury and certify that all assets have been liquidated or properly accounted for and that funds of the estate are available for distribution. AMOU. The TFR must be prepared as soon as all monies have been collected, all claims have been reviewed or determined by the court, and the bar date has expired for creditors to file claims. The report must be filed prior to any distribution of funds to creditors, unless the court has previously ordered an interim distribution. AMOU. In any event, a TFR must be filed before final distribution of all funds in the case. See Fed. R. Bankr. P. 5009; AMOU.

The TFR must consist of the Individual Estate Property Record and Report (Form 1); the Cash Receipt and Disbursement Record (Form 2); and the proposed dividend distribution report. (AMOU). The TFR should summarize all actions taken by the trustee to administer the case. Each report must:

1. Describe the disposition of each estate asset (as listed in the debtor's schedules or otherwise discovered). Form 1, the Estate Property Record and Report, meets this requirement.
2. Report all financial transactions by the trustee. Form 2, the Cash Receipt and Disbursement Record, may be included in the final report to meet this requirement.
3. Request payment of the trustee's compensation and expenses and any unpaid professional fees and expenses.
4. Report the trustee's actions on claims or their disposition.
5. Propose distribution to creditors according to §§ 507 and 726.
6. Attach original bank statements and original canceled checks (from estate accounts) received by the trustee during the case.

All outstanding applications for professional compensation and expenses should also be filed along with the TFR. The TFR enables the United States Trustee and any other party in interest to determine how the trustee proposes to disburse the funds.

Generally, estate funds should be maintained in an interest-bearing account until the trustee is ready to distribute the funds to creditors. The difference between the distribution as calculated in the TFR and reported in the TDR should be footnoted in the TDR. No amended TFR should be filed. The trustee may receive a fee on the increase, if authorized by the court (although many trustees waive the extra fee). If the balance of estate funds on hand is less than \$5,000, the trustee has the discretion to move the funds to a non-interest bearing account when the TFR is filed with the United States Trustee. This amount may be adjusted at the United States Trustee's discretion. If there is a substantial delay in approval of the TFR, the trustee is expected to reinvest the funds, in accordance with the trustee's duty to maximize the return to creditors. Funds should not be invested after the final tax return is prepared if the cost of preparing an additional tax return would exceed the interest earned. Normally, this situation will only be an issue for corporate or partnership cases.

The United States Trustee must conduct a thorough review of each TFR within 60 days of receipt to assess whether the trustee has properly and completely administered estate property. The United States Trustee shall examine

exemptions, abandonments, sales or other liquidations; ensure inclusion of all necessary court orders; and verify the accuracy of calculations. The United States Trustee will also determine whether the trustee reviewed and properly dealt with all claims. Deficiencies in the trustee's administration or other problems or mistakes will be brought to the trustee's attention for corrective action. Upon completion of this review, the United States Trustee will forward the TFR to the court. If there is a dispute between the United States Trustee and the trustee concerning the report, the TFR will be filed with an objection and the dispute resolved by hearing before the court. See the AMOU at Appendix 2-9.

The TFR must set forth the distributions to be made under § 726. The order of payment is as follows:

1. First, costs of administration allowed under § 503(b), including trustee's fees, professional fees, certain postpetition claims, and costs and fees assessed under chapter 123 of title 28. Administrative expenses incurred in a chapter 11, 12 or 13 case are subordinated upon conversion to chapter 7 to administrative expenses incurred in the chapter 7 case. Quarterly fees from a converted chapter 11 case are paid along with other fees assessed under chapter 123 of title 28 and are not subordinated to chapter 7 administrative expenses.
2. Second, certain expenses incurred in an involuntary bankruptcy case before entry of an order of relief or appointment of a trustee, whichever occurs first.
3. Third, certain wage, salary, or commission claims.
4. Fourth, certain claims for contributions to an employee benefit plan.
5. Fifth, certain claims of farmers and fisherman.
6. Sixth, certain claims arising from purchase, lease, or rental deposits.
7. Seventh, certain claims for alimony, maintenance, or support.
8. Eighth, certain governmental claims for income, property, employment, and excise taxes, and customs duties.
9. Ninth, certain claims by a federal depository institution regulatory agency.

10. Tenth, unsecured claims in which a proof of claim is timely filed or in which a claim is tardily filed but the creditor had no notice or actual knowledge of the case.
11. Eleventh, unsecured claims in which a proof of claim is tardily filed with notice or actual knowledge of the case.
12. Twelfth, claims for any fine, penalty, or forfeiture, or for multiple, exemplary, or punitive damages to the extent the amounts are not for compensation for actual pecuniary losses.
13. Thirteenth, interest on the claims paid above from the date of filing the petition at the legal rate.
14. Fourteenth, to the individual debtor or equity holders of the corporate or partnership debtor pursuant to the articles of incorporation or state law.

Within any class of claims, if insufficient funds exist to pay all claims in full, the balance is prorated among that class of creditors. The prorated amount is determined as follows:

1. Divide the balance on hand by the total dollar amount of claims in the class. The quotient is the dividend percentage.
2. Multiply each claim by the dividend percentage to determine the amount to be paid on that claim.

Under Fed. R. Bankr. P. 2002(f), the trustee is required to notice all creditors with a summary of the final report before actually making the distribution to the creditors if the net proceeds realized in an estate exceed \$1,500. If no objections are lodged to the trustee's notice of intent to distribute or to the report of distribution, then the trustee may make the distribution according to the final report.

The following checklist may be used as a guide to review TFRs:

1. Verify that the section 341 meeting was held and concluded.
2. Petition, Schedules, and Form 1

Examine schedules A, B, C, and G to determine whether all assets have

been properly administered (i.e., examination of exemptions claimed and allowed, compromises, turnovers, or other liquidations). The disposition of each asset must be accounted for. The reviewer should also review the debtor's Statement of Financial Affairs and Schedule of Creditors Holding Security, Schedule D, for undisclosed assets, such as possible tax refunds, fraudulent transfers, preferences, and assets in the hands of a third party that were not listed on the debtor's property schedules.

3. Bank Statements, Canceled Checks, and Form 2

Ensure that the amount of dollar realized for all assets liquidated or turned over are properly recorded on Form 1, including receipts that would not require a Report or Notice of Sale or other court authority. Such items would include tax refunds, debtor bank account balances, or other non-sale transaction receipts. All realizations reported on Form 1 must be traced to a corresponding deposit on Form 2. Interest earned on estate bank accounts should be reflected on Form 1 and Form 2.

The United States Trustee should review all interim disbursements made prior to the closing process. For all interim disbursements paid to professionals, the reviewer must determine that approval for both the employment and payment of the professional were obtained in accordance with the Bankruptcy Code and Rules. Professional services and fees that require a court order include those for attorneys, accountants, certain types of agents, appraisers, etc. Disbursements to non-professionals, such as utility payments, bond premium payments, insurance payments, payments to secured creditors in order to obtain clear title, administrative taxes, closing costs associated with the sale of real estate (except professional fees incurred by the estate), and the turnover of funds that are not property of the estate (e.g., debtor's share of tax refunds or debtor exemption payments, and the like) do not necessarily require a court order to be paid in the interim. The reviewer should examine all of the cancelled checks to ensure that the payee, endorsement, and amount match the Form 2 and other applicable documentation. The reviewer should specifically look for unusual endorsements, alterations, and forged signatures.

The reviewer should verify any transfers of estate funds between checking and savings accounts so as not to include those transfers as receipts into or disbursements from the estate. After those inter-account transfers are verified, the reviewer should subtract the disbursements from the receipts to determine that the balance on hand, as reported by the trustee in the

final report, reconciles with the bank statements from the estate's depositories. The reviewer should obtain an explanation for any unusual transfers, withdrawals, or deposits shown on the bank statements.

The bank reports received by the United States Trustee from the authorized depository provide additional verification of the receipts and disbursements shown on Form 2.

4. Docket Sheet

Review the court's docket for any transactions (sales, abandonments, etc.) that do not appear on Forms 1 and 2.

5. United States Trustee Case File

Ensure that there are proper court orders as may be required for the trustee to take particular actions (i.e., sales, settlements and/or compromises, turnovers, etc.). For example, if a source of income indicated in the final report was from the sale of assets, verify the sale description and the dollar amount from a Report or Notice of Sale or other court order authorizing the same in the case file. If the trustee acted without proper court authority, inform the trustee to obtain the necessary court approval or authority as appropriate.

6. Trustee and Unpaid Professional Compensation

All outstanding applications for the payment of professional compensation that are submitted with or as part of the final report should be reviewed for compliance with the Bankruptcy Rules, the Bankruptcy Code, and the Program's fee guidelines.

Verify that the request for trustee compensation does not exceed the statutory limit set forth in § 326(a). If the trustee received interim compensation per court order, it should be properly reflected as an interim disbursement.



As of October 22, 1994, the following percentages govern the trustee's maximum compensation:

25% of the first 5,000 or less	= \$ 1,250
10% of the amount in excess of \$5,000, up to 50,000	= \$ 4,500
5% of the amount in excess of \$50,000, up to \$1,000,000	= \$47,500
3% of the amount in excess of \$1,000,000	

Under the current version of § 326(a), the trustee's maximum compensation is computed upon all monies disbursed or turned over in the case by the trustee to parties in interest, excluding the debtor, but including holders of secured claims. Disbursements or receipts that would not be included in the § 326(a) calculation include payment for debtor's exemptions and refunds to the estate from previous disbursements from the estate. See USTM 2-2.8.

The reviewer must also examine the trustee's request for expense reimbursement in conformance with the Fee Guidelines at Appendix 2-8.

#### 7. Review of Claims

The reviewer should determine whether the trustee reviewed and properly dealt with all claims. If deemed necessary, the trustee's certification that all claims have been reviewed should be verified by further review of the documents on file with the clerk of the bankruptcy court.

A determination should be made that the proper amount of court costs (and claims for unpaid quarterly fees in a case converted from chapter 11) are included as proposed administrative expense claims. Many jurisdictions utilize a procedure by which the trustee, at the time of preparing the final report, obtains a notice of court costs due from the clerk of the court with a copy of the same being provided to the United States Trustee.

When deemed necessary by the United States Trustee, a review should also be made to determine that the proposed distribution by the trustee is in accordance with the priorities as established under the Bankruptcy Code. Further, in those cases where insufficient funds are available to pay a specific class of claims in full, a determination should be made that the trustee has correctly pro-rated the distribution.

## 8. Unpaid Quarterly Fees

If the case converted from chapter 11, unpaid quarterly fees are entitled to be paid pro rata with the chapter 7 administrative expenses. See In re Endy, 104 F.3d 1154 (9th Cir. 1997); In re Juhl Enterprises, Inc., 921 F.2d 800 (8<sup>th</sup> Cir. 1990). The United States Trustee shall file a proof of claim with the clerk of the court for any unpaid fees accrued during the chapter 11 case. If appropriate, the proof of claim may indicate the amount as “undetermined.” Since the trustee will have the books and records of the debtor, the trustee should review the cash disbursements made for the applicable period(s) to determine the appropriate amount of unpaid fees. The United States Trustee shall generally accept the lowest appropriate amount as reflected in the books and records. If there are no books and records or the information is inadequate, the minimum amount due for the period(s) will be acceptable.

### 2-3.3.2 Distribution

The United States Trustee must approve the trustee’s proposed distribution of funds. Court orders are necessary prior to payment of trustee and professional fees and expenses and to resolve claims objections, but are not necessary for the general distribution of funds to creditors, absent any other objections to the trustee’s final report. If no objections are filed, the trustee should immediately make disbursements upon the entry of any appropriate court order(s) and after any applicable appeal period has expired. Fed. R. Bankr. P. 3009. If the court modifies the fees and expenses, the trustee’s revised dividend distribution report must be reviewed by the United States Trustee within 10 days of receipt. The final distribution to creditors must be paid within 30 days of the entry of the final orders on compensation and expenses. AMOU.

Typically, distributions are made at the end of the case; however, limited circumstances sometimes support an interim distribution to creditors. Interim distributions should occur only after claims are resolved and sufficient assets have been reserved to administer the estate. The United States Trustee must review and approve the trustee’s proposed interim distribution of funds. See also USTM 2-3.3.1.

### 2-3.3.3 Final Accounts (Post-Distribution)

Within 125 days after the entry of an order allowing final compensation and expenses, a trustee must submit to the United States Trustee for review a final

account (TDR) signed under penalty of perjury certifying that the estate has been fully administered. Fed. R. Bankr. P. 5009. The original bank statement(s) showing a zero balance and all original canceled checks (except those already submitted with the TFR) must be attached to the TDR. The trustee must certify that all funds have been disbursed consistent with the distribution report and that all checks have been negotiated or any remaining checks have been paid into court and that the estate has been fully administered. Under § 347, if any checks remain outstanding 90 days after the final distribution, the trustee must stop payment on them and pay the monies into the Bankruptcy Court Registry Fund as unclaimed funds pursuant to Fed. R. Bankr. P. 3011.

The TDR is to be submitted to the United States Trustee, who must review and file it with the court within 30 days of receipt. If any problems or discrepancies are detected, follow-up action should be taken. Once the reviewer is satisfied that distributions have been made properly by the trustee and that the TDR is correct, the original of the TDR should be filed with the clerk of the bankruptcy court. The United States Trustee must attach a statement to the TDR which states it has been reviewed and the United States Trustee has no objection to the trustee's certification of full administration. See AMOU. If there is no timely objection by the United States Trustee or other party in interest, there shall be a presumption that the estate has been fully administered and the court may close the case.

At a minimum, the United States Trustee should verify that all disbursements were made in accordance with the trustee's TFR, as approved. The canceled checks should be reviewed to determine that they were issued to the correct parties and in the correct dollar amounts. Under Fed. R. Bankr. P. 3010, unless the court orders otherwise, all dividends of less than \$5 must be paid into the Clerk's Registry Fund.

Unless the clerk of the bankruptcy court requires custody, the canceled checks and zero bank statement may be retained by the United States Trustee or returned to the trustee. The bank statements and cancelled checks must be retained for the two-year period specified in § 322(d), or as otherwise required by the Internal Revenue Service, whichever period is longer.

Once the TDR has been filed with the clerk of the bankruptcy court, the case can be closed by the United States Trustee in ACMS. In addition, the trustee can be discharged and the case closed by the court, unless other matters not affecting the administration of assets are pending.

The United States Trustee shall establish a procedure to monitor the timeliness of final distributions and the filing of TDRs by trustees.

The trustee may encounter a situation in which a creditor refuses a dividend payment because the debt was previously paid. Depending on the amount of any returned payments, the number of other creditors otherwise receiving distributions, and local court policy or procedure, the trustee may be required to redistribute returned funds to the other creditors. Because a supplemental distribution normally will occur prior to the submission of the trustee's TDR, the supplemental distribution should be included as part of the United States Trustee's review of the trustee's TDR.

#### 2-3.3.3.1 Distribution Report for Closed Asset Cases (Form 4)

Trustees are required to attach Form 4 to the TDRs for cases filed or converted on or after July 1, 1999. Form 4 will be filed electronically commencing April 1, 2000. Form 4 is not required for asset cases open as of June 30, 1999, as long as the TDR is submitted on or before June 30, 2002. See Appendix 2-10 for the Form 4 and related instructions.

All trustees are expected to submit Form 4. Compliance may be waived only on a case-by-case basis. For example, compliance may be waived for a very large, older case that cannot be closed by July 1, 2002, due to exigent circumstances, such as pending litigation. In addition, non-panel trustees, who are winding down their caseloads, are exempt. However, if a non-panel trustee is elected or appointed to serve in a case filed or converted on or after July 1, 1999, the trustee will be expected to provide a Form 4 with the TDR.

As part of the TDR review process, the United States Trustee will review Form 4 to ensure it accurately reflects the distributions made by the trustee. This information will be accumulated for all cases and all trustees for periodic reporting to interested parties by the EOUST.

#### 2-3.4 **SECTION 341 MEETINGS**

At least annually, the United States Trustee should select for review cases assigned to each trustee, monitor the meeting of creditors (by attending in person or reviewing audio tapes), evaluate whether appropriate questions were asked, whether the length of the meeting and thoroughness of the questioning was adequate in view of the nature and complexity of the case, whether irregularities in petitions were identified, and whether the trustee's demeanor toward all parties

was appropriate and professional. The reviewer should note whether necessary follow-up deadlines were imposed. A list of questions required to be asked on the record at the section 341 meeting is found in Appendix A to the Handbook. The trustee must establish on the record that each debtor is aware of the provisions of § 341(d). The results of the review must be documented in writing and retained in the oversight file.

#### 2-3.4.1 **Declination of Cases**

A trustee should be familiar with §§ 101(4), 101(13) and 701(a), and must decline any appointment in which a trustee has a conflict of interest or lacks disinterestedness. A trustee's timely declination of cases or dockets and the reasons given, as well as a trustee's acknowledgment and evaluation of conflicts of interests, should be in writing and maintained in the appropriate file. See USTM 2-1.6.6 for further discussion of conflicts of interest.

#### 2-3.5 **SECURING ESTATE PROPERTY**

The trustee must promptly secure possession of estate assets, and to preserve the assets for the benefit of creditors. The United States Trustee should verify that the trustee effectively identifies and inventories assets, and takes appropriate action to control and preserve estate property. See USTM 2-2.2.2.

#### 2-3.6 **LEGAL ADMINISTRATION**

The United States Trustee reviews the trustee's employment and supervision of counsel, and management of litigation and legal issues. As part of that review, attention should be given to litigation analysis, the cost-benefit analysis of legal work and cause(s) of action, the control exercised over fees and expenses, and the quality of legal services rendered.

The United States Trustee, as part of the review of the trustee's legal administration, may attend court hearings in which the trustee or trustee's counsel appears. Special attention should be paid to the preparation, demeanor, and professional quality of legal service or presentation. The United States Trustee's review of the trustee's selection and monitoring of counsel for the trustee and the pleadings drawn, and court performance of counsel shall be documented in writing.

### 2-3.6.1 **Pleadings**

The United States Trustee should review a trustee's pleadings for timeliness, sufficiency, and necessity. Pleadings to be scrutinized include employment applications, professional fee applications, motions to sell assets, motions to abandon assets, objections to exemptions, objections to discharge, and adversary complaints. All applications for fees are to be prepared in compliance with the Fee Guidelines at Appendix 2-8.

### 2-3.6.2 **Court Performance**

The United States Trustee should routinely observe a trustee's court appearances. Special attention should be paid to the preparation, demeanor and professional quality of legal service or presentation. Findings should be documented in the oversight file.

## 2-3.7 **180-DAY REPORTS AND OPERATING CHAPTER 7 REPORTS**

### 2-3.7.1 **Semi-Annual (180-Day) Reports**

Section 704(2) and Fed. R. Bankr. P. 2015(a) establish require the trustee to be accountable for all property of an estate received by the trustee and to report on the administration of the estate. To properly perform these duties and to effectively administer an asset case, a uniform record keeping and reporting system has been established by the United States Trustee Program which must be used by all trustees. This system consists of three distinct reports: an Individual Estate Property Record and Report (Form 1); a Cash Receipts and Disbursements Record (Form 2); and a Summary Interim Asset Report (Form 3) (hereinafter, referred to collectively as the "180-day report" or "semi-annual report").

The instructions for completing Forms 1, 2, and 3 are contained in the Handbook (see Chapter 9, Forms and Instructions, and the Sample Case). Following is a brief description of each Form.

#### 2-3.7.1.1 **Form 1**

The Individual Estate Property Record and Report (Form 1) provides a blueprint for each asset case. It details all estate assets, both scheduled and unscheduled, and reflects the status of their disposition. It compares the debtor's opinion of each scheduled asset's value, the trustee's estimated net value to the estate for each estate asset, and the actual value realized by the trustee. It also supports the

decision regarding administration of each asset. For assets not administered, Form 1 reflects abandonments, whether past or future, formal or informal. For assets administered or to be administered, Form 1 reflects amounts realized and the anticipated remaining value of assets not completely liquidated.

Form 1 must be prepared and maintained for every case that is either expected to be or declared to be an asset case by the trustee, for each case in which the trustee has received funds of the estate, and for each case in which an NDR has not been filed and 60 days have passed since the initial examination of the debtor at the section 341 meeting. All assets of the debtor must be listed from the petition, schedules, and statement of affairs. All unscheduled assets identified by the trustee also must be recorded. In a case converted from chapter 11, assets reported in the final report required by Fed. R. Bankr. P. 1019(5), or in any schedules submitted post-conversion, should be listed. If no such report or schedules are filed, the trustee will list the assets remaining in the case and keep a record in the estate file which describes how the trustee determined the assets remaining in the case. If the trustee is serving as a successor trustee, Form 1 should list all receipts or deposits turned over by the prior trustee as well as all property of the estate not administered by the prior trustee.

#### 2-3.7.1.2 Form 2

The Estate Cash Receipts and Disbursements Record (Form 2) is a combination checkbook/journal. A separate Form 2 is maintained for each checking account, money market account, savings account, and/or Certificate of Deposit that are opened on behalf of the bankruptcy estate. It shows all receipts, disbursements, and bank account transfers for each account. All transactions must be entered on Form 2, in chronological order, as soon as they occur. The trustee should not wait and enter transactions from the monthly bank statements. No Form 2 is necessary until the bank account is opened.

If the trustee is serving as a successor trustee, Form 2 should begin with the balance turned over by the previous trustee, thereby remaining consistent with the successor trustee's bank statements.

#### 2-3.7.1.3 Form 3

Form 3 lists all pending cases expected, or declared, to be asset cases by the trustee, all cases in which the trustee has received funds of an estate, and all cases in which an NDR has not been filed and 60 days have passed since the initial examination of the debtor at the section 341 meeting. Cases are entered in

sequence by case number. Many of the entries on Form 3 are made from Form 1 and Form 2. The key to preparing an accurate Form 3 is to make sure that Forms 1 and 2 are accurate and up-to-date for each case that is required to be included on Form 3. These Forms should be carefully reviewed and updated before Form 3 is prepared.

#### 2-3.7.1.4 Chapter 7 Trustee Reporting Requirements

A trustee is required to file Form 3 at least every six months, unless the United States Trustee requires that it be filed more frequently. In addition to Form 3, a trustee must submit Forms 1 and 2 for each pending case unless a TDR was filed in the case during the current or prior reporting period, a final report was filed for an asset case that was converted, dismissed, or reassigned during the current reporting period; or 3) an NDR was filed for the case during the current reporting period. Such cases need only be listed on Form 3. Additional requirements are described in the Handbook.

If a trustee cannot submit the semi-annual report by the due date, the trustee should obtain a date specific extension in writing from the United States Trustee prior to the deadline.

Fed. R. Bankr. P. 2012(b) requires a successor trustee to file with the United States Trustee an accounting of the prior trustee's administration of the estate. This accounting should be a separate and distinct record of the activities which were solely within the control of the prior trustee. The Fed. R. Bankr. P. 2012(b) accounting ultimately may be the basis of criminal investigation, surcharge of the prior trustee, suspension or termination of the prior trustee's appointment, or the basis for an award of compensation to a decedent's estate. The rule does not have a deadline of submission of the accounting. Absent some evidence of defalcation or other harm to the estate, the accounting can be provided in conjunction with the submission by the successor trustee of the standard reports required by the United States Trustee.

#### 2-3.7.1.5 Review by United States Trustee

The semi-annual report provides information concerning a trustee's financial management, internal controls, organizational effort and legal administration of the cases in which the trustee serves. The United States Trustee reviews the 180-day report to ensure adherence to fiduciary standards in the administration of the chapter 7 case load. The United States Trustee must establish appropriate procedures for reviewing semi-annual reports. The review must be completed



within 60 days of receipt. Particular emphasis should be given to the trustee's zeal and diligence in identifying, pursuing, and recovering assets for the benefit of creditors; timeliness in closing cases; compliance with reporting and other requirements of the United States Trustee; and performance of the trustee's responsibilities pursuant to § 704. The United States Trustee should examine all cases (unless a smaller sample size is authorized by the United States Trustee) in each trustee's semi-annual report, with particular attention paid to cases open more than 18 months as well as those cases involving substantial assets. Findings from a review should be documented in writing and discussed, if appropriate, with the trustee. Where appropriate, the trustee should provide a written response and corrected forms. Correspondence to the trustee documenting issues raised with semi-annual reports is part of the trustee oversight file. The actual semi-annual reports and related review notes may be retained separately.

Any major problems that surface in the review process must be discussed with the trustee. Trustees who are deficient in their administration of cases will be subject to a wide range of compliance measures by the United States Trustee or the court.

The United States Trustee does not need to conduct a separate review of the semi-annual report for any six-month period that is also the subject of an Office of the Inspector General audit or UST Field Examination. Audits and examinations are discussed at USTM 2-3.12.

### 2-3.7.2 **Reports in Operating Chapter 7 Cases**

Under § 721, the court may authorize a trustee to operate the business of a debtor for a limited period of time. In order for the court to grant such a request, two basic requirements must be met. First, operation of the debtor's business must be in the best interest of the estate. Second, such operation must be consistent with the liquidation of the estate. Prior to seeking authority from the court to operate the business, the trustee should consult with the United States Trustee to discuss the nature of the operation, cash management controls, and the appropriate monthly operating business report form required by § 704(8). Note that the format of the monthly operating report may vary from district to district. See USTM 2-2.5.9.

#### 2-3.7.2.1 **Review by United States Trustee**

The United States Trustee should review the monthly operating report within 15 days of receipt to determine the adequacy of the trustee's bond; the proper and timely administration of the case; and the possibility of the sale of the business as

a going concern or, in the alternative, conversion of the case to allow reorganization under chapter 11. Written notice of deficiencies or problems with a monthly operating report should be given to the trustee immediately upon review by the United States Trustee, along with deadlines for corrective action or additional information.

If a trustee fails to file the reports required by § 704(8) or if the reports demonstrate a loss to the estate, the United States Trustee should seek an order terminating the trustee's authority to operate the business or seek removal of the trustee if continued operation is in the estate's best interest.

Even when the court finds operation of a business will increase the estate's value without endangering the estate's assets, the trustee should seek to operate the business for the shortest practical period. The trustee should either close the case, liquidate the business, or convert the case to a chapter 11 within a reasonable time, normally not to exceed one year from entry of the order authorizing the operation of the business.

Trustees who are deficient in their administration of operating cases will be subject to a wide range of compliance measures by the United States Trustee or the court.

### 2-3.8

#### **CASE PROGRESS**

Section 704(1) provides that a trustee shall "close [an] estate as expeditiously as is compatible with the best interests of parties in interest." Delays in case closing diminish the return to creditors, undermine the creditors' and public's confidence in the bankruptcy system, increase the trustee's exposure to liability, raise the costs of administration and, in cases involving non-dischargeable prepetition tax liabilities, expose the debtor to increased penalties and interest. Delays also give rise to public criticism of the bankruptcy process.

In order to ensure that a trustee complies with the duty to expeditiously close cases under § 704(1), the United States Trustee monitors the number and age of open cases and the reasons they remain open. For United States Trustee reporting purposes, an "old" case is defined as one which has been open more than three years. The United States Trustee will give heightened scrutiny to a trustee's administration of cases and should consider remedial actions when a trustee has an excess of old cases or is not expeditiously administering or closing cases. Traditionally, if the trustee's old cases were ten percent or more of the trustee's total cases, this was viewed as an indicator of an excess of old cases, but the

United States Trustee must consider the percentage of old cases, the number of old cases, general case progress, and other relevant factors in determining whether the trustee has an excess of old cases or is not expeditiously administering or closing cases.

The United States Trustee must periodically review the processing of chapter 7 cases in his/her offices. The areas to be evaluated include:

1. The efficiency and fairness of the United States Trustee's intake and assignment procedures for new cases.
2. The efficiency of the case closing process, including the timely filing of final reports by trustees and the review conducted by the United States Trustee's office.
3. The impact of local rules of the court or local customs on efficient case administration.
4. The adequacy of the regional or district blanket bond and separate bond procedures.
5. The educational and training needs of panel members.

Corrective actions should be taken to improve any areas of weakness. The United States Trustee should also work through proper channels, e.g., the local bar, the clerk of the bankruptcy court, or the chief judge of the bankruptcy court, to improve communications and other identified problems.

## 2-3.9

### **BANKING**

#### 2-3.9.1

#### **General Trustee Responsibilities**

As set out in § 345, the trustee must immediately open a separate account for each estate as soon as funds are received. The accounts must be maintained under the direction and control of the trustee at all times. Accounts may only be maintained at depositories which have agreed to abide by the requirements established by the United States Trustee (see USTM 2-3.9.2). The trustee must notify the United States Trustee of the identity of the banking institution in which estate funds are held and thereafter must immediately notify the United States Trustee of an intent to transfer estate accounts to another banking institution.

Generally, a trustee should utilize a single banking institution<sup>9</sup> and should initially deposit funds to an interest-bearing account in order to maximize the return to creditors. Under no circumstances may monies of separate estates be aggregated or commingled. Bankruptcy-related funds may not be deposited to the trustee's business, personal or trust account.

Funds are to be deposited to the estate bank account promptly after receipt (generally within two business days) and must not be placed in a file while the trustee waits for subsequent events to occur. If the trustee receives currency that cannot be immediately deposited, it should be converted to a cashier's check or money order (any charge to purchase the cashier's check or money order is treated as a cost of administration). All funds are to be kept in a safe place until deposited.

All bank accounts, statements, deposit slips, and checks should be captioned with the bankruptcy case and number in the style of: "Estate of Jane Smith, Debtor, John Jones, Trustee, Case Number 98-00000." Pre-numbered checks and deposit slips shall be used for each account. Services charges are to be avoided. Checks must include a statement that the checks will be void if not cashed in 90 days.

All deposit slips and check stock should be kept in a limited access area. If the trustee uses an automated data processing system to print and issue checks on blank check stock, adequate precautions must be instituted and maintained to ensure that all check stock, including voided checks, is accounted for and that every check in each case is consecutively numbered. Cashier's checks and wire transfers may only be used under extraordinary circumstances, upon approval of the United States Trustee, unless applicable law or regulation requires otherwise (e.g., tax deposits in excess of \$50,000 per 26 C.F.R. Parts 1, 31, and 40). Counter checks may never be used. A copy of the cashier's check or wire transfer bank advice and related documentation must be maintained in the estate file.

The trustee must retain all original bank account statements, deposit slips, and canceled checks for a period of two years from the closing of the case by the court, unless the original documents are submitted to the court or United States Trustee.

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<sup>9</sup>In the interest of diversity, however, the trustee may place investment vehicles in minority-owned banks.

See Handbook Chapter 9 for additional information about the trustee's responsibilities in connection with bank accounts.

### 2-3.9.2 **Depositories**

The trustee may only use a depository that has agreed to comply with § 345, 31 C.F.R. Part 225, and the requirements of the United States Trustee. The United States Trustee can provide the trustee with a list of depositories that meet these requirements. If a bank wishes to be added to the list, it should contact the appropriate United States Trustee for the specific requirements. If a depository fails to comply with the United States Trustee requirements, the trustee should promptly notify the United States Trustee and arrange to move the funds to another depository.

#### 2-3.9.2.1 **§ 345, Pledge of Securities and Collateralization**

It is the responsibility of the trustee to ensure that the banking institution is in compliance with § 345 to the extent of the trustee's deposits. If the aggregate funds on deposit for an estate in a single institution exceed the \$100,000 FDIC insurance limit, the excess funds must be bonded or be collateralized by securities deposited with the appropriate Federal Reserve Bank. The trustee must notify the United States Trustee if the amount on deposit in any individual estate in any single depository exceeds or is expected to exceed \$100,000.

When securities are deposited, a copy of the Federal Reserve document evidencing the deposit must be sent to the United States Trustee. The depository must obtain prior written consent from the United States Trustee to reduce the amount of any collateral posted by the depository. The United States Trustee may, however, allow increases and any substitution of like-kind securities without prior approval.

As required by § 345(b)(2), securities used as collateral must be the kind specified in 31 U.S.C. § 9303, which specifies that government obligations, which are valued at par, may be used as security. A government obligation is defined in 31 U.S.C. § 9301(2) as a public debt obligation of the United States Government and an obligation whose principal and interest is unconditionally guaranteed by the Government. Public debt obligations consist of United States Treasury Bills, Bonds, or Notes. United States Trustees should not accept zero-coupon Treasury Bonds as collateral. While not public debt obligations, banks may also pledge a limited number of other bonds issued or guaranteed by the Government that contain an unconditional guarantee of principal and interest. The United States

Trustee should obtain an opinion from bank counsel or contact the Executive Office before accepting bonds that purportedly contain an unconditional Government guarantee.

If a bond in favor of the United States is filed to protect the deposit of estate funds, § 345 requires the United States Trustee to approve the corporate surety securing the bond. The format for the Surety Bond is at Appendix 2-11. The United States Trustee can only select a surety listed in Treasury Circular 570. See USTM 2-3.10.1. To help the United States Trustee assess the sufficiency of the corporate surety, the Office of Review and Oversight maintains a Bank Surety Bond Tracking System. The system enables the United States Trustee to determine the number and dollar amount of the bonds secured by each corporate surety pursuant to § 345(b)(1). The system provides the information sorted by bank, surety, region, and district. New bonds are added as they are issued. The United States Trustee reviews and updates the tracking system on a semi-annual basis.

#### 2-3.9.2.2 Reports from Depositories

The United States Trustee should require each depository to provide monthly or quarterly bank reports or duplicate monthly statements for all bankruptcy estate accounts on deposit at all branches of the depository within the district. If the financial institution is under bonded or has not pledged a sufficient amount of securities, it should be advised to remedy the deficiency and to provide evidence to that effect to the United States Trustee. If an institution fails to comply, the United States Trustee shall direct the trustee to remove all estate funds from the institution. The depository reports should be reviewed at least every calendar quarter and used to check the accuracy of the trustees' financial reports and the adequacy of their bonds.

#### 2-3.9.2.3 Other Depository Requirements

Funds in the banking institution must be insured by the Federal Deposit Insurance Corporation (FDIC) and the banking institution must comply with the requirements of the Bankruptcy Code and the United States Trustee. In addition to the foregoing, these requirements include, but are not limited to:

- a. Providing original canceled checks with the monthly bank statements mailed to the trustee in whose name the account was opened. Only the trustee in whose name the account was opened is authorized to sign checks

or make withdrawals unless the bank is otherwise instructed in writing by the United States Trustee.

- b. Certifying annually, and upon request, that the trustee has not and will not receive favorable treatment from the bank on non-bankruptcy related business because of the trustee's bankruptcy accounts.
- c. Transferring funds between bankruptcy estates or between bankruptcy estate accounts and non-bankruptcy estate accounts only when presented with an estate check signed by the trustee (except for incoming wire transfers from an independent third party). Verbal or written requests for funds transfers are not acceptable, unless the transfer of funds is between accounts of the same estate. In addition, the United States Trustee must require depository institutions to provide notice by phone of any cash withdrawals and all overdrafts.
- d. Releasing to the United States Trustee, upon request, any and all information pertaining to bank accounts, deposits, instruments, transactions and withdrawals of funds entrusted to or pertaining to the trustee or the United States Trustee or designee in performance of their official duties, and to provide further information including, but not limited to, copies of statements, deposit slips, canceled checks and account agreements as the United States Trustee may from time to time require in the performance of the United States Trustee's official duties at no cost to the United States Trustee.
- e. Waiving all service charges (with the possible exception of chapter 7 operating business accounts) or fees for supplying pre-numbered check and deposit slip stock, computer hardware or software, canceled checks or monthly bank statements.
- f. Implementing adequate controls over on-line banking. Such controls include, but are not limited to: passwords or another method of limiting the ability to open new accounts; periodic verification that the trustee has approved all new accounts; no transfers between estates; no transfers between bankruptcy and non-bankruptcy accounts; no deletion or closure of accounts that have activity; and no changes to an account number if the account has activity.
- g. Complying with any subsequent requirements established by the United States Trustee.

If a depository fails to comply with the United States Trustee requirements, the trustee should promptly notify the United States Trustee and immediately arrange to move the funds to another depository.

### 2-3.9.3 **Investment of Estate Funds**

Section 345(a) provides that a trustee may invest monies of an estate. Estate funds should be deposited at interest or invested in order to provide a maximum, reasonable net return to creditors. Estate accounts generally may be money market accounts or interest-bearing checking accounts. The interest rate should be no less than that available for other similar accounts. The trustee may be held personally liable for lost interest. See In re Charlestown Home Furnishings, 150 B.R. 226 (Bankr. E.D. Mo. 1993).

When substantial funds (e.g., \$50,000) are received by the estate which will not be distributed for an extended period of time (e.g., six months), the trustee should consider higher yield investments such as Certificates of Deposit or Treasury Bills.

In general, investments are to be as risk free as possible. The trustee should exercise care that no withdrawal of funds results in a loss to the estate. The trustee should not make an investment that will predictably delay closing.

Investment vehicles must be opened, issued or purchased in the name of the trustee as trustee of the estate. When the debtor is a corporation or partnership, the trustee should use the debtor's tax identification number. However, when the debtor is an individual, the bankruptcy estate is a separate taxable entity and, therefore, the debtor's personal social security number may not be used to establish the estate bank account. Rather, the trustee must complete an IRS Form SS-4 to obtain a federal identification number for the bankruptcy estate individual debtor. Failure to provide the tax identification number to the bank results in back up withholding being assessed and remitted to the Internal Revenue Service by the banking institution.

See USTM 2-3.3.1 regarding the continued investment of estate funds after the TFR has been filed for an estate.



Under certain circumstances, the trustee may maintain money of the estate in a non-interest bearing accounts. Some of those circumstances are:

1. The interest-bearing account only allows a limited number of withdrawals each month and the trustee needs to pay administrative expenses in excess of the monthly limit;
2. The trustee will be making an interim distribution to creditors; or
3. The trustee is directed by court order to make an immediate distribution.

#### 2-3.9.4 **Review of Bank Account Information by United States Trustee**

The United States Trustee shall establish procedures to routinely review the reports submitted by the authorized depositories to verify that:

1. estate funds are adequately collateralized;
2. trustees are sufficiently bonded;
3. that estate funds are held in interest-bearing accounts;
4. that the bank account information contained in the 180-day reports is accurate; and
5. that all cases with funds are reported by the trustee on Form 3.

The United States Trustee also regularly examines estate account bank statements while reviewing semi-annual reports, TFRs, and TDRs, and as part of routine audits and examinations of panel trustee operations. This ongoing review enables the United States Trustee to determine that:

1. estate funds have been promptly deposited;
2. court ordered disbursements have been made timely;
3. no unauthorized fund transfers or check-kiting has occurred.

Trustees are required to cooperate with the United States Trustee and, upon request, must authorize their banks to release all estate account information to the United States Trustee.

2-3.10 **BONDING**

Pursuant to § 322(a), a trustee does not qualify for appointment until the trustee has filed with the court a bond in favor of the United States of America conditioned on the trustee's faithful performance of the trustee's official duties. The United States Trustee determines the amount and terms of the bond and the sufficiency of the surety on each bond. § 322(b)(2).

The following are the most common types of bonds available for chapter 7 trustees:

1. **individual case bond** - A single trustee is bonded for a single case for a scheduled amount which includes a cushion based upon a percent of funds on deposit. The deposits are monitored and the bond is adjusted as the deposits significantly increase or decrease. This type of bond is often used for trustees in operating chapter 7 cases, trustees who are not panel active, and for trustees who have a case in which the funds on hand exceed the per case limit under a schedule bond.
2. **blanket bond** - This bond may cover multiple cases for one or more trustees. See Appendix 2-12 for a sample blanket bond form.
  - a. **schedule bond** - This bond covers all trustees of a particular group, district, region or other unit, based upon the discretion of the United States Trustee. Each trustee within the group is bonded for an individually scheduled amount and the premium paid by the trustee is based upon the scheduled amount. The scheduled amount should include a cushion based upon a percent of funds on deposit by trustee at the time the bond is renewed. Because of the cushion, there should be no need to adjust a scheduled amount during the term of the bond absent a dramatic fluctuation in the funds on deposit with a particular trustee. These bonds generally have a per-case cap which means an individual case bond is required for cases with funds over a designated amount.
  - b. **aggregate bond** - The term "aggregate" means that the trustee is covered for the full amount of the bond, regardless of the premium actually paid by the trustee and regardless of the amount the trustee had on deposit at the time the bond was obtained. There are two general types of aggregate bonds which are distinguishable by the method used to calculate the total amount of the bond. In one type,

the United States Trustee will fix the amount of the bond based upon 100 percent of the funds on deposit for all of the trustees covered by the bond, with no cushion included. In the second type, the United States Trustee will fix the bond at an amount which is lower than the total amount of the funds on deposit held by all of the trustees, but significantly higher than the total deposit held by any one of the trustees covered by the bond.

In each aggregate bond, the trustee's share of the premium is based upon the amount of the trustee's deposits used to determine the amount of the bond. The amount of the bond and the trustee's premium share are recalculated each time the bond is renewed, usually annually. There is usually no need to adjust the covered amount during the term of the bond, unless the United States Trustee finds that the total funds on deposit have changed dramatically.

The foregoing types of bonds are illustrative only. Ultimately, § 322 and the language of the bond will determine what is covered. Therefore, the language of every bond, including riders and amendments, should be carefully reviewed. Any new or questionable term, such as a limitation on liability or a requirement to give notice, should be brought to the attention of the United States Trustee immediately.

The United States Trustee must ensure that the bond premiums are competitive by periodically seeking bids or making other price comparisons. The United States Trustee should also consider changing bonds and sureties periodically. Most bonds contain a clause that regardless of the number of years the bond is in effect, the surety's liability is limited to the face amount of the bond. Some refer to it as a non-aggregation clause. Thus, if a \$10 million bond is renewed every year for five years, the surety is only liable for \$10 million – not for \$10 million each year for a total of \$50 million. See *In re Endeco*, 718 F.2d 879 (8<sup>th</sup> Cir. 1983).

The United States Trustee's responsibility to monitor trustee bonds is an integral part of the general duty to supervise panels of chapter 7 trustees and chapter 7 cases. See 28 U.S.C. §§ 586(a)(1) and (a)(3). The bond serves to protect any party in interest that is injured as a result of the trustee's breach of duty. Fed. R. Bankr. P. 2010(b).

The United States Trustee must develop a monitoring system that corresponds to the various types of cases and bonds in effect. Although specific individuals within an office should be designated with the primary responsibility to monitor bonds, bonds should be reviewed on an ongoing, office-wide basis similar to the quarterly fee collection program. The trustee has a concurrent obligation to continually review the adequacy of bond coverage.

#### 2-3.10.1 **Selection of the Surety**

The surety on any bond written in favor of the United States of America must be authorized by the Secretary of the Treasury. 31 U.S.C. §§ 9304 and 9308. The Treasury Department publishes Treasury Circular 570, a list of authorized sureties, every July 1<sup>st</sup> in the Federal Register. The Circular is also posted on the Internet and updated frequently at <http://www.fms.treas.gov/c570/index.html>. The Treasury publication must be consulted before approving a bond to identify potential problems (e.g., with state licensing) and to ensure coverage falls within authorized underwriting limits. Underwriting limitations are on a per bond basis. If a bond exceeds authorized underwriting limitations, it cannot be approved absent proper coinsurance or reinsurance.

#### 2-3.10.2 **Selection of the Broker/Agent**

Generally, the selection of a broker/agent involves considerations of convenience, timeliness in responding to requests, and services (billing, pricing, allocation of premiums, etc.). The agent signing the bond must have a valid power of attorney that authorizes the agent to write the applicable bond, including a bond of the appropriate type and amount. See Appendix 2-12 for a sample blanket bond form that includes a sample power of attorney.

#### 2-3.10.3 **Chapter 7 Bond Clauses**

The trustee's bond is required by statute. At a minimum, each covered trustee must be a principal on the bond, it must be written in favor of the United States of America and must be conditioned on the faithful performance of the trustee's official duties. Most bonds contain additional language depending on what has been negotiated. The following identify the types of clauses most commonly found with bonds:

1. No joint and several liability among trustees.

2. A reference to cases in which the trustee was appointed by the United States Trustee.
3. A clause that the trustee shall obey lawful orders of the bankruptcy judges and requirements of the United States Trustee.
4. A time frame for serving notice of cancellation on the United States Trustee. A 60-day notice is common. A longer time limit may be preferable if the United States Trustee is dependent on a single bonding company.

The bonding company will likely seek indemnification from the trustee for any payments the bonding company is required to make to third parties. Since the bond protects estate beneficiaries and not the trustee, a trustee may wish to consider obtaining professional liability insurance coverage. Such coverage is usually an overhead expense and not recoverable from the estate.

If an elected trustee is not a panel member, the trustee must obtain a separate bond and provide it to the United States Trustee.

#### 2-3.10.3.1 Per Case Limitations

The surety company will often include a provision that limits liability in a regional or district blanket bond to a specific dollar amount per case. The per case limit should be high enough to minimize the number of individual bonds that may be necessary. At the same time, the per case limit must be carefully monitored and considered in the context of overall coverage because it may convey a false sense of security. For example, a \$500,000 limit per case may be viewed as adequate, but when the overall coverage of the trustee is only \$1.5 million, three large cases could subsume the whole coverage. The dollar limits will vary depending upon the size of the asset cases in a given locality and the range of trustees' caseloads; they also impact the type of monitoring that must be done.

The per case limitation clause should be stated as a maximum amount of coverage instead of indicating that once the dollar amount is reached the case is removed from coverage.

#### 2-3.10.3.2 Per Trustee Limitations

The surety may also include a provision that limits liability in a regional or district blanket bond to a specific dollar amount per trustee. In negotiating this limit, the

United States Trustee should use existing or projected bank balances as a baseline and add a cushion. The general practice has been to use a 50 percent cushion factor. Thus, if a trustee has \$100,000 on deposit as of the effective date of the bond, the per trustee limitation on the bond can be fixed at \$150,000. The cushion is designed to protect against fluctuations in account balances and the existence of unreported funds and unliquidated assets. It also avoids the need for the United States Trustee to constantly adjust bond limits throughout the year, absent a dramatic change.

A cushion may not be necessary in regions utilizing a regional or district blanket bond in which the per trustee limit is equal to the total amount of the bond.

#### 2-3.10.4 **Fixing the Face Amount of the Bond**

When a regional or district blanket bond is contemplated (i.e., one that covers more than one trustee), the United States Trustee must establish a method to fix the face amount of the bond and to prorate the premium among the trustees.

The simplest method of fixing the face amount of a bond covering more than one trustee is to calculate the minimum bond coverage required for each individual trustee and to add those amounts together. For example, a bond covering five trustees, each of whom requires a minimum bond of \$200,000, might have a face amount of \$1,000,000. In a district or region with a large number of trustees covered by a bond, the United States Trustee may consider reducing the face amount of the bond below the sum of the individual trustee amounts.

#### 2-3.10.5 **Prorating the Premium**

The premium can be prorated on the same basis that the face amount of the regional or district blanket bond was calculated. Assume, for example, three trustees are covered. Two trustees require \$300,000 bond coverage and one requires \$400,000 coverage. The premium for the \$1,000,000 bond would be prorated at 30 percent for the first two trustees and 40 percent for the third trustee.

The United States Trustee should recalculate the face amount of the bond and prorate the premium no less than annually. The broker/agent should be able to assist the United States Trustee by making the proration based on information supplied by the trustee. The broker/agent also may agree to bill the premium directly to the trustee. The United States Trustee should ensure that the trustee properly pro-rates the bond premium among the trustee's asset cases.

### 2-3.10.6 **Monitoring Trustee Bonds**

The United States Trustee should review the adequacy of most types of trustee bonds as frequently as the United State Trustee determines appropriate, but no less than at least quarterly. Factors that influence this decision include the historical volatility of account balances, a trustee's bonding history, the size of estates, and the type of bond.

The United States Trustee should review a trustee's cash balances as of the starting point for the bonding review. These cash balances should be verified from sources independent of the trustee's reports. Examples of independent sources are duplicate bank statements and bank reports summarizing bankruptcy estate accounts that are provided by the depositories directly to the United States Trustee.

The United States Trustee should notify the depository banks and emphasize the need to report on all investments of bankruptcy estate funds. Bank reports frequently omit investments such as certificates of deposit, but these investments can often involve the largest amount of cash on hand in the estates.

The trustee must report all accounts and investments in the 180-day reports filed with the United States Trustee.

The United States Trustee should also check the adequacy of the trustee's bond where it is evident that the trustee will receive large sums. The trustee must inform the United States Trustee of any situation, such as an upcoming asset sale or the operation of a business, which may necessitate a separate trustee case bond or an increase in bond coverage. The trustee's regional or district blanket bond may not cover the trustee's operation of a business in a chapter 7 case. The trustee should discuss with the United States Trustee whether it is necessary for the trustee to acquire a separate bond.

When the United States Trustee determines that the amount of a bond should be increased, the trustee should be so advised. The trustee's failure to adequately bond estate funds may constitute grounds to seek the trustee's removal from a case or to take other appropriate remedial action.

### 2-3.10.7 **Auctioneer Bonding**

The trustee must ensure that auctioneers are adequately bonded, prior to taking possession of estate property, in an amount that is sufficient to cover all receipts

from the sale. The bond should be in favor of the United States of America and distinct from any other auctioneer's bond required under state law. The amount of the bond will be established by local bankruptcy rule or the United States Trustee. The trustee should confirm that the auctioneer is bonded in an appropriate amount to cover all estates in which the particular auctioneer has been employed and the United States Trustee should monitor the adequacy of the bond. All original bonds should be forwarded to the United States Trustee.

## 2-3.11 **STATISTICS: CASELOAD AND DISTRIBUTIONS TO CREDITORS**

The purpose of statistics is to determine whether cases are administered competently and expeditiously by a trustee. The statistics are used by field offices, regional offices, and the Executive Office. Both caseload statistics and closed case distribution statistics are an integral component of the trustee's performance review.

### 2-3.11.1 **Caseload Statistics**

The following statistical information from ACMS should be reviewed for each trustee on a quarterly basis: the number of chapter 7 no-asset cases pending 60 days or more after the date when the § 341 meeting was held; the status of final reports and final accounts; and the asset and no-asset caseload.

The United States Trustee must furnish a quarterly report to the Executive Office of the number of open chapter 7 cases without an approved final report per trustee. The Executive Office will provide the region with the format and instructions for maintaining and reporting caseload statistics, and will compile the data and provide statistical reports to the United States Trustee.

### 2-3.11.2 **Distribution Statistics**

The Executive Office will furnish the region with a spreadsheet format and instructions for maintaining and reporting distribution statistics. This information is to be reported semi-annually to the Office of Review and Oversight, which compiles and provides statistical reports to the United States Trustees. For a discussion of the new Distribution Report for Closed Asset Cases (Form 4), see USTM 2-3.3.3.1



**2-3.12      RESPONSE TO AUDITS**

Audits provide information concerning a trustee's financial management, internal control procedures, organizational support, and legal administration of cases.

As part of the United States Trustee's ongoing supervision of trustees, a system to audit chapter 7 trustee operations has been established. Under this system, the trustee is subject to an audit or field examination at least once every four years. An audit conducted by the Office of Inspector General (OIG) must occur at least once every eight years. Thus, during an eight-year cycle, every trustee who administers a chapter 7 estate will receive at least one audit conducted by the OIG and at least one UST Field Examination conducted by the United States Trustee (unless a second OIG audit is performed in lieu of the UST Field Examination). As an example of the most common eight-year cycle: if an OIG audit was conducted in FY98, a UST Field Examination will be performed in FY2002, and another OIG audit will be conducted no later than FY2006.

Non-panel trustees are included in the audit/examination cycle. However, at the United States Trustee's discretion, an OIG audit or UST Field Examination may be waived if the non-panel trustee's few remaining cases will be closed within a short period. Key factors to be considered are the number and age of the cases,

the amount of funds on hand, and the possible benefit to be derived from the audit/examination. Examples of when the United States Trustee may prefer to proceed with the audit or examination are:

1. A trustee resigned or was not reappointed, but still has ten asset cases that will be closed during the next two to three years.
2. An elected trustee has a very large case that has been open for several years.

The Office of Review and Oversight suggests that non-panel trustees be scheduled for an OIG audit or a UST Field Examination if the trustees have more than ten cases or a large amount of funds on hand, or if they have not been audited or examined within the past four years.

In addition to the audits and examinations, Case Administrative Reviews may be conducted by the United States Trustee as and when deemed necessary or appropriate by the United States Trustee. The United States Trustee also meets annually with the trustee in a Trustee Conference.

### 2-3.12.1 **OIG Audits**

OIG audits are designed to identify a trustee's internal control weaknesses in case administration and cash management practices. Prior to the audit, the United States Trustee should communicate any concerns about the trustee to the auditor.

An OIG audit will contain one of the following three opinions: (1) "Adequate"; (2) "Adequate Except For" noted deficiencies; and (3) "Inadequate." Audit deficiencies noted as consequential require special consideration. Consequential deficiencies indicate potential for fraud, are serious internal control weaknesses, or are chronic, repeat deficiencies. *See the 1998 Chapter 7 Initiatives*, pp. 5-6 and Appendix 2-13.

At the conclusion of an audit, the OIG will conduct an exit conference with the trustee. The United States Trustee should attend the conference to determine the appropriate remedial actions that may be necessary. A written report of the results of the audit is issued to the United States Trustee within 30 days of the exit conference. The United States Trustee forwards a copy of the report to the trustee and requests a written response within 45 days of the date of the written audit report, confirming that corrective action has been taken and changes implemented. Whenever an audit report contains a consequential finding or a series of less consequential findings, an on-site visit to the trustee's office must be made to verify compliance within six months of the trustee's response.

An OIG audit should be closed within six months from the date of the audit report. A written request that the audit be closed must be submitted by the United States Trustee to the Office of Review and Oversight regardless of whether or not deficiencies were noted. When deficiencies have been noted, and the United States Trustee has determined that a trustee has corrected all noted deficiencies, the audit closure memorandum should contain a written recommendation from the United States Trustee to close the audit, a description of the on-site visit (if one was conducted) or any other action taken to verify that all deficiencies were corrected, a copy of the trustee's response addressing each noted deficiency, and all relevant documents which support the United States Trustee's recommendation.

Refusal by the trustee to implement the necessary changes should be reported to the Assistant Director for Review and Oversight and the Deputy Director, with a recommendation as to the appropriate enforcement action.

### 2-3.12.2 **UST Field Examinations**<sup>10</sup>

UST Field Examinations are conducted by the United States Trustee in accordance with the uniform procedures adopted by the United States Trustees in April 1999. The UST Field Examinations are designed to identify whether the trustee's accounting and cash management practices are adequate to safeguard estate assets. Written notice of deficiencies and required changes with deadlines for implementation must be provided to the trustee and to the Office of Review and Oversight. A written response to the report is required from the trustee within 45 days. Whenever a UST Field Examination report notes a consequential deficiency or a series of less consequential deficiencies, a visit to the trustee's office should be made to verify compliance. The UST Field Examination report, along with the trustee's response, must be maintained in the trustee oversight file. Appropriate remedial action should be taken by the United States Trustee for failure by the trustee to correct noted deficiencies or to meet deadlines set forth in the report. All post-examination activity and closure should be concluded within six months. Closure is achieved by submission of the United States Trustee's memorandum or letter to the Office of Review and Oversight explaining how each deficiency has been resolved, attaching a copy of the trustee's response to the report and requesting closure.

### 2-3.12.3 **Consequential Findings**

Both OIG audits and UST Field Examinations may report deficiencies that are considered consequential. These types of deficiencies require special consideration. The United States Trustee Program defines consequential deficiencies as those deficiencies which indicate the potential for fraud, are serious internal control weaknesses, or are chronic, repeat deficiencies, in contrast to deficiencies which are ministerial in nature. See Appendix 2-13 for a non-exhaustive list of consequential deficiencies. When an audit contains one or more consequential deficiencies, there are certain requirements for resolving each deficiency, one of which is that the trustee's audit response must include appropriate documentation which demonstrates correction of the deficiencies.

Depending upon the number and severity of the specific audit deficiencies, the United States Trustee will visit the trustee's office to verify the trustee's corrective actions. Follow-up office visits are required when: (1) an audit or examination contains certain consequential deficiencies, as identified at Appendix 2-13;

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<sup>10</sup>The UST Field Examination replaces the Accelerated Restricted Scope (ARS) review.

(2) correction of a consequential deficiency, or a series of less than consequential deficiencies, cannot be verified by examining the documentation submitted with the trustee's response to the audit or examination report; or (3) due to the nature of the consequential deficiency, or series of less than consequential deficiencies, correction can only be verified at the trustee's office.

#### 2-3.12.4 **Inadequate OIG Audit Opinion or UST Field Examination Conclusion**

A trustee who receives an inadequate audit opinion from the OIG or an inadequate conclusion from a UST Field Examination will be suspended from active rotation, in accordance with the Administrative Procedures. See Appendix 2-5. The trustee will receive written notice of the suspension pursuant to the Administrative Procedures, and an interim directive requiring immediate suspension of case assignments may be issued, if the circumstances under § 58.6(d) exist. Reinstatement of the trustee requires the approval of the Deputy Director. Prior to reinstatement, the trustee shall provide evidence that the necessary corrective actions were implemented. The United States Trustee shall review the trustee's response and make an on-site visit to the trustee's office to verify compliance. To expedite the trustee's reinstatement, the audit or examination closure memorandum sent to the Assistant Director should state that reinstatement is requested. The Assistant Director will forward the request to the Deputy Director with a recommendation.

If the United States Trustee believes that the inadequate audit opinion or examination conclusion is unwarranted, because of factual inaccuracy or a mistake in judgment, or for another reason, the United States Trustee should immediately notify the Assistant Director to request advance approval from the Deputy Director for the trustee to remain on rotation. The United States Trustee will need to provide written documentation in support of retaining the trustee on rotation and may be requested to visit to the trustee's office to determine the advisability of keeping the trustee on rotation. The Assistant Director will review the documentation and forward a recommendation to the Deputy Director, who will determine whether or not the suspension will be waived.

#### 2-3.12.5 **Case Administrative Reviews**<sup>11</sup>

The Case Administrative Review (CAR) is discretionary; it may be conducted if, and whenever, the need arises. A CAR addresses issues that include the trustee's

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<sup>11</sup>The Case Administration Review replaces the Field Office Visit (FOV).

pursuit of assets, the filing of objections, the closing of cases, compliance with laws and United States Trustee requirements and all other matters relevant to a case. At the discretion of the United States Trustee, the CAR may also incorporate internal control reviews and testing that go beyond the scope of a Field Exam.

When appropriate, the trustee will receive a written notice of deficiencies with deadlines for implementing corrective actions. The trustee should provide a written response to the United States Trustee within 45 days of the date of the written notice. The United States Trustee may arrange a follow-up visit or accept documentation to verify implementation of the corrective actions described in the trustee's response.

#### 2-3.12.6 **Trustee Conferences**

The United States Trustee will meet with each trustee no less than once a year. The substance of the trustee meeting should be directed to any area which the trustee's oversight file indicates may call for attention. The trustee meeting should include a review of the trustee's performance in case reporting and case closing, administration of estate assets, distributions to creditors, and performance of the trustee's other duties under § 704. At least every other year, the visit shall take place at the trustee's office.

#### 2-3.13 **RESPONSE TO UNITED STATES TRUSTEES**

The trustee must timely and appropriately respond to the United States Trustee's requests, whether those requests are for specific actions or information. The trustee's responses should be timely, professional, considerate, clear and accurate. The trustee should demonstrate a willingness to attend and participate in training provided by the United States Trustee.

Copies of written responses, notes of oral responses, training attendance records and responses to UST enforcement actions should be maintained in the trustee's performance review file.

#### 2-3.14 **INVESTIGATION OF AND RESPONSE TO BANKRUPTCY FRAUD AND ABUSE**

Statements of financial affairs and schedules of assets and liabilities must be reviewed thoroughly and diligently and the debtor must be examined carefully to detect abuse or criminal activity. Section 3057 of title 18 requires trustees to

report suspected violations of federal criminal law to the appropriate United States Attorney. Depending on local practice, the trustee should transmit the referral through the United States Trustee or furnish a copy to the United States Trustee. The United States Trustee should establish the proper procedure to be followed in their region in coordination with the United States Attorney. See USTM 2-2.11.

The trustee must thoroughly and diligently review schedules of assets and liabilities and statements of financial affairs, and statements of current income and expenses for evidence of substantial abuse that may provide the basis for a motion to dismiss pursuant to § 707(b). The trustee must assist the United States Trustee in the prosecution of the motion to dismiss if filed by the United States Trustee. See USTM 2-2.3.4.

The trustee must object to the discharge of a debtor if the debtor has not complied with the provisions of § 727(a) or if the debtor has committed any of the acts described therein. The trustee should not oppose the discharge of particular debts under § 523(a). See USTM 2-2.2.6.

The United States Trustee must maintain in the trustee's performance review file a list of all criminal referrals, § 707(b) referrals and objections to discharge brought by the panel trustee; the list should contain the case name, case number and outcome.

### 2-3.15

#### **RESPONSE TO PUBLIC COMPLAINTS**

All complaints concerning a trustee should be made in writing. Upon receipt of a public complaint, the United States Trustee should send it to the trustee requesting a response within a reasonable time. Each complaint is to be independently reviewed and should not be evaluated solely on the basis of the trustee's response. Appropriate remedial action should be taken on all valid complaints.

If the complainant has requested confidentiality or if there is another reason to keep the name of the complainant confidential, then the issue may be raised by letter from the United States Trustee to the trustee without identifying the complainant.

All complaints and a full report of the investigation are to be maintained in the oversight file. A pleading requesting a trustee to close a case, to abandon estate property in a case more than 60 days after the section 341 meeting is concluded, to distribute estate funds, or seeking the removal of the trustee may be considered a public complaint.

2-3.16

**RETENTION AND COMPENSATION OF PROFESSIONALS**

The United States Trustee reviews the trustee's selection and monitoring of professionals. The employment must be appropriate under the circumstances of the case. Routine employment of professionals and the use of boiler plate language justifying the employment should not be allowed. The employment application should evidence that the trustee has analyzed the litigation or other work to be performed and has determined the costs and benefits of the work prior to employing the professional. The United States Trustee should review pleadings, documents or reports drawn by the trustee's professionals and attend court hearings in which the trustee's professionals appear so that an assessment of the professionals' preparation and demeanor as well as the professional quality of the service or presentation can be made. The trustee may not delegate his/her § 704(b) decision-making authority to professionals. The trustee's efforts to achieve greater diversity among the professionals employed should be determined.

The United States Trustee reviews the trustee's exercise of control over fees and expenses of professionals. The compensation request should evidence the trustee's determination that the professional has provided quality professional services, the requested fees and expenses are reasonable and the work was effective. The trustee's approval of the compensation request must be evident in the compensation request. See Appendix 2-8 – Guidelines for Reviewing Applications for Compensation and Reimbursement of Expenses (Jan. 30, 1996), Section II, A.5. Professional fee applications must not include time spent on trustee duties; expense requests must include only actual and necessary expenses. The trustee must be effective in negotiating reductions or filing objections to fee applications, when appropriate.

For a general discussion of professional retention and compensation, see USTM 2-2.7 and 2-2.8, respectively, and Appendix 2-8.

2-3.17

**THE TRUSTEE PERFORMANCE REVIEW**

The ongoing review of a trustee's performance is an integral part of the United States Trustee's duties. The observation and review of matters relating to trustee performance should be documented for later reference.

Each trustee is monitored on an ongoing basis by a performance review team designated by the United States Trustee or Assistant United States Trustee. The performance review team normally consists of a staff attorney and a bankruptcy

analyst or paralegal. The “team concept” helps ensure that both financial and legal case administration matters are fully considered. Each team member does not need to review all aspects of a trustee’s performance.

Effective May 1, 2000, the frequency of performance reviews changed. The United States Trustee now prepares a written review of each panel trustee’s performance at least once every two years.<sup>12</sup> More frequent performance reviews might be appropriate, however, for new trustees or if performance issues arise.

The goal of the review is to provide information about the trustee’s competency, adherence to fiduciary standards, and commitment to pursue assets for the benefit of creditors. The performance review takes into account the factors described in this chapter, including (but not limited to):

1. the size and age of the trustee’s caseload;
2. the trustee’s progress in closing cases;
3. the trustee’s performance in section 341 meetings and in court;
4. the trustee’s procedures for safeguarding estate assets;
5. professional costs incurred by the trustee and maximization of funds distributed to creditors;
6. the number and nature of complaints against the trustee as well as the trustee’s responsiveness in addressing the complaints;
7. the trustee’s cooperation in furnishing reports and requested information to the United States Trustee;
8. the trustee’s judgment in determining whether to administer assets; and
9. the trustee’s demeanor in dealing with debtor’s, creditors, and members of the general public.

The conclusions and recommendations contained in a performance review should be fully documented in the United States Trustee’s oversight file for the respective

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<sup>12</sup>Biennial performance reviews are not required for non-panel trustees.



trustee. The trustee will receive a copy of the performance review and may discuss it with the United States Trustee personally. Any pattern of case administration that deviates from standards must be brought to the trustee's attention for immediate corrective action. Any written response by the trustee concerning issues raised in the performance review will become part of the United States Trustee's trustee oversight file. The trustee oversight file will be made available to the trustee for review, upon request, except for work papers, intra-agency correspondence, and records or information compiled or used for law enforcement purposes. A FOIA request by a trustee for access to their complete file must be in writing and forwarded to General Counsel, Executive Office for United States Trustee.

## 2-3.18 **RECORDS RETENTION**

### 2-3.18.1 **By the Trustee**

A trustee should maintain an estate file for each individual estate. One part of the file should contain pleadings and related documents. All financial documentation should be maintained in a separate part of the estate file. Documents in addition to Forms 1, 2, and 3 which should be retained by a trustee include, but are not limited to, the following:

1. All documents relating to the financial transactions of the estate (cancelled checks, bank account statements, deposit slips, bills or invoices for estate expenses, other documents received as to estate investments, tax returns or waivers, etc.).
2. All documents relating to the possession and maintenance of assets (receipts for property turned over to trustee, appraisals, inventories, casualty insurance, etc.);
3. All documents relating to the disposition of assets (lien documentation, collection letters, notices or advertisements of sales or abandonments, court orders as to the disposition of assets and the payment of expenses, offers received, auctioneer's reports, etc);

All cases, files, paper and computer accounting records, as well as the computer, should be stored in secure facilities, not accessible to the public. Savings certificates, savings account books, cash, blank checks, and estate checks should be kept in a safe or locked cabinet.

The trustee should develop and maintain a disaster recovery plan for the estate financial and administrative records, as well as for the computer system and data.

Depending on the type of automated data processing software utilized, the trustee should request that the case records be made available in an ASCII format. If this is not possible, the trustee should find out if the vendor will provide an electronic copy of the trustee's case records. Either of these features enables a trustee to more easily transfer their data to another software product should the need arise.

For an asset case, the trustee is required to retain case files and estate accounting records for a period of at least two years after the case is closed during which the trustee may be sued on the bond or as otherwise required by the IRS. § 322(d).

For a no-asset case, the trustee should retain in the estate file all documentation that supports the independent investigation and determination that the case is a no-asset case, for a period of at least two years after the case is closed during which the trustee may be sued on the bond. § 322(d). Such documentation may include: payoff letters, lien search results, appraisals, blue book values, section 341 meeting notes, etc. After the case is closed by the court, the trustee may discard the petition, schedules, and statement of affairs, unless these documents contain the trustee's notes regarding the no-asset determination.

### 2-3.18.2 **By the United States Trustee**

The Program's general policies governing general records retention and disposition are described in USTM 6-24. There are additional requirements for the retention and disposition of trustee oversight files and other information prepared or gathered in connection with the supervision of trustees. See Appendix 2-14.

A trustee oversight file is created for each trustee and maintained in the local United States Trustee's office by the performance review team. This file should contain the trustee's performance reviews, memoranda concerning remedial actions, if any, and all supporting documentation relied upon to prepare performance reviews or take remedial actions.

Supporting documentation includes: correspondence with the trustee regarding 180-day reports, final reports and accounts, case closing, and other matters; memoranda summarizing the review of section 341 meetings, court performance, and retention and compensation requests; the results of audits, examinations, or reviews; copies of relevant pleadings; information on objections to discharge and

§ 707(b) and criminal referrals; public complaints and their disposition; and any other information utilized in support of the performance review or remedial action.

The trustee oversight file also must contain all correspondence and documentation in support of the suspension or non-reappointment of a trustee pursuant to 28 C.F.R. § 58.6.

For purposes of file retention, disposition, and destruction, the following definitions apply:

- ▶ Active trustees: those who are currently receiving cases, either on a regular panel rotation or when another trustee has a conflict.
- ▶ Trustees no longer receiving cases: those whose case assignments have been suspended (panel inactive) or who have retired, resigned, or otherwise permanently had the assignment of cases terminated (non-panel). Often, these trustees continue to administer their existing caseload. However, some of them may have resigned from their cases or may have been removed from the cases by the court.

## **CHAPTER 2-4 COMPLIANCE MEASURES**

### **2-4.1 INTRODUCTION**

The United States Trustee must be prepared to take swift, aggressive actions whenever a trustee demonstrates an inability or unwillingness to perform as a fiduciary or departs from standards. Compliance measures include both remedial and enforcement actions, and play an important and vital role in trustee supervision. Remedial actions are those actions taken by the United States Trustee to improve trustee performance or address trustee deficiencies. Enforcement actions are more serious remedial actions such as those described in this section.

A range of enforcement actions can be taken to ensure prompt, honest, and effective case administration by trustees. These include administrative, civil, and criminal proceedings. The United States Trustee may be able to effectuate a remedy by suspending or terminating a panel member. In other circumstances, the United States Trustee may decide to initiate formal legal proceedings in court or before an administrative tribunal (e.g., state licensing agency). Finally, there may be circumstances that require referral of a possible criminal violation to the

United States Attorney for prosecution. It is critical that enforcement actions be exercised in a manner that is justified by the facts and the law, and in keeping with the high standards of the Department of Justice.

In selecting the appropriate enforcement action to address trustee misconduct, the United States Trustee must consider the nature of the problem, the resources to be committed, and the impact the enforcement action will have on the system. If the nature of the trustee's misconduct reflects dishonesty, deceitfulness, fraud, or the serious mishandling of estate funds, a single substantiated incident may justify immediate action by the United States Trustee to protect estates. These remedies include trustee removal, temporary restraining orders, orders to turnover books and records, and referral to the United States Attorney and state licensing authorities. See USTM Volume 5.

Trustee misconduct below dishonesty, fraud, or immediate asset risk calls for the use of progressive or cumulative remedies that may range in severity from meetings with the trustee to filing motions to compel, seeking disgorgement or surcharge, temporarily suspending the trustee from rotation, not reappointing the trustee to the panel, or seeking permanently to remove the trustee from the panel. Imposition of these remedies is at the discretion of the United States Trustee. The types of conduct that may warrant one or more of these remedies include inadequate reporting or asset investigative efforts, inadequate internal controls, and weak case administration, as well as repeated instances of under bonding. The identification and documentation of these problems are an integral part of supervision and serve to establish a record upon which to base future action.

In commencing any type of enforcement action, the United States Trustee should bear in mind the impact it will have on the integrity of the system. The preference to negotiate and avoid formal proceedings may be outweighed by conduct that undermines the integrity of the bankruptcy system. A trustee must not be able to negotiate the closure of asset cases and leave those with minimal assets for a successor trustee without penalty. Disgorgement, surcharge, disallowance of fees, and the imposition of sanctions must be pursued when appropriate. Moreover, a public record of serious abuses in trustee administration rather than a negotiated resignation of the trustee serves to deter inappropriate conduct.

#### 2-4.2

#### **MOTIONS TO COMPEL**

Section § 704(1) states that a trustee shall “close estate[s] as expeditiously as is compatible with the best interests of parties in interest.” Delays in case closure diminish the return to creditors; undermine the creditors’ and public’s confidence

in the bankruptcy system; increase the trustee's exposure to liability; raise the costs of administration; and, in cases involving non-dischargeable prepetition tax liabilities, expose the debtor to increased penalties and interest. The expeditious closure of cases can be enhanced by filing a motion to compel the filing of a final report.

When evaluating whether to file a motion, it is important to assess the posture of the case and whether there is a reasonable basis for the trustee's delay in closing. For example, if the trustee has requested the court to send notice to creditors to file claims pursuant to Fed. R. Bankr. P. 3002(c)(5), the delay in closing may not be attributable solely to the trustee's conduct, unless the claims bar date has long since passed. Other factors that can cause delays include the need to file tax returns and a request for a review of the return pursuant to § 505(b) (potential 60-180 day delay).

If a final report is filed as a result of a motion, the United States Trustee often expends substantial resources to assist in preparing the report. In such circumstances, a reduction of the trustee's fee, corresponding to the equivalent costs of private accounting or paralegal assistance should be sought. The time spent should be documented so that this objection may be properly presented to the court in conjunction with the hearing on approval of the final report.

A motion to compel a final report should request a deadline for the filing of both the final report and the final account. The motion should also state that the reports must be in a format approved by the United States Trustee. Any order compelling the filing of a final report should provide for consequences if the trustee fails to comply with the deadline for filing an acceptable final report. These consequences should include automatic removal of the trustee from all cases upon the filing of an affidavit of default by the United States Trustee.

### 2-4.3

### **SUSPENSION AND NON-REAPPOINTMENT**

The United States Trustee may temporarily suspend case assignments to a trustee as an enforcement tool. Suspension can lead to non-reappointment to the panel. The United States Trustee must notify the panel trustee in writing of the decision to suspend. The panel trustee will continue to receive cases for the next twenty (20) days or longer if the panel trustee appeals the United States Trustee's action to the Director, Executive Office for United States Trustees. In cases where estate assets are at risk or there appears to be gross misconduct, the United States Trustee may issue an interim directive and the cessation of cases is immediate. The regulation governing suspension of a trustee, and for obtaining review of the

decision, is found at 28 C.F.R. § 58.6. See Appendix 2-5. Strict adherence to the required time tables and procedures is mandatory.

An inadequate audit opinion issued by the Office of the Inspector General or an inadequate UST Field Examination conclusion issued by the United States Trustee indicates an inability to confirm that the trustee is adhering to fiduciary standards. The United States Trustee's options upon receipt of an inadequate opinion or an inadequate conclusion are: 1) suspension (with or without an interim directive; 2) a deferral of suspension with Deputy Director approval; or 3) a waiver of suspension with Deputy Director approval. An interim directive can be issued with the suspension notice only when the continued assignment of cases places estate assets at risk. A deferral of suspension may be appropriate when the audit deficiencies will be corrected and verified within twenty (20) calendar days or less from when the audit report is issued. Waiver of suspension may be appropriate when the United States Trustee believes the inadequate opinion is unwarranted, because of a factual inaccuracy, mistake in judgment or due to the nature and type of deficiencies. If a trustee is suspended for an inadequate audit opinion or examination conclusion, the United States Trustee shall not return the trustee to active rotation without the approval of the Deputy Director.

Unless the United States Trustee allows a late-filed submission, a trustee's failure to file timely semi-annual reports requires suspension from the panel until, at a minimum, the reports are submitted and reviewed by the United States Trustee.

A suspension may also be used in cases where a trustee has a disproportionate number of asset cases that impedes his/her resolution of cases or where a trustee has aged cases that should have been closed. Suspension in these latter instances is for purposes of providing the trustee with sufficient time to address the present cases and demonstrate the ability to receive future cases. The stated goal should be as specific as possible, e.g., final reports must be filed by a date certain.

Suspension is also warranted when a trustee has failed to adhere to acceptable fiduciary standards. For example, the administration of assets for the sole benefit of secured creditors, failure to close cases in an expeditious manner, and failure to examine claims sufficiently may all constitute cause for suspension.

If the trustee voluntarily seeks temporary suspension from case assignments, the trustee should submit a Notice of Voluntary Suspension which conforms to the example at Appendix 2-7. Voluntary suspensions, which are not subject to 28 C.F.R. § 58.6, may result under two scenarios. The first scenario is the

situation where the trustee requests a suspension for personal reasons. For example, the trustee may have health concerns, wish to take maternity leave or need to care for a family member. In the second scenario, the trustee requests a suspension for the purpose of correcting a deficiency or deficiencies in the trustee's administration of bankruptcy estates. If the United States Trustee agrees, 28 C.F.R. § 58.6, as an enforcement tool, is not invoked. Under this scenario, Appendix 2-7 may be modified to delete the time period, so that the United States Trustee determines when the deficiency has been resolved and the suspension may be lifted. If a time period is set and the deficiency has not been remedied, the United States Trustee may need to pursue suspension or non-reappointment.

A review of a trustee's cases that demonstrates a history of serious and frequent failure to administer assets, to properly report on estate administration, or to close cases in a timely manner may result in a decision to not reappoint the trustee to the panel. Non-reappointment may also result from cumulative evidence that a trustee cannot carry out the responsibilities of the office.

See Appendix 2-5 for additional circumstances that may warrant suspension or non-reappointment to the panel. See Appendix 2-6 for the format of the Notice of Suspension or Non-Reappointment.

#### 2-4.3.1 **Case Progress**

To ensure that a trustee complies with the duty to expeditiously close cases under § 704(1), the United States Trustee must monitor the number and age of open cases and the reasons they remain open. For United States Trustee reporting purposes, an "old" case is defined as one which has been open more than three years. The United States Trustee will give heightened scrutiny to a trustee's administration of cases and should consider compliance measures actions when a trustee has an excess of old cases or is not expeditiously administering or closing cases. Traditionally, if the trustee's old cases were ten percent or more of the trustee's total cases, this was viewed as an indicator of an excess of old cases, but the United States Trustee must consider the percentage of old cases, the number of old cases, general case progress, and other relevant factors in determining whether the trustee has an excess of old cases or is not expeditiously administering or closing cases.

#### 2-4.4 **RESIGNATION**

When confronted with evidence of deficiencies and the United States Trustee's intention to take formal action, trustees will frequently resign from the problem

case(s) voluntarily. Whenever a trustee resigns from certain cases, the United States Trustee must assess whether to seek the trustee's removal from all assigned cases pursuant to § 324. If the resignation was negotiated, it should be accompanied by an agreement to expeditiously close all remaining cases within specific time frames and consequences. The agreement must be monitored and enforced aggressively.

## 2-4.5

**REMOVAL**

Section § 324 provides that the court, after notice and a hearing, may remove a trustee for cause. The statute also provides that whenever the court removes a trustee in a case, the trustee shall be removed in all other assigned cases unless the court orders otherwise.

There is wide latitude to bring removal actions under varying fact patterns. The clearest circumstance for removal is where embezzlement or fraud is discovered. Cases where a trustee has failed to timely file reports (e.g., interim reports, final reports, reports of sale); to expeditiously close cases; to timely collect, liquidate, protect, or preserve estate assets; to appropriately investigate estate assets or debtor's conduct; and to pursue actions for preferences, fraudulent conveyances, or turnover may serve as a basis for removal. Finally, there are circumstances where the failure to administer an estate over a significant length of time demonstrates sufficient cause for removal.

The General Counsel of the Executive Office for United States Trustees must review and approve all motions to remove a trustee.

## 2-4.6

**DISALLOWANCE OF FEES, DISGORGEMENT OF FEES AND SURCHARGE**

The disallowance of fees or disgorgement, the recovery of fees previously approved and paid, must be considered a remedy for trustee misconduct or inadequate administration. It ensures adequate funds for a successor trustee's administration and prevents a trustee from receiving an unjust enrichment. Surcharge may be asserted against a trustee whose actions have reduced the amount of income for the estate. An example of lost income is the failure of a trustee to maintain estate funds in an interest-bearing account. Moreover, when the trustee's inaction causes the United States Trustee to perform the trustee's duties, a reduction of the trustee's fees corresponding to the equivalent cost of private legal, accounting or paralegal assistance should be sought. The time spent



should be documented so that this objection may be properly presented to the court in conjunction with any hearing on the matter.

2-4.7

### **SANCTIONS**

Fed. R. Bankr. P. 9011 was amended in 1991 to clarify that sanctions may be imposed for the unnecessary delay or needless increase in the cost of the administration of a case (patterned after F.R. Civ. P. 11). The rule provides that a trustee's signature on a document constitutes a certification that the trustee has read the document; that to the best of the trustee's knowledge, information, and belief, after reasonable inquiry, the document is well grounded in fact and warranted by existing law or is a good faith argument for the extension, modification, or reversal of existing law; and, that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation or administration of the case. When the conduct of a trustee violates Fed. R. Bankr. P. 9011, the United States Trustee should consider filing a motion for the imposition of sanctions.

2-4.8

### **REFERRAL TO STATE LICENSING AUTHORITY**

Many trustees are attorneys or certified public accountants (CPAs). Both attorneys and CPAs are licensed and regulated by state authorities. State boards and associations have promulgated codes and rules of professional conduct to govern technical competence and professional ethics. Breaches of fiduciary duties by trustees who are attorneys or CPAs are to be reported to the relevant state licensing authorities.

A trustee's responsibilities are similar in many respects to those of attorneys and CPAs. Attorneys frequently have fiduciary relationships with their clients, other attorneys, and CPAs, and they must perform their duties promptly. Attorneys and CPAs have obligations of fidelity to their clients. Trustee misconduct is, therefore, relevant to the character and fitness of an attorney or a CPA to perform in that professional capacity. In circumstances demonstrating a level of misconduct impacting on an individual's character and fitness, the United States Trustee shall make a referral to the appropriate disciplinary body. The United States Trustee should become familiar with the procedures of their region's state bar associations and accountancy boards in order to pursue the matter.

A referral to a state licensing authority must be approved by the General Counsel of the Executive Office for United States Trustees.

**2-4.9      LOSS OF, OR INABILITY TO ACCOUNT FOR, ESTATE FUNDS**

Whenever the United States Trustee receives information that a trustee or an employee of a trustee or auctioneer is unable to account for estate funds, the procedures set forth in USTM 5-6 must be followed immediately.

**2-4.10      CRIMINAL REFERRALS**

Whenever it is discovered that a trustee or an employee of a trustee is engaged in conduct that may constitute a federal crime, the United States Trustee must immediately notify the Assistant Director for Review and Oversight and the General Counsel. See USTM Volume 5 for additional procedures.

The United States Trustee shall coordinate with the Executive Office to provide whatever assistance is needed to carry out an investigation of trustee misconduct. The United States Trustee also shall make regular contacts with the Office of the United States Attorney to determine the progress of any criminal investigation or prosecution.

**CHAPTER 2-5: STOCKBROKER AND COMMODITY BROKER LIQUIDATION****2-5.1      INTRODUCTION**

The provisions of §§ 741 through 766 address the manner in which stock and commodity brokers are to be liquidated. Once it has been determined that a debtor is a stockbroker or a commodity broker, the case must be assigned to a trustee as quickly as possible, and the trustee must be urged to liquidate the estate expeditiously in order to lessen the impact of the filing on brokerage customers.

The Securities and Exchange Commission (SEC) and the Securities Investor Protection Corporation (SIPC) should be provided notice of a filing by a stockbroker. The Commodity Futures Trading Commission (CFTC) should be informed of a commodity broker case.

The United States Trustee should be aware that § 109(d) prohibits a stockbroker or a commodity broker from filing under chapter 11. See In re SSIW Corp., 7 B.R. 735 (Bankr. S.D.N.Y. 1980); In re CO Petro Marketing Group, Inc., 11 B.R. 546 (Bankr. 9<sup>th</sup> Cir. 1981), rev'd in part, 680 F.2d 566 (9<sup>th</sup> Cir. 1982). If a broker files a chapter 11 petition, a motion should be made by the United States

Trustee to convert the case to a chapter 7 case or to dismiss it, with specific notice to the SEC and SIPC for the stockbroker and to the CFTC for the commodity broker.

### 2-5.2 **STOCKBROKER LIQUIDATION**

§ 742 exempts the SIPC from the automatic stay provisions of § 362. In fact, once the SIPC has invoked the provisions of the Securities Investor Protection Act of 1970, 15 U.S.C. § 78aaa et seq., all bankruptcy proceedings are stayed and the SIPC trustee liquidates the debtor. If the SIPC chooses not to invoke the provisions of 15 U.S.C. § 78aaa et seq., the United States Trustee should appoint a panel member who has stock liquidation experience. The trustee should be familiar with:

1. The 30 day period to assume or reject executory contracts (§ 744);
2. The segregation of customer accounts (§ 745);
3. The treatment of customers who dealt with the debtor not knowing of the filing (§ 746);
4. The subordination of certain customer claims, such as those of insiders (§ 747), and voidable transfers (§ 749); and
5. The distribution of customer name securities and customer property (§§ 750, 751, and 752).

### 2-5.3 **COMMODITY BROKER LIQUIDATION**

Due to the volatile nature of the futures trading market, a trustee must act quickly so as not to penalize customers unnecessarily. This is especially important because the CFTC does not have authority comparable to that of the SIPC in filing its own proceeding. The following instructions are provided to assist the United States Trustee in supervising the trustee who is assigned to a commodity broker case.

### 2-5.3.1 Identifying and Securing Customer Property

#### 2-5.3.1.1 First Priority

Sections §§ 766(c) and 766(h) prescribe the first priority treatment of both specifically identifiable customer property and non-specifically identifiable customer property (e.g., segregated customer account funds). Customer property is defined at § 761(10).

#### 2-5.3.1.2 Locating, Identifying, and Securing Computer Runs

Daily computer runs should be obtained and the debtor's computer service should be instructed to continue daily runs pending further instruction. Computer runs should contain:

1. A daily equity run reflecting the current status of all customer accounts, and credit balances marked to market as of the close of the prior day's trading.
2. A general ledger that indicates where all customer property and other firm assets are located. It is important to note, however, that debtor records may not be up to date.

#### 2-5.3.1.3 Use of Debtor Personnel

A conference should be held immediately with the debtor's principals, key employees, and accountants. A list must be obtained of customer property accounts, specifically identifiable customer property, the location of physical commodities, the location of documents of title, proprietary accounts maintained by or for the debtor or its own principals, clearing broker or brokers if the firm does not clear its own trades, the names of contacts at exchanges, major commodity trade advisors, and major commodity pool operators. If the debtor's records are not up to date, accountants should be employed to update them to the day of filing.

#### 2-5.3.1.4 Notification to Exchanges

All commodity exchanges should be notified of the trustee's appointment. All exchanges are to be instructed that no further trading in any accounts maintained by or for the debtor's account should be conducted except under the direct

authorization and express authority of the trustee. An accounting of all bonds and securities that may be on deposit with each exchange should be requested.

2-5.3.1.5 Conference with Clearing Brokers

Immediate verification of the status of all customer segregated and non-segregated accounts must be obtained, and clearing brokers instructed to stand by for the liquidation or transfer of open commodity contracts.

2-5.3.1.6 Customer Lists

A list of all customers with open commodity contracts, including names, addresses, and telephone numbers must be assembled.

2-5.3.2 **Transferring or Liquidating Open Commodity Contracts**

2-5.3.2.1 Notice to Customers

Each customer with open contracts pursuant to § 765(a)(2) must be notified, both by telegram and by telephone, that immediate election must be made to either transfer or liquidate open positions and, absent prompt instruction from the customer, that the trustee will liquidate. This notification must be done immediately because positions are at risk and subject to dramatic fluctuations in value. It is highly advisable to require the election from the customer either in writing or by telegram or to have a third party record responses. Otherwise, customers may try to disavow the election to liquidate if the contracts should subsequently appreciate.

2-5.3.2.2 Margin Calls

Margin calls are to be issued to customers with open positions and are to be liquidated immediately if payment is not remitted promptly.

2-5.3.2.3 Estimation of Distributive Shares Percentage

Estimated distributive share percentages for customers should be calculated. In order to transfer customer accounts with open contracts to receiving brokers, an estimated distributive share for each customer is necessary. A preliminary computation of the estimated distributive share is made by computing the percentage of required segregated funds which are actually on hand. For example, if \$1,000,000 in customer segregated funds should be on hand, but only \$250,000

can be located, the preliminary estimated distribution percentage is 25 percent. Adjustments must then be made for unposted items in the debtor's books, administrative expenses, and other charges against the \$250,000 of segregated funds. If administrative expenses incurred in preserving customer property must be paid out of such segregated funds in an estimated amount of \$25,000, and other adjustments will further deplete the fund in an amount of \$25,000, then the adjusted estimated distributive share for each customer will be 20 percent (i.e., \$200,000 divided by the required \$1,000,000).

#### 2-5.3.2.4 Estimated Distributive Share for Transferring Customer Shares

Once the estimated distributive share for transferring customers is calculated, the amount of cash to be transferred to receiving brokers with transferred accounts is determined by taking the estimated distributive share percentage of transferring customer's net equity. New equity is defined at § 761(17). In effect, it consists of the customers' net credit balance at filing, if there are no open contracts in the account or on the date of liquidation or transfer of open contracts, after adjusting for specifically identifiable property and offsetting obligations to the debtor.

#### 2-5.3.2.5 Court Approval

Court approval of estimated distributive share calculations must be obtained prior to transferring open contract accounts on notice to transferring customers. If possible, testimony by an accountant and/or CFTC auditor should be obtained as to how the estimated share was calculated and safeguard adjustments for unposted items made.

#### 2-5.3.2.6 Releases

Release and indemnification agreements from receiving brokers should be obtained prior to transferring accounts.

#### 2-5.3.2.7 Open Contracts

All open contracts for which customers elect liquidation or fail to promptly elect after notification are to be liquidated. Clearing brokers must be instructed to remit customer account funds promptly to the trustee's account.

### 2-5.3.3 **Expedited Interim Distribution of Customer Account Funds**

#### 2-5.3.3.1 **The Questionnaire**

A questionnaire should be sent to all customers reflected on the debtor's books and records as having credit. The questionnaire should instruct each customer to file a proof of claim, should request verification of the balance shown on the debtor's records, a listing of beneficial owners of the accounts, other accounts with the debtor, other debts owed to the debtor, business or personal relationships with the debtor or its principals or employees carrying the accounts, and any other information pertinent to the account to enable the trustee to perform the duties imposed by §§ 746, 747, 750, and 751.

#### 2-5.3.3.2 **Contents of Questionnaire**

The questionnaire should specify that no interim distribution will be made until the questionnaire is returned with all requested information. Each questionnaire should include an affirmation by the customer that the information is true and complete, that the customer submits to the jurisdiction of the bankruptcy court, and that he/she will indemnify the estate for all claims arising out of inappropriate or excessive customer distributions.

#### 2-5.3.3.3 **Interim Distributions**

Questionnaires should be processed immediately and estimated distributive shares calculated for each customer with a confirmed net credit balance. Application should be made to the bankruptcy court, on notice to the CFTC, for authority to make interim distributions to customers with net credit balances and supporting schedules reflecting credit balance accounts and computation of each distributive share. Upon receipt of court approval, interim distributions of the estimated distributive shares should be made. The use of a questionnaire and interim distributions could also be helpful in a stockbroker liquidation.

# **APPENDICES**



**APPENDIX 2-1 Standard Public Vacancy Notice for Chapter 7 Panel Trustees**

## PUBLIC NOTICE

## APPOINTMENT TO PANEL OF CHAPTER 7 TRUSTEES

The Office of the United States Trustee is seeking resumes from persons wishing to be considered for appointment to the panel of trustees who administer chapter 7 bankruptcy cases of the bankruptcy code. The appointment is for cases filed in the United States Bankruptcy Court for the <<district>> of <<state>>, <<division>>. Chapter 7 trustees receive compensation and reimbursement for expenses pursuant to 11 U.S.C. § 326, in each case in which they serve.

The minimum qualifications for appointment are set forth in Title 28 of the Code of Federal Regulations at Part 58. To be eligible for appointment, an applicant must possess strong administrative, financial and interpersonal skills. Fiduciary experience or familiarity with the bankruptcy area is desirable but not mandatory. A successful applicant will be required to undergo a background check, and must qualify to be bonded. Although chapter 7 trustees are not federal employees, appointments are made consistent with federal Equal Opportunity policies which prohibit discrimination in employment.

Forward resumes to the Office of the United States Trustee, <<address>>. All resumes will be kept confidential and should be received on or before <<minimum of two weeks after advertisement is placed>>.

EOUST: ORO 7/27/99 Contact ORO for the most current version.

**APPENDIX 2-2 Initial Appointment Form**

**APPOINTMENT TO THE  
PANEL OF CHAPTER 7 TRUSTEES**

I hereby appoint (NAME) to the panel of chapter 7 trustees for the (DISTRICT). You are designated to be the presiding officer at the § 341 meetings and have the authority to examine debtors under oath (Fed. R. Bankr. P. 2003(b)). The appointment shall not exceed one year commencing (DATE). This appointment is subject to the satisfactory completion of a background check and, in any event, may be terminated anytime at the discretion of the United States Trustee.

By accepting this appointment to the panel or to any bankruptcy case filed under Chapter 7 of the Bankruptcy Code, you agree to allow the United States Trustee access to any and all files and records maintained on behalf of any bankruptcy estate under your administration, including (but not limited to) files maintained on the estate’s behalf by an attorney for the trustee (whether the attorney is a member of your firm or a third party firm).

Dated: \_\_\_\_\_

\_\_\_\_\_  
(NAME)  
United States Trustee for Region \_\_, the Judicial Districts  
Established for  
\_\_\_\_\_  
\_\_\_\_\_

Effective 3/1/97

EOUST: ORO 7/27/99 Contact ORO for the most current version.

**APPENDIX 2-3 Renewal Appointment Form**

APPOINTMENT TO THE  
PANEL OF CHAPTER 7 TRUSTEES

I hereby appoint (NAME) to the panel of chapter 7 trustees for the (DISTRICT). You are designated to be the presiding officer at the §341 meetings and have the authority to examine debtors under oath (Fed. R. Bankr. P. 2003(b)). The appointment shall not exceed one year commencing (DATE) (or if less than one year: "be for the xx period (DATE) to (DATE)), and may be terminated anytime at the discretion of the United States Trustee.

By accepting this appointment to the panel or to any bankruptcy case filed under Chapter 7 of the Bankruptcy Code, you agree to allow the United States Trustee access to any and all files and records maintained on behalf of any bankruptcy estate under your administration, including (but not limited to) files maintained on the estate's behalf by an attorney for the trustee (whether the attorney is a member of your firm or a third party firm).

Dated: \_\_\_\_\_

\_\_\_\_\_  
(NAME)  
United States Trustee for Region \_\_, the Judicial Districts  
Established for

Effective 3/1/97

EOUST: ORO 7/27/99 Contact ORO for the most current version.

**APPENDIX 2-4 Chapter 7 Trustee Performance Review**

AMENDMENT NO. 3 (6/2/97)

**United States Trustee System  
Trustee Performance Review**

Name of Trustee: \_\_\_\_\_

Region/Judicial District(s): \_\_\_\_\_

Original Appointment: \_\_\_\_\_

Most Recent Renewal Appointment: \_\_\_\_\_

Annual Evaluation Period (From/To): \_\_\_\_\_

**SUMMARY**

<b>PERFORMANCE REVIEW FACTORS:</b>	<b>Adequate</b>	<b>Adequate, Except For</b>	<b>Inadequate</b>
1. NDRs			
2. TFRs and TDRs			
3. Section 341 Meetings			
4. Securing Estate Property			
5. Legal Administration			
6. 180-Day and Operating Chapter 7 Reports			
7. Case Progress			
8. Banking			
9. Bonding			
10. Distributions to Creditors			
11. Response to Audits			
12. Response to USTs			
13. Investigation of and Response to Bankruptcy Fraud and Abuse			
14. Response to Public Complaints			
15. Retention and Compensation of Professionals			

*Note: The purpose of the trustee performance review is to document the trustee's performance during the period shown above. The renewal of the trustee's appointment to the chapter 7 panel is based upon a variety of factors, including this performance review. Nothing in this review should be construed as a guarantee of future reappointment.*

[http://www.usdoj.gov/ust/r05/pdfs/Ch\\_7\\_Case\\_Admin\\_Manual.pdf](http://www.usdoj.gov/ust/r05/pdfs/Ch_7_Case_Admin_Manual.pdf)

**CONCLUSION:**

Based upon our review of the factors outlined above, it is our opinion that during the past year the trustee's overall performance was:

\_\_\_\_\_ adequate \_\_\_\_\_ adequate, except for \_\_\_\_\_ inadequate

\_\_\_\_\_  
Date Signature of Reviewer(s)

I concur with the conclusion of the reviewer(s):

\_\_\_\_\_  
Date United States Trustee

**OVERALL COMMENTS AND RECOMMENDATIONS**

(Comments required when overall rating is "adequate, except for" or "inadequate.")

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

EOUST:ORO 6/2/97

**A. TRUSTEE DUTY NO. 1: NDRs**

Prepares and files appropriate reports of no distribution (NDRs).

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Timeliness, accuracy and completeness			
Ability to identify assets to be administered			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 2: TFRS AND TDRS**

Prepares and files appropriate final reports and accounts.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Timeliness, accuracy, and completeness			
Timeliness and accuracy of corrections			
Appropriateness and accuracy of claims objections and proposed distributions			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 3: SECTION 341 MEETINGS**

Effectively conducts §341 meetings of creditors.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Punctuality and efficiency of meetings			
Preparation of trustee; knowledge of petition and schedules			
Thoroughness and appropriateness of questioning given the nature and complexity of the specific case			
Establishment of necessary follow-up deadlines			
Demeanor (appropriate and professional)			
Knowledge of bankruptcy laws and procedures			
Use of substitutes			
Declination of cases (i.e., timely, when appropriate)			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)



**A. TRUSTEE DUTY NO. 4: SECURING ESTATE PROPERTY**

Effectively protects assets when appropriate.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Effectiveness in identifying and inventorying assets			
Effectiveness in securing and protecting estate property			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 5: LEGAL ADMINISTRATION**

Adequately justifies and monitors retention of attorneys for the estate. Prepares or ensures the preparation of appropriate pleadings/notices. Trustee and/or counsel appear effectively before U.S. Bankruptcy Court.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Appropriateness of employment of attorneys for the estate			
Effectiveness in supervising attorneys and other professionals throughout term of employment			
Effectiveness in reviewing attorney compensation applications and negotiating reductions or filing objections, when appropriate			
Trustee's and counsel's familiarity with case			
Effectiveness of research and presentation in pleadings			
Preparation and demeanor of trustee and counsel in court (professional, appropriate)			
Knowledge of and compliance with bankruptcy laws and procedures			
Timeliness			
Service on UST and appropriate parties			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 6: 180-DAY AND OPERATING CHAPTER 7 REPORTS**

Prepares and files appropriate 180-day reports and, when applicable, monthly operating reports.

**B. EVALUATION CRITERIA**

<b>180-day Reports:</b>	<b>Adequate</b>	<b>Adequate, Except For</b>	<b>Inadequate</b>
Timeliness, accuracy and completeness of 180-day reports			
Timeliness and accuracy of corrections to 180-day reports			

(Complete the following section if the trustee has operating chapter 7 cases.)

<b>Reports for Operating Chapter 7 Cases:</b>	<b>Adequate</b>	<b>Adequate, Except For</b>	<b>Inadequate</b>
Knowledge of UST policies regarding operating Chapter 7 cases (e.g., obtaining court order to operate the business, monitoring need for continued operation, terminating operation when appropriate)			
Timeliness, accuracy and completeness of monthly reports			
Effectiveness in monitoring bond coverage (e.g. notification to bonding company about operating case status)			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 7: CASE PROGRESS**

Expediently administers and closes cases.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Efforts to expeditiously close cases, in a manner compatible with the best interests of parties in interest			
Effectiveness and efficiency in collecting and liquidating estate assets			
Soundness of judgment in determining assets to be administered or abandoned			
Effectiveness and efficiency in collecting receivables, preference actions, and other claims			
Effectiveness and efficiency in recovering the maximum amount possible for the benefit of creditors			
Justification for administration of old cases			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 8: BANKING**

Maximizes and safeguards estate deposits/investments. Complies with UST policy on banking.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, except for	Inadequate
Use of approved depositories			
Monitoring of collateralization and reporting problems to UST			
Investment of estate funds			
Avoidance of service charges			
Submission of bank statements to the UST, as appropriate			
Preparation of bank reconciliations for estate accounts and follow-up on outstanding items			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 9: BONDING**

Complies with UST policy on bonding.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Monitoring of bond coverage (e.g., requesting increases or decreases when needed and obtaining individual bonds when appropriate)			
Monitoring of auctioneer bonding			
Payment/proration of bond premium			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 10: DISTRIBUTIONS TO CREDITORS**

Maximizes dividends to creditors.

**B. EVALUATION CRITERIA**

Trustee distribution statistics are for the period covering \_\_\_\_\_ to \_\_\_\_\_.\*

Office/Region/Nation statistics are for the period covering \_\_\_\_\_ to \_\_\_\_\_.\*

	TRUSTEE	OFFICE	REGION	NATION
Total Asset Cases Closed				
Total Receipts				
Receipts per Case (Average)				
% Disbursed to Secured Creditors				
% Disbursed to Priority Creditors				
% Disbursed to Unsecured Creditors				
% Disbursed to Professionals (not including Trustee/Trustee's firm)				
% Disbursed to Trustee/Trustee's Firm (for Trustee Comp. and Atty./Prof. Fees)				

See attached distribution statistical summary (if applicable).\*

**C. COMMENTS (DETAILED NARRATIVE)**

\* Unless otherwise noted, the statistical information in this table is taken from the most recent semi-annual *Summary of Chapter 7 Statistics by Office* and *Percent Analysis of Chapter 7 Statistics by Office*. These charts are distributed by the Office of Review and Oversight as of June 30 and December 31 each year, and present information for the most recent twelve-month period and for the cumulative period since inception (August 1992). Reviewers may use either the twelve-month data or the cumulative data to prepare this table. It is not necessary to attach these charts to the performance review. However, if other charts are used, please include them with the review.

**A. TRUSTEE DUTY NO. 11: RESPONSE TO AUDITS**

Timely and appropriately responds to audits.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Most recent OIG or UST audit opinion (Date: _____ )			
Timeliness and completeness of audit response			
Corrective actions instituted to cure deficiencies			
Internal controls maintained to protect against loss of estate funds			
Accuracy of records and organization of files			
Maintenance of estate records and reports (e.g., regular, ongoing maintenance)			
Familiarity with UST policies/guidelines, including Handbook			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)



**A. TRUSTEE DUTY NO. 12: RESPONSE TO UST**

Timely and appropriately responds to UST requests.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Nature of responses to UST requests			
Attendance at UST training classes and meetings			
Avoidance of and/or response to UST enforcement actions			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 13: INVESTIGATION OF AND RESPONSE TO BANKRUPTCY FRAUD AND ABUSE**

Assists in the discovery and prosecution of criminal referrals, 707(b) cases and opposition to discharge in chapter 7 cases.

**B. EVALUATION CRITERIA**

Key statistics for the period \_\_\_\_\_ to \_\_\_\_\_ :

	Number During Period
Criminal Referrals	
707(b) Referrals	
Objections to Discharge	

**Overall performance:**

	Adequate	Adequate, except for	Inadequate
Thoroughness and diligence of investigations to detect abuse or criminal activity			
Compliance with criminal referral procedures			
Diligence in prosecution of objections to discharge			
Assistance to UST and prosecutor			

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 14: RESPONSE TO PUBLIC COMPLAINTS**

Responds to inquiries from the public and parties in interest. Promptly and appropriately responds to complaints.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Nature of responses to inquiries from the public and parties in interest			
Resolution of matters raised in complaints			

Describe below any public complaints that were frequent and/or serious in nature.

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**A. TRUSTEE DUTY NO. 15: RETENTION AND COMPENSATION OF PROFESSIONALS**

Appropriately retains and compensates professionals.

**B. EVALUATION CRITERIA**

	Adequate	Adequate, Except For	Inadequate
Appropriateness of employment of non-attorney professionals (1)			
Effectiveness in reviewing professional compensation applications and negotiating reductions or filing objections, when appropriate			
Effectiveness in supervising accountants, auctioneers, and other professionals			
Appropriateness of compensation requests submitted by trustee (e.g., professional fee applications do not include time spent on trustee duties, expense requests include only actual, necessary expenses--no overhead)			

(1) See Trustee Duty No. 5 Legal Administration regarding trustee supervision of attorneys.

**C. COMMENTS (DETAILED NARRATIVE)**

(Comments required for each "adequate, except for" or "inadequate" response)

**APPENDIX 2-5 Administrative Procedures (28 C.F.R. § 58.6)****PROCEDURES FOR SUSPENSION AND REMOVAL OF  
PANEL TRUSTEES AND STANDING TRUSTEES**

28 C.F.R. § 58.6

(As of November 6, 1997)

(a) A United States Trustee shall notify a panel trustee or a standing trustee in writing of any decision to suspend or terminate the assignment of cases to the trustee including, where applicable, any decision not to renew the trustee's term appointment. The notice shall state the reason(s) for the decision and should refer to, or be accompanied by copies of, pertinent materials upon which the United States Trustee has relied and any prior communications in which the United States Trustee has advised the trustee of the potential action. The notice shall be sent to the office of the trustee by overnight courier, for delivery the next business day. The reasons may include, but are in no way limited to:

- (1) Failure to safeguard or to account for estate funds and assets;
- (2) Failure to perform duties in a timely and consistently satisfactory manner;
- (3) Failure to comply with the provisions of the Code, the Bankruptcy Rules, and local rules of court;
- (4) Failure to cooperate and to comply with orders, instructions and policies of the court, the bankruptcy clerk or the United States Trustee;
- (5) Substandard performance of general duties and case management in comparison to other members of the chapter 7 panel or other standing trustees;
- (6) Failure to display proper temperament in dealing with judges, clerks, attorneys, creditors, debtors, the United States Trustee and the general public;
- (7) Failure to adequately monitor the work of professionals or others employed by the trustee to assist in the administration of cases;
- (8) Failure to file timely, accurate reports, including interim reports, final reports, and final accounts;
- (9) Failure to meet the eligibility requirements of 11 U.S.C. § 321 or the qualifications set forth in 28 C.F.R. § 58.3 and 58.4 and in 11 U.S.C. § 322;

- (10) Failure to attend in person or appropriately conduct the 11 U.S.C. section 341 meeting of creditors;
- (11) Action by or pending before a court or state licensing agency which calls the trustee's competence, financial responsibility or trustworthiness into question;
- (12) Routine inability to accept assigned cases due to conflicts of interest or to the trustee's unwillingness or incapacity to serve;
- (13) Change in the composition of the chapter 7 panel pursuant to a system established by the United States Trustee under 28 C.F.R. § 58.1;
- (14) A determination by the United States Trustee that the interests of efficient case administration or a decline in the number of cases warrant a reduction in the number of panel trustees or standing trustees.

(b) The notice shall advise the trustee that the decision is final and unreviewable unless the trustee requests in writing a review by the Director, Executive Office for United States Trustees, no later than 20 calendar days from the date of issuance of the United States Trustee's notice ("request for review"). In order to be timely, a request for review must be received by the Office of the Director no later than 20 calendar days from the date of the United States Trustee's notice to the trustee.

(c) A decision by a United States Trustee to suspend or terminate the assignment of cases to a trustee shall take effect upon the expiration of a trustee's time to seek review from the Director or, if the trustee timely seeks such review, upon the issuance of a final written decision by the Director.

(d) Notwithstanding paragraph (c) of this section, a United States Trustee's decision to suspend or terminate the assignment of cases to a trustee may include, or may later be supplemented by an interim directive, by which the United States trustee may immediately discontinue assigning cases to a trustee during the review period. A United States Trustee may issue such an interim directive if the United States Trustee specifically finds that:

- (1) A continued assignment of cases to the trustee places the safety of estate assets at risk;
- (2) The trustee appears to be ineligible to serve under applicable law, rule, or regulation;

- (3) The trustee has engaged in conduct that appears to be dishonest, deceitful, fraudulent, or criminal in nature; or
- (4) The trustee appears to have engaged in other gross misconduct that is unbecoming his or her position as trustee or violates the trustee's duties.

(e) If the United States Trustee issues an interim directive, the trustee may seek a stay of the interim directive from the Director if the trustee has timely filed a request for review under paragraph (b) of this section.

(f) The trustee's written request for review shall fully describe why the trustee disagrees with the United States Trustee's decision, and shall be accompanied by all documents and materials that the trustee wants the Director to consider in reviewing the decision. The trustee shall send a copy of the request for review, and the accompanying documents and materials, to the United States Trustee by overnight courier, for delivery the next business day. The trustee may request that specific documents in the possession of the United States Trustee be transmitted to the Director for inclusion in the record.

(g) The United States Trustee shall have 15 calendar days from the date of the trustee's request for review to submit to the Director a written response regarding the matters raised in the trustee's request for review. The United States Trustee shall provide a copy of this response to the trustee. Both copies shall be sent by overnight courier, for delivery the next business day.

(h) The Director may seek additional information from any party in the manner and to the extent the Director deems appropriate.

(i) Unless the trustee and the United States Trustee agree to a longer period of time, the Director shall issue a written decision no later than 30 calendar days from the receipt of the United States Trustee's response to the trustee's request for review. That decision shall determine whether the United States Trustee's decision is supported by the record and the action is an appropriate exercise of the United States Trustee's discretion, and shall adopt, modify or reject the United States Trustee's decision to suspend or terminate the assignment of future cases to the trustee. The Director's decision shall constitute final agency action.

(j) In reaching a determination, the Director may specify a person to act as a reviewing official. The reviewing official shall not be a person who was involved in the United States Trustee's decision or a Program employee who is located within the region of the United States Trustee who made the decision. The reviewing official's duties shall be specified by the Director on a case by case basis, and may include reviewing the record, obtaining additional information from the participants, providing the Director with written recommendations, or such other duties as the Director shall prescribe in a particular case.

(k) This rule does not authorize a trustee to seek review of any decision to increase the size of the chapter 7 panel or to appoint additional standing trustees in the district or region.

(l) A trustee who files a request for review shall bear his or her own costs and expenses, including counsel fees.



**APPENDIX 2-6 Notice of Suspension or Termination**

**Via Overnight Courier  
Next Business Day Delivery**

**NOTICE OF [SUSPENSION OR TERMINATION]**

**To:** \_\_\_\_\_

**Address:** \_\_\_\_\_

**SPECIFY:** whether you are issuing a suspension, a non-renewal of appointment, or a termination. Any deviation from normal case rotation, e.g., a skipping of a rotation, constitutes a suspension. If you are issuing a suspension, describe the condition or the duration (i.e., for six months).

**DESCRIBE:** in detail, the specific reason or reasons for the decision. Explain —fully— the basis or bases for each reason you rely on. Whenever possible, you should support specific statements or findings in the notice with detailed citations to relevant documents. Describe any history of relevant past problems, instances of inadequate performance, or other factors that you considered or that weighed in your decision.

**CITE:** all relevant materials that document those problems or factors and that document prior communications in which you have advised the trustee of those problems or factors. If you considered and rejected less drastic measures, or if you have been using progressive measures, it is appropriate to explain why you decided not to use lesser measures or to describe the progressive steps you have taken in the past and why they have not resolved the matter.

**Insert the Following Language in Every Notice:**

3. “This decision is final and unreviewable unless you request in writing a review by the Director, Executive Office for United States Trustees, no later than 20 calendar days from the date of this notice. 28 C.F.R. § 58.6(b). To be timely, the request for review must be received by the office of the Director no later than 20 calendar days from the date of this notice. 28 C.F.R. § 58.6(b). Your request for review shall fully describe why you disagree with the United States Trustee’s decision, and shall be accompanied by all documents and materials that you want the Director to consider in reviewing the decision. 28 C.F.R. § 58.6(f). You may request that specific documents in the possession of the

United States Trustee be transmitted to the Director for inclusion in the record. 28 C.F.R. § 58.6(f).

The request for review should be sent to:

Director,  
Executive Office for United States Trustees  
Department of Justice  
901 E Street, N.W.  
Suite 700  
Washington, D.C. 20530

You must send a copy of your request for review, and any accompanying documents and materials, to the United States Trustee by overnight courier, for delivery the next business day. 28 C.F.R. § 58.6(f).”

4. (a) **Unless you are issuing an interim directive, insert:** “The United States Trustee’s decision shall take effect twenty (20) days from the date of this notice unless within that time you seek review from the Director; if you timely seek such review from the Director, the United States Trustee’s decision will take effect upon the issuance of a final written decision by the Director.” 28 C.F.R. § 58.6(c).

(b) **If you are issuing an interim directive** (see 28 C.F.R. §§ 58.6(d) and (e)), your notice must inform the trustee that you have issued the directive. The interim directive shall be set forth in a separate document, and a copy of the directive shall be attached to the notice.

DATE: \_\_\_\_\_

\_\_\_\_\_  
United States Trustee

Additional instructions for Notice:

1. **SEND:** the notice to the office of the trustee by overnight courier, for delivery the next business day, with a copy to the Executive Office for United States Trustees, attention: Director.

2. **ATTACH:** to the notice copies of all pertinent materials upon which the United States Trustee has relied and any prior communications in which the United States Trustee has advised the trustee of the potential action. 28 C.F.R. § 58.6.
3. **ATTACH:** to the notice a copy of 28 C.F.R. § 58.6.

**APPENDIX 2-7 Notice of Voluntary Suspension**

**NOTICE OF VOLUNTARY SUSPENSION**

I, \_\_\_\_\_, a [standing] [panel] trustee in Region [ ], request a voluntary suspension of the assignment of future cases for the following time period [specify]. I request this voluntary suspension for the following reason(s): [specify].

By seeking this Voluntary Suspension, I understand that 28 C.F.R. § 58.6 does not apply.

\_\_\_\_\_  
Date

\_\_\_\_\_  
Name

Received:  
  
\_\_\_\_\_

**APPENDIX 2-8 United States Trustee Program Fee Guidelines****GUIDELINES FOR REVIEWING APPLICATIONS FOR  
COMPENSATION AND REIMBURSEMENT OF EXPENSES  
FILED UNDER 11 U.S.C. § 330  
(Appendix A to 28 C.F.R. § 58)****(a) General Information.**

(1) The Bankruptcy Reform Act of 1994 amended the responsibilities of the United States Trustees under 28 U.S.C. § 586(a)(3)(A) to provide that, whenever they deem appropriate, United States Trustees will review applications for compensation and reimbursement of expenses under § 330 of the Bankruptcy Code, 11 U.S.C. § 101, et seq. (“Code”), in accordance with procedural guidelines (“Guidelines”) adopted by the Executive Office for United States Trustees (“Executive Office”). The following Guidelines have been adopted by the Executive Office and are to be uniformly applied by the United States Trustees except when circumstances warrant different treatment.

(2) The United States Trustees shall use these Guidelines in all cases commenced on or after October 22, 1994.

(3) The Guidelines are not intended to supersede local rules of court, but should be read as complementing the procedures set forth in local rules.

(4) Nothing in the Guidelines should be construed:

(i) To limit the United States Trustee’s discretion to request additional information necessary for the review of a particular application or type of application or to refer any information provided to the United States Trustee to any investigatory or prosecutorial authority of the United States or a state;

(ii) To limit the United States Trustee’s discretion to determine whether to file comments or objections to applications; or

(iii) To create any private right of action on the part of any person enforceable in litigation with the United States Trustee or the United States.

(5) Recognizing that the final authority to award compensation and reimbursement under § 330 of the Code is vested in the Court, the Guidelines focus on the disclosure of information relevant to a proper award under the law. In evaluating fees for professional services, it is

relevant to consider various factors including the following: the time spent; the rates charged; whether the services were necessary to the administration of, or beneficial towards the completion of, the case at the time they were rendered; whether services were performed within a reasonable time commensurate with the complexity, importance, and nature of the problem, issue, or task addressed; and whether compensation is reasonable based on the customary compensation charged by comparably skilled practitioners in non-bankruptcy cases. The Guidelines thus reflect standards and procedures articulated in § 330 of the Code and Rule 2016 of the Federal Rules of Bankruptcy Procedure for awarding compensation to trustees and to professionals employed under §§ 327 or 1103. Applications that contain the information requested in these Guidelines will facilitate review by the Court, the parties, and the United States Trustee.

(6) Fee applications submitted by trustees are subject to the same standard of review as are applications of other professionals and will be evaluated according to the principles articulated in these Guidelines. Each United States Trustee should establish whether and to what extent trustees can deviate from the format specified in these Guidelines without substantially affecting the ability of the United States Trustee to review and comment on their fee applications in a manner consistent with the requirements of the law.

(b) Contents of Applications for Compensation and Reimbursement of Expenses. All applications should include sufficient detail to demonstrate compliance with the standards set forth in 11 U.S.C. § 330. The fee application should also contain sufficient information about the case and the applicant so that the Court, the creditors, and the United States Trustee can review it without searching for relevant information in other documents. The following will facilitate review of the application.

(1) Information about the Applicant and the Application. The following information should be provided in every fee application:

(i) Date the bankruptcy petition was filed, date of the order approving employment, identity of the party represented, date services commenced, and whether the applicant is seeking compensation under a provision of the Bankruptcy Code other than § 330.

(ii) Terms and conditions of employment and compensation, source of compensation, existence and terms controlling use of a retainer, and any budgetary or other limitations on fees.

(iii) Names and hourly rates of all applicant's professionals and paraprofessionals who billed time, explanation of any changes in hourly rates from those previously charged, and statement of whether the compensation is

based on the customary compensation charged by comparably skilled practitioners in cases other than cases under title 11.

(iv) Whether the application is interim or final, and the dates of previous orders on interim compensation or reimbursement of expenses along with the amounts requested and the amounts allowed or disallowed, amounts of all previous payments, and amount of any allowed fees and expenses remaining unpaid.

(v) Whether the person on whose behalf the applicant is employed has been given the opportunity to review the application and whether that person has approved the requested amount.

(vi) When an application is filed less than 120 days after the order for relief or after a prior application to the Court, the date and terms of the order allowing leave to file at shortened intervals.

(vii) Time period of the services or expenses covered by the application.

(2) Case Status. The following information should be provided to the extent that it is known to or can be reasonably ascertained by the applicant:

(i) In a chapter 7 case, a summary of the administration of the case including all moneys received and disbursed in the case, when the case is expected to close, and, if applicant is seeking an interim award, whether it is feasible to make an interim distribution to creditors without prejudicing the rights of any creditor holding a claim of equal or higher priority.

(ii) In a chapter 11 case, whether a plan and disclosure statement have been filed and, if not yet filed, when the plan and disclosure statement are expected to be filed; whether all quarterly fees have been paid to the United States Trustee; and whether all monthly operating reports have been filed.

(iii) In every case, the amount of cash on hand or on deposit, the amount and nature of accrued unpaid administrative expenses, and the amount of unencumbered funds in the estate.

(iv) Any material changes in the status of the case that occur after the filing of the fee application should be raised, orally or in writing, at the hearing on the application or, if a hearing is not required, prior to the expiration of the time period for objection.

(3) Summary Sheet. All applications should contain a summary or cover sheet that provides a synopsis of the following information:

- (i) Total compensation and expenses requested and any amount(s) previously requested;
- (ii) Total compensation and expenses previously awarded by the court;
- (iii) Name and applicable billing rate for each person who billed time during the period, and date of bar admission for each attorney;
- (iv) Total hours billed and total amount of billing for each person who billed time during billing period; and
- (v) Computation of blended hourly rate for persons who billed time during period, excluding paralegal or other paraprofessional time.

(4) Project Billing Format.

(i) To facilitate effective review of the application, all time and service entries should be arranged by project categories. The project categories set forth in Exhibit A should be used to the extent applicable. A separate project category should be used for administrative matters and, if payment is requested, for fee application preparation.

(ii) The United States Trustee has discretion to determine that the project billing format is not necessary in a particular case or in a particular class of cases. Applicants should be encouraged to consult with the United States Trustee if there is a question as to the need for project billing in any particular case.

(iii) Each project category should contain a narrative summary of the following information:

- (A) a description of the project, its necessity and benefit to the estate, and the status of the project including all pending litigation for which compensation and reimbursement are requested;
- (B) identification of each person providing services on the project; and



(C) a statement of the number of hours spent and the amount of compensation requested for each professional and paraprofessional on the project.

(iv) Time and service entries are to be reported in chronological order under the appropriate project category.

(v) Time entries should be kept contemporaneously with the services rendered in time periods of tenths of an hour. Services should be noted in detail and not combined or “lumped” together, with each service showing a separate time entry; however, tasks performed in a project which total a de minimis amount of time can be combined or lumped together if they do not exceed .5 hours on a daily aggregate. Time entries for telephone calls, letters, and other communications should give sufficient detail to identify the parties to and the nature of the communication. Time entries for court hearings and conferences should identify the subject of the hearing or conference. If more than one professional from the applicant firm attends a hearing or conference, the applicant should explain the need for multiple attendees.

(5) Reimbursement for Actual, Necessary Expenses. Any expense for which reimbursement is sought must be actual and necessary and supported by documentation as appropriate. Factors relevant to a determination that the expense is proper include the following:

(i) Whether the expense is reasonable and economical. For example, first class and other luxurious travel mode or accommodations will normally be objectionable.

(ii) Whether the requested expenses are customarily charged to non-bankruptcy clients of the applicant.

(iii) Whether applicant has provided a detailed itemization of all expenses including the date incurred, description of expense (e.g., type of travel, type of fare, rate, destination), method of computation, and, where relevant, name of the person incurring the expense and purpose of the expense. Itemized expenses should be identified by their nature (e.g., long distance telephone, copy costs, messengers, computer research, airline travel, etc.) and by the month incurred. Unusual items require more detailed explanations and should be allocated, where practicable, to specific projects.

(iv) Whether applicant has prorated expenses where appropriate between the estate and other cases (e.g., travel expenses applicable to more than one case) and has adequately explained the basis for any such proration.

(v) Whether expenses incurred by the applicant to third parties are limited to the actual amounts billed to, or paid by, the applicant on behalf of the estate.

(vi) Whether applicant can demonstrate that the amount requested for expenses incurred in-house reflect the actual cost of such expenses to the applicant. The United States Trustee may establish an objection ceiling for any in-house expenses that are routinely incurred and for which the actual cost cannot easily be determined by most professionals (e.g., photocopies, facsimile charges, and mileage).

(vii) Whether the expenses appear to be in the nature nonreimbursable overhead. Overhead consists of all continuous administrative or general costs incident to the operation of the applicant's office and not particularly attributable to an individual client or case. Overhead includes, but is not limited to, word processing, proofreading, secretarial and other clerical services, rent, utilities, office equipment and furnishings, insurance, taxes, local telephones and monthly car phone charges, lighting, heating and cooling, and library and publication charges.

(viii) Whether applicant has adhered to allowable rates for expenses as fixed by local rule or order of the Court.

### Exhibit A--Project Categories

Here is a list of suggested project categories for use in most bankruptcy cases. Only one category should be used for a given activity. Professionals should make their best effort to be consistent in their use of categories, whether within a particular firm or by different firms working on the same case. It would be appropriate for all professionals to discuss the categories in advance and agree generally on how activities will be categorized. This list is not exclusive. The application may contain additional categories as the case requires. They are generally more applicable to attorneys in chapter 7 and chapter 11, but may be used by all professionals as appropriate.

**Asset Analysis and Recovery:** Identification and review of potential assets including causes of action and non-litigation recoveries.

**Asset Disposition:** Sales, leases (§ 365 matters), abandonment and related transaction work.

**Business Operations:** Issues related to debtor-in-possession operating in chapter 11 such as employee, vendor, tenant issues and other similar problems.

**Case Administration:** Coordination and compliance activities, including preparation of statement of financial affairs; schedules; list of contracts; United States Trustee interim statements and operating reports; contacts with the United States Trustee; general creditor inquiries.

**Claims Administration and Objections:** Specific claim inquiries; bar date motions; analyses, objections and allowances of claims.

**Employee Benefits/Pensions:** Review issues such as severance, retention, 401K coverage and continuance of pension plan.

**Fee/Employment Applicants:** Preparation of employment and fee applications for self or others; motions to establish interim procedures.

**Fee/Employment Objections:** Review of and objections to the employment and fee applications of others.

**Financing:** Matters under §§ 361, 363 and 364 including cash collateral and secured claims; loan document analysis.

**Litigation:** There should be a separate category established for each matter (e.g., XYZ Litigation).

**Meetings of Creditors:** Preparing for and attending the conference of creditors, the section 341 meeting and other creditors' committee meetings.

**Plan and Disclosure Statement:** Formulation, presentation and confirmation; compliance with the plan confirmation order, related orders and rules; disbursement and case closing activities, except those related to the allowance and objections to allowance of claims.

**Relief From Stay Proceedings:** Matters relating to termination or continuation of automatic stay under § 362.

The following categories are generally more applicable to accountants and financial advisors, but may be used by all professionals as appropriate.

**Accounting/Auditing:** Activities related to maintaining and auditing books of account, preparation of financial statements and account analysis.

**Business Analysis:** Preparation and review of company business plan; development and review of strategies; preparation and review of cash flow forecasts and feasibility studies.

**Corporate Finance:** Review financial aspects of potential mergers, acquisitions and disposition of company or subsidiaries.

**Data Analysis:** Management information systems review, installation and analysis, construction, maintenance and reporting of significant case financial data, lease rejection, claims, etc.

**Litigation Consulting:** Providing consulting and expert witness services relating to various bankruptcy matters such as insolvency, feasibility, avoiding actions, forensic accounting, etc.

**Reconstruction Accounting:** Reconstructing books and records from past transactions and bringing accounting current.

**Tax Issues:** Analysis of tax issues and preparation of state and federal tax returns.

**Valuation:** Appraise or review appraisals of assets.



**APPENDIX 2-9 Amended Memorandum of Understanding****AMENDED MEMORANDUM OF UNDERSTANDING BETWEEN  
THE EXECUTIVE OFFICE FOR UNITED STATES TRUSTEES  
AND THE ADMINISTRATIVE OFFICE OF THE UNITED STATES  
COURTS REGARDING CASE CLOSING AND POST CONFIRMATION  
CHAPTER 11 MONITORING**

The purpose of this memorandum is to amend the Memorandum of Understanding (MOU) between the Administrative Office of the United States Courts (AO) and the Executive Office for United States Trustees (EOUST) regarding the responsibilities and procedures for the closing of cases and the monitoring of chapter 11 cases after confirmation. This amended MOU seeks to reflect changes in the rules governing bankruptcy procedure since the original MOU and further allocates responsibilities of the case trustee, United States Trustee, and clerk in the case closing process.

Obtaining and maintaining an adequate level of resources to fulfill the responsibilities of the MOU remains a challenge. The standards set forth are a foundation of proper administration of bankruptcy cases. All parties continue to be committed to this goal and the need to examine continually policies and procedures so that they can be improved. Accordingly, this MOU may be modified from time to time as necessary by written agreement between the parties.

Comments, questions, or problems regarding this memorandum and its implementation should be directed to the Working Group established by the AO and the EOUST.

**I. Background**

Since enactment of the nationwide United States trustee program, Pub. L. 99-554 (1986), the AO and the EOUST meet periodically to discuss matters of mutual concern. Representatives of the bankruptcy courts and United States Trustees participate in those meetings. The purpose of the meetings is to delineate responsibilities and examine and improve procedures. The following factors have been established:

- A. The administration of a bankruptcy estate is entrusted to a private person, whether a trustee under chapters 7, 11, 12 and 13 of the Bankruptcy Code, or the debtor itself under chapter 11. As the degree of creditor participation in a chapter 7 liquidation case is often minimal, review by the United States Trustee of the manner a particular estate is being administered is important. Additionally, ensuring that chapter 11 estates have been fully administered, so that the court may close the case, is an important element of effective case administration.

- B. Pursuant to 28 U.S.C. § 586, the United States Trustee has the responsibility to appoint private trustees, oversee their performance, and generally supervise the administration of estates.
- C. Pursuant to 11 U.S.C. § 350, and 28 U.S.C. § 151 et seq., the court's responsibilities includes adjudicating disputes arising in a case and approving certain actions of debtors and trustees. Under 11 U.S.C. § 350, the court has the responsibility to close a case and discharge the trustee.
- D. Pursuant to 28 U.S.C. § 156(b) and Fed. R. Bankr. P. 5001, and 5003, the clerk of the court (clerk) is the recipient and repository of all court records. The clerk also assists the court in carrying out its duties.
- E. The court, the clerk, and the United States Trustee each have responsibility within the scope of their offices, to ensure that cases move expeditiously, efficiently and properly through the system.
- F. In March 1988 the Judicial Conference of the United States directed that clerks' offices not perform or duplicate the case closing review function performed by the United States Trustee. See Resolution of the Judicial Conference, Conf. Rpt. At pp 9-10 (March 1988).
- G. If a case trustee under chapter 7, chapter 12 or chapter 13 has filed a Final Report and Final Account and has certified that the estate has been fully administered, and no objection has been filed by the United States Trustee or a party in interest within 30 days, Fed. R. Bankr. P. 5009 provides that there shall be a presumption that the estate has been fully administered.
- H. In chapter 7 asset cases, prior to the filing of the Final Account and Certification that the Estate has been Fully Administered, the case trustee is to transmit to the United States Trustee a Final Report wherein the trustee details the administration of the estate, including the proposed dividend distribution. Effective August 1, 1993, Fed. R. Bankr. P. 3009 was amended to delete the requirement that the court approve the amounts and times of distributions in recognition of the role of the United States Trustee in supervising trustees and estates.
- I. Pursuant to 11 U.S.C. § 330, the court must approve the compensation and expenses of the trustee and that of any professional paid from estate funds. A case closing process encompassing both the approval of fees and expenses by the court, as well as review of the Final Report by the United States Trustee is desirable.

## II. Responsibilities of the Chapter 7 Case Trustee

- A. Submission of the Final Report - The case trustee shall submit to the United States Trustee a Final Report. The Final Report is the pre-distribution summary of all actions taken by the chapter 7 case trustee to administer the case and a summary of the creditor and administrative claims outstanding at the time of submission to the United States Trustee. It is a signed statement by the trustee, submitted under penalty of perjury, certifying that all assets have been liquidated or properly accounted for and that funds of the estate are available for distribution. Prior to the submission of the Final Report, the trustee shall have ensured that the claims review process is completed, including, if necessary, the completed adjudication by the court of any disputed claim.

The Final Report shall consist of a) the Individual Estate Property Record and Report (United States Trustee Form 1); b) the Cash Receipt and Disbursement Record (United States Trustee Form 2); and c) the proposed dividend distribution report. A proposed Notice of the Final Report and the Application for Compensation and Expenses, in a format similar to that set forth on either Attachment A or Attachment B, shall also be submitted.

With the Final Report, the trustee shall submit to the United States Trustee a) the application or previously entered order of court for trustee compensation and reimbursement of expenses; b) the applications or orders of court for compensation and expenses for all professionals retained by the trustee; and c) appropriate financial documentation relating to the estate to support the Final Report. The applications submitted are to be drawn in accordance with the Guidelines promulgated by the Executive Office for the United States Trustees.

- B. Distribution of Estate Dividends - If the court awards compensation and expenses as provided in the Notice of the Final Report and the Application for Compensation and Expenses and the United States Trustee has approved the Final Report, upon entry of the compensation and expense order, the case trustee shall commence payment of dividends in accordance with the reviewed dividend distribution report. If, however, the court modifies the fees and expenses, the trustee shall not make distribution of dividends until the revised dividend distribution report has been reviewed by the United States Trustee. The payment of the final compensation and expenses shall not be made prior to the payment of the final dividends to creditors and in no event shall the final dividend to creditors be paid later than 30 days after the entry of the final order on compensation and expenses.



- C. Submission of the Final Account, Certification that the Estate has been Fully Administered, and Applications to be Discharged - Within 125 days after the entry of the order of court allowing compensation and expenses, the case trustee shall submit to the United States Trustee a Final Account, Certification that the Estate has been Fully Administered, and Application for Discharge pursuant to Fed. R. Bankr. P. 5009. The Final Account is the trustee's post distribution statement and includes a certification, submitted under penalty of perjury, that all funds have been disbursed consistent with the dividend distribution report and that all checks have been negotiated, or any remaining estate monies have been paid into court, and that the estate has been fully administered. The case trustee shall submit to the United States Trustee all necessary financial documents to support the Final Account.
- III. Responsibilities of Standing Trustee - Within 150 days of the final distribution to creditors in a chapter 12 or 13 case, the standing trustee shall file with the court, pursuant to Fed. R. Bankr. P. 5009, the Final Account, the Certification that the Estate has been Fully Administered, and an Application for Discharge.
- IV. Duties of the United States Trustee in Case Closing - The United States Trustee shall undertake the following efforts with regard to case closings in chapters 7, 12 and 13 cases.
- A. Review of chapter 7 asset reports - The United States Trustee shall review within 60 days of receipt all Final Reports in chapter 7 asset cases utilizing the following procedures:

The United States Trustee shall conduct a thorough review of all asset case reports. This process involves the determination that all assets in the estate were properly administered (i.e., examination of exemptions, abandonments, sales, or other liquidations). All reports shall be reviewed to ensure the inclusion of court orders approving employment, payment of compensation, sales (if applicable) and other actions taken by the trustee in the case. All compensation and expense reimbursement requests filed on behalf of the trustee or other professionals or agents will be reviewed for compliance with the Bankruptcy Code, Rules and the Fee Guidelines. All calculations in the trustee's Final Report, including the calculation of the trustee's fee and proposed dividend to creditors, will be reviewed for accuracy. Based upon a review of case documents received by the United States Trustee, a determination will be made that the trustee has reviewed and properly dealt with all claims. The United States Trustee will rely on the trustee's certification that all claims have been reviewed. If deemed necessary by the United States Trustee, the trustee's certification will be verified by further review of the documents on file with the clerk. Deficiencies in the trustee's

administration or other problems or mistakes will be brought to the trustee's attention for corrective action.

The United States Trustee shall file the Final Report or an amended Final Report, and Application for Compensation and Expenses with the clerk, noting that the report has been reviewed, at or before the end of the 60 day , if all deficiencies are resolved. If the case trustee does not agree with the United States Trustee's position that the report is deficient, the United States Trustee shall file the Final Report with the clerk within 60 days of receipt, indicating the objection of the United States Trustee to the Final Report. The United States Trustee shall also file any objection to the Application for Compensation and Expenses and may combine the objection to the Final Report and to the Application in one document.

If the court orders compensation and expenses in an amount different from the trustee's application, the United States Trustee shall review the trustee's revised dividend distribution report within 10 days of receipt and return it to the trustee noting that it has been reviewed.

With regard to the Final Account, Certification that the Estate has been Fully Administered and Application for Discharge, Fed. R. Bankr. P. 5009 places responsibility on the case trustee to certify that the estate has been properly administered, including documenting the disposition of assets, expenditures, review of claims and final distribution. Although it shall be the United States Trustee's responsibility to see that adequate procedures are in place to ensure an effective and efficient case closing procedure, the United States Trustee is not a guarantor or insurer of the work performed by the case trustee. Rather, the United States trustee shall review the trustee's final account for accuracy and upon completion of the review and the correction of any deficiencies, the United States trustee will file within 30 days of receipt, the Final Account, Certification that the Estate has been Fully Administered, and Application for Discharge of the trustee with the court, and shall provide the following statement: "The United States Trustee has reviewed the Final Account, Certification that the Estate has been Fully Administered and Application for Discharge of the trustee in accordance with the standards set forth in the MOU dated (.....) and has no objection to the trustee's certification that the estate has been fully administered and is ready to close."

- B. Review of chapter 7 no asset cases - the case trustee shall submit a No Distribution Report (NDR) to the United States Trustee , within 60 days of the meeting required by 11 U.S.C. § 341(a) or file the NDR with the Court and serve a copy on the United States Trustee within the same time period. The NDR constitutes the Final Report and Final Account in an estate where the case trustee

has determined that there are no assets to administer. If the original NDR has been submitted to the United States Trustee then the United States Trustee shall file the NDR with the court within five days of receipt.

Because of the nature and volume of no asset cases, a detailed review of each case is not feasible. The United States Trustee's review will be based on an evaluation of a random sample of NDRs submitted by each trustee. Within 30 days of the filing of the NDR, the United States Trustee will, in those cases selected review the schedules to determine that all assets listed were properly exempted or of no value to the estate. If it appears that assets were available for liquidation, the record of the section 341 meeting will be reviewed to see if it explains the failure to liquidate assets. If the information is not adequate, the trustee will be required to provide an explanation. If the deficiencies warrant, the United States Trustee will file an objection to the NDR or move to reopen the case so an objection can be filed. Errors, omissions or a clear failure to perform will result in a more thorough review of that trustee's work and, if deemed appropriate, action will be taken by the United States Trustee. In addition to this process, a verification letter will be sent to the debtor in sampled cases as a further substantiation that assets were not turned over to the trustee.

- C. Review of chapter 12 and 13 cases - With regard to chapter 12 and 13 case closings, the United States Trustee's review will be based on the supervision of the standing trustee through reporting requirements, budget approvals and on site visits as well as an annual audit by an independent certified public accounting (CPA) firm. If the standing chapter 12 and 13 trustee caseload or cash flow falls below the threshold amount for the hiring of an independent CPA, an annual review will be conducted by the United States Trustee's office or other office of the Department of Justice. During an audit, selected cases will be reviewed in depth for the accuracy of receipts and disbursements. Internal controls and procedures will also be scrutinized. The annual audit will be made available to the court if requested.

In order to comply with the provisions of Fed. R. Bankr. P. 5009, in the Final Report and Final Account, the chapter 12 or 13 standing trustee shall certify that the estate has been fully administered. If warranted, the United States Trustee will object to the standing trustee's Final Report and Final Account

If the caseload is not sufficient for the appointment of a standing chapter 12 or 13 trustee, chapter 12 and 13 cases will be processed on a case by case basis in the manner established for chapter 7 asset cases.

V. Court and Clerk - The court and clerk shall undertake the following efforts.

A. Chapter 7 Asset Cases

1. After review by the United States Trustee, all Final Reports and Final Accounts, Certifications that the Estate has been Fully Administered, and Applications for Discharge shall be filed with the clerk. The clerk shall have the responsibility to keep a docket in each case and ensure that all docket entries are accurate and complete. The clerk's office will bring to the attention of the United States Trustee any discrepancies or deficiencies discovered in the course of its processing so that such can be resolved. Staff of the clerk's office, however, should not be used to perform or duplicate the United States Trustee's Responsibilities.
2. Upon filing of the Final Report and Application for Compensation and Expenses, a notice in a form similar to that set forth on Attachment A or Attachment B, shall be given to creditors pursuant to Fed. R. Bankr. P. 2002(f)(8), and 2002 (a)(7). The notice shall be sent by the case trustee or such other person as the court directs as provided under Fed. R. Bankr. P. 2002(a), or the clerk. The notice is to state that the Final Report has been filed, the amount of money in the estate, the amount of compensation and expenses requested by the trustee and the professionals for the trustee (or the amount previously approved by the court), the names and the amount of the approved claim for each entity in a class that will be part of the distribution, the estimated amount of the dividend or the pro rata percent, the date of any hearing or the procedure for filing an objection to the fees or the proposed distribution. If the clerk provides the notice, the case trustee shall provide its content in the format set forth on Attachment A or Attachment B.
3. The clerk shall submit to the court applications for compensation and reimbursement of expenses.
4. Upon filing of a Final Account, Certification that the Estate has been Fully Administered and Application for Discharge of trustee, and if within 30 days of that filing no objection has been filed by the United States Trustee or by a party in interest, the court shall enter an Order closing the case pursuant to 11 U.S.C. § 350 and Fed. R. Bankr. P. 5009.

B. Chapter 7 No Asset Cases

1. Upon filing of the NDR in a no asset case, and the expiration of the time limits for filing objections to the case trustee's report pursuant to Fed. R.

Bankr. P. 5009, and for filing objections to the debtor's discharge pursuant to Fed. R. Bankr. P. 4004(a), the clerk shall authorize payment to the trustee of the fee established by 11 U.S.C. § 330(b).

2. After the above events occur the court, pursuant to 11 U.S.C. § 350 and Fed. R. Bankr. P. 5009, shall enter an order to discharge the trustee and close the case after the expiration of the 30 day period set forth in Fed. R. Bankr. P. 5009.

C. Chapter 12 and 13 Cases

1. After the standing trustee has filed the Final Report and Final Account and Certification that an Estate has been Fully Administered, the court shall close the case, pursuant to 11 U.S.C. § 350 and Fed. R. Bankr. P. 5009.
2. When chapter 12 and 13 estates are individually administered, cases shall be processed and closed in the manner provided for chapter 7 asset cases.

VI. Post Confirmation Chapter 11 Cases

A. Background

1. The AO and EOUST agree that the issue of ensuring that a confirmed plan is implemented to the degree necessary to allow the court to close the case continues to be a challenge to efficient and effective case administration. The following delineates the parameters of responsibility:
  - a. Court and Clerk - As part of the confirmation of a plan, courts have generally provided that, by a specified date, the debtor shall certify to the court that disbursements pursuant to the plan have been undertaken, and that the plan has been substantially consummated, so that an Application for Final Decree can be filed pursuant to Fed. R. Bankr. P. 3022. The clerk will periodically provide the United States Trustee with a list of those cases where an Application for Final Decree has not been timely filed.
  - b. United States Trustee - Because of the United States Trustee's responsibility to monitor the case, and the debtor in possession or trustee, the United States Trustee shall review any application for a Final Decree, and the report(s) required by the order of confirmation. It is within the discretion of the United States Trustee to object to an Application for Final Decree or to the

contents of any reports required by the order of confirmation. If no objection has been filed within 30 days of the filing of the application or report(s), it is presumed that the estate has been fully and properly administered. Where no timely Application for Final Decree has been filed, the United States Trustee shall undertake efforts as the United States Trustee deems appropriate to secure the filing of an Application for Final Decree, or seek an order from the court.

\_\_\_\_\_/S/\_\_\_\_\_  
\_\_\_\_\_/S/\_\_\_\_\_

Administrative Office of  
the United States Courts

Executive Office for  
United States Trustees,  
Department of Justice

*April 1, 1999*

*February 10, 1999*

**Attachment A to the Memorandum of Understanding**

[Note: This attachment to the April 1,1999, MOU has been updated for accuracy & re-formatted for ease of use (2/8/00).]

IN THE UNITED STATES BANKRUPTCY COURT  
 FOR THE \_\_\_\_\_ DISTRICT OF \_\_\_\_\_  
 \_\_\_\_\_ DIVISION

IN RE:

CASE NO. \_\_\_\_\_

\_\_\_\_\_/

**NOTICE OF TRUSTEE’S FINAL REPORT AND APPLICATIONS FOR COMPENSATION**

Pursuant to Fed. R. Bankr. P. 2002(a)(6) and 2002(f)(8), please take notice that \_\_\_\_\_, trustee of the above styled estate, has filed a Final Report and the trustee and the trustee’s professionals have filed final fee applications.

*The Final Report shows receipts of* \$ \_\_\_\_\_  
*and approved disbursements of* \$ \_\_\_\_\_  
*leaving a balance of* \$ \_\_\_\_\_

Applications for chapter 7 fees and administrative expenses have been filed as follows:

<i>Reason/Applicant</i>	<i>Fees</i>	<i>Expenses</i>
<i>Trustee</i>	\$ _____	\$ _____
<i>Attorney for trustee</i>	\$ _____	\$ _____
<i>Appraiser</i>	\$ _____	\$ _____
<i>Auctioneer</i>	\$ _____	\$ _____
<i>Accountant</i>	\$ _____	\$ _____
<i>Special Attorney for trustee</i>	\$ _____	\$ _____
<i>Charges, U.S. Bankruptcy Court</i>	\$ _____	\$ _____
<i>United States Trustee</i>	\$ _____	\$ _____
<i>Other</i>	\$ _____	\$ _____
<i>Other</i>	\$ _____	\$ _____

Applications for chapter 11 fees and administrative expenses have been filed as follows:

<i>Reason/Applicant</i>	<i>Fees</i>	<i>Expenses</i>
<i>Attorney for debtor</i>	\$ _____	\$ _____
<i>Attorney for</i>	\$ _____	\$ _____
<i>Accountant for</i>	\$ _____	\$ _____
<i>Appraiser for</i>	\$ _____	\$ _____
<i>Other</i>	\$ _____	\$ _____

In addition to the expenses of administration listed above as may be allowed by the Court, priority claims totaling \$ \_\_\_\_\_ must be paid *pro rata* in advance of any dividend to general (unsecured) creditors. The priority dividend is anticipated to be \_\_\_\_\_ percent.

Allowed priority claims are:

<i>Claim Number</i>	<i>Claimant</i>	<i>Allowed Amt. of Claim</i>
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____

Claims of general (unsecured) creditors totaling \$ \_\_\_\_\_ have been allowed and will be paid *pro rata* only after all allowed administrative and priority claims have been paid in full. The general (unsecured) dividend is anticipated to be \_\_\_\_\_ percent.

Allowed general (unsecured) claims are as follows:

<i>Claim Number</i>	<i>Claimant</i>	<i>Allowed Amt. of Claim</i>
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____



The trustee’s Final Report and all applications for compensation are available for inspection at the Office of the Clerk, U.S. Bankruptcy Court:

\_\_\_\_\_

Any person wishing to object to any fee application, or the Final Report, must file a written objection within 20 days of the date of this notice, serve a copy of the objections upon the trustee, any party whose application is being challenged, and the United States Trustee. A hearing on the fee applications and any objection to the Final Report will be held at \_\_: \_\_ .m. on \_\_\_\_\_, \_\_\_\_\_, in Courtroom \_\_\_\_\_, United States Courthouse:

\_\_\_\_\_

If no objections are filed, upon entry of an order on the fee applications, the trustee may pay dividends pursuant to Fed. R. Bankr. P. 3009 without further order of the Court.

Dated: this \_\_\_\_\_ day of \_\_\_\_\_, \_\_\_\_\_.

By: \_\_\_\_\_  
Clerk of Court  
[Address]

*Trustee’s name*  
*address*

**Attachment B to the Memorandum of Understanding**

[Note: This attachment to the April 1,1999, MOU has been updated for accuracy & re-formatted for ease of use (2/8/00).]

IN THE UNITED STATES BANKRUPTCY COURT  
 FOR THE \_\_\_\_\_ DISTRICT OF \_\_\_\_\_  
 \_\_\_\_\_ DIVISION

IN RE:

CASE NO. \_\_\_\_\_

\_\_\_\_\_/

**NOTICE OF TRUSTEE’S FINAL REPORT AND APPLICATIONS FOR COMPENSATION**

Pursuant to Fed. R. Bankr. P. 2002(a)(6) and 2002(f)(8), please take notice that \_\_\_\_\_, trustee of the above styled estate, has filed a Final Report and the trustee and the trustee’s professionals have filed final fee applications.

*The Final Report shows receipts of* \$ \_\_\_\_\_  
*and approved disbursements of* \$ \_\_\_\_\_  
*leaving a balance of* \$ \_\_\_\_\_

Applications for chapter 7 fees and administrative expenses have been filed as follows:

<i>Applicant or Reason</i>	<i>Fees</i>	<i>Expenses</i>
<i>Trustee</i>	\$ _____	\$ _____
<i>Attorney for trustee</i>	\$ _____	\$ _____
<i>Appraiser</i>	\$ _____	\$ _____
<i>Auctioneer</i>	\$ _____	\$ _____
<i>Accountant</i>	\$ _____	\$ _____
<i>Special attorney for trustee</i>	\$ _____	\$ _____
<i>Charges, U.S. Bankruptcy Court</i>	\$ _____	\$ _____
<i>United States Trustee</i>	\$ _____	\$ _____
<i>Other</i>	\$ _____	\$ _____
<i>Other</i>	\$ _____	\$ _____

Applications for chapter 11 fees and administrative expenses have been filed as follows:

<i>Applicant or Reason</i>	<i>Fees</i>	<i>Expenses</i>
<i>Attorney for debtor</i>	\$ _____	\$ _____
<i>Attorney for</i>	\$ _____	\$ _____
<i>Accountant for</i>	\$ _____	\$ _____
<i>Appraiser for</i>	\$ _____	\$ _____
<i>Other</i>	\$ _____	\$ _____

In addition to the expenses of administration listed above as may be allowed by the Court, priority claims totaling \$ \_\_\_\_\_ must be paid *pro rata* in advance of any dividend to general unsecured creditors. The priority dividend is anticipated to be \_\_\_\_\_ percent.

Allowed priority claims are:

<i>Claim No.</i>	<i>Claimant</i>	<i>Allowed Amt. of Claim</i>	<i>Proposed Payment</i>
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____

Claims of general unsecured creditors totaling \$ \_\_\_\_\_ have been allowed and will be paid *pro rata* only after all allowed administrative and priority claims have been paid in full. The general unsecured dividend is anticipated to be \_\_\_\_\_ percent.

Allowed general unsecured claims are as follows:

<i>Claim No.</i>	<i>Claimant</i>	<i>Allowed Amt. of Claim</i>	<i>Proposed Payment</i>
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____

The trustee's Final Report and all applications for compensation are available for inspection at the Office of the Clerk, U.S. Bankruptcy Court:

\_\_\_\_\_  
\_\_\_\_\_

Any person wishing to object to any fee application, or the Final Report, must file a written objection within 20 days of the date of this notice, together with a request for a hearing, and serve a copy of both upon the trustee, any party whose application is being challenged, and the United States Trustee. If no objections are filed, the Court will act on the fee applications and the trustee may pay dividends pursuant to Fed. R. Bankr. P. 3009 without further order of the Court.

Dated: this \_\_\_\_ day of \_\_\_\_\_, \_\_\_\_.

By: \_\_\_\_\_  
Clerk of Court  
[Address]

*Trustee's name*  
*address*

## APPENDIX 2-10 Form 4, Instructions and Q's &amp; A's

## PART A

## SAMPLE FORM 4

12/20/99

## Distribution Report for Closed Asset Cases

Case No. 399-123456 Trustee Name: Jenny Ward  
Case Name: John L. & Sally B. Doe Date: \_\_\_\_\_

	<b>\$ AMOUNT RECEIVED</b>	<b>% OF RECEIPTS</b>
GROSS RECEIPTS	\$1,000,000.00	100.00%
Less:		
Funds Paid to Debtor		
Exemptions	3,400.00	0.34%
Excess Funds	0.00	0.00%
Non-Estate Funds Paid to 3 <sup>rd</sup> Parties	0.00	0.00%
<b>NET RECEIPTS</b>	<b>\$996,600.00</b>	<b>99.66%</b>
	<b>\$ CLAIMS</b>	<b>% OF RECEIPTS</b>
SECURED CLAIMS:	<b>PAID</b>	
Real Estate	\$400,000.00	40.00%
Personal Property & Intangibles	33,000.00	3.30%
Internal Revenue Service Tax Liens	0.00	0.00%
Other Governmental Tax Liens	3,000.00	0.30%
<b>TOTAL SECURED CLAIMS</b>	<b>\$436,000.00</b>	<b>43.60%</b>
PRIORITY CLAIMS:		
CHAPTER 7 ADMINISTRATIVE FEES § 507(a)(1) and CHARGES under Title 28, Chapter 123:		
Trustee Fees	47,330.00	4.73%
Trustee Expenses	2,000.00	0.20%
Legal Fees & Expenses:		
Trustee's Firm Legal Fees	0.00	0.00%
Trustee's Firm Legal Expenses	0.00	0.00%
Other Firm's Legal Fees	25,000.00	2.50%
Other Firm's Legal Expenses	1,500.00	0.15%
Accounting Fees and Expenses		
Trustee's Firm Accounting Fees	0.00	0.00%
Trustee's Firm Accounting Expenses	0.00	0.00%
Other Firm's Accounting Fees	4,000.00	0.40%
Other Firm's Accounting Expenses	0.00	0.00%
Real Estate Commissions	25,000.00	2.50%
Auctioneer/Liquidator Fees	20,000.00	2.00%
Auctioneer/Liquidator Expenses	10,000.00	1.00%
Other Professional Fees/Expenses	1,000.00	0.10%
Expenses of Operating Business in Chapter 7	0.00	0.00%
Other Expenses	5,700.00	0.57%
Income Taxes - Internal Revenue Service	5,000.00	0.50%
Other State or Local Taxes	0.00	0.00%

U.S. Trustee Fees	0.00	0.00	0.00%
Court Costs	800.00	800.00	0.08%
<b>TOTAL CHAPTER 7 ADMINISTRATIVE FEES &amp; CHARGES</b>	<b>\$147,330.00</b>	<b>\$147,330.00</b>	<b>14.73%</b>
<b>TOTAL PRIOR CHAPTER ADMINISTRATIVE FEES § 507(a)(1);</b> (From attached Part B)	0.00	0.00	0.00%
WAGES § 507(a)(3)	9,200.00	9,200.00	0.92%
CONTRIBUTIONS: EMPLOYEE BENEFIT PLANS § 507(a)(4)	900.00	1,900.00	0.09%
ALIMONY & CHILD SUPPORT § 507(a)(7)	4,600.00	4,600.00	0.46%
CLAIMS OF GOVERNMENTAL UNITS § 507(a)(8)	25,000.00	25,000.00	2.50%
OTHER § 507 (a)(2), (5), (6), & (9)	0.00	0.00	0.00%
<b>TOTAL PRIORITY CLAIMS</b>	<b>\$187,030.00</b>	<b>\$187,030.00</b>	<b>18.70%</b>
<b>GENERAL UNSECURED CLAIMS</b>	<b>\$1,200,000.00</b>	<b>\$373,570.00</b>	<b>37.36%</b>
<b>TOTAL DISBURSEMENTS</b>	<b>\$1,823,030.00</b>	<b>\$996,600.00</b>	<b>99.66%</b>

PART B

SAMPLE FORM 4

12/20/99

Distribution Report for Closed Asset Cases

Case No. 399-123456  
Case Name: John L. & Sally Doe

Trustee Name: Jenny Ward  
Date: \_\_\_\_\_

	<b>\$ CLAIMS</b>	<b>\$ AMOUNT PAID</b>	<b>% OF RECEIPTS</b>
<b>PRIOR CHAPTER ADMINISTRATIVE FEES § 507(a)(1)</b>			
Trustee Fees	\$0.00	\$0.00	0.00%
Trustee Expenses	0.00	0.00	0.00%
Legal Fees & Expenses:			
Trustee's Firm Legal Fees	0.00	0.00	0.00%
Trustee's Firm Legal Expenses	0.00	0.00	0.00%
Other Firm's Legal Fees	0.00	0.00	0.00%
Other Firm's Legal Expenses	0.00	0.00	0.00%
Accounting Fees and Expenses			
Trustee's Firm Accounting Fees	0.00	0.00	0.00%
Trustee's Firm Accounting Expenses	0.00	0.00	0.00%
Other Firm's Accounting Fees	0.00	0.00	0.00%
Other Firm's Accounting Expenses	0.00	0.00	0.00%
Real Estate Commissions	0.00	0.00	0.00%
Auctioneer/Liquidator Fees	0.00	0.00	0.00%
Auctioneer/Liquidator Expenses	0.00	0.00	0.00%
Other Professional Fees/Expenses	0.00	0.00	0.00%
Income Taxes - Internal Revenue Service	0.00	0.00	0.00%
Other State or Local Taxes	0.00	0.00	0.00%
Operating Expenses	0.00	0.00	0.00%
Other Expenses	0.00	0.00	0.00%
<b>TOTAL PRIOR CHAPTER ADMINISTRATIVE FEES</b>	<b>\$0.00</b>	<b>\$0.00</b>	<b>0.00%</b>

12/20/99

**INSTRUCTIONS REGARDING  
DISTRIBUTION REPORT FOR CLOSED ASSET CASES (FORM 4)  
(INCLUDING QUESTIONS & ANSWERS AT THE END)**

**GENERAL INSTRUCTIONS****CASES COVERED  
BY FORM 4**

Form 4 is required for chapter 7 cases filed or converted on or after 7/1/99. It is submitted with the final account or TDR. Form 4 should not be submitted for cases dismissed or converted to another chapter.

Commencing 4/1/2000, Form 4 must be filed electronically, unless the United States Trustee grants a waiver of this requirement.

**HEADER INFORMATION**

Enter the case number, case name, trustee name, and date. The date entered is the date Form 4 was prepared by the trustee.

**CLAIMS**

Allowed claims for which a distribution was made. Zeroes (0's) would be inserted under "Claims" and "\$ Amount Paid" for each claim category in which no amount was paid. (For example, if there is only sufficient funds to pay administrative and priority unsecured claims, the amount of each allowed administrative and priority unsecured claim would be shown under "Claims," and the amount of funds distributed on account of such claims would be shown under "\$ Amount Paid." Zeroes (0's) would be inserted under "Claims" and "\$ Amount Paid" for General Unsecured Claims.)

**% OF RECEIPTS**

The formula for this column is:

$$\frac{\text{\$ Amount Received" or "\$ Amount Paid" (whichever applies)}}{\text{Gross Receipts}}$$

All percentages under "% of Receipts" should be based on this formula. The percentages for totals and subtotals (e.g., Total Secured Claims) may not equal the sum of the individual component percentages, due to rounding.

**LINE-BY-LINE INSTRUCTIONS****PART A**

**GROSS RECEIPTS:** All funds received by trustee<sup>13</sup>, except for funds deposited to the estate in error and refunds of trustee overpayments (an example is a refund of excess bond premium which should be netted against the applicable expense line item).

Funds Paid to Debtor:

**Exemptions:** Funds disbursed to debtor(s) pursuant to exemptions permitted under Federal or State law.

**Excess Funds:** Funds disbursed to debtor(s), if any, after all other disbursements made.

Non-Estate Funds Paid to 3<sup>rd</sup> Parties:

Examples include payments to co-owners from sales of property in which a co-owner has an interest, escrow deposit refunds, PACA trust funds (Perishable Agricultural Commodities Act), and other similar trust funds.

**NET RECEIPTS:** The sum of gross receipts less funds paid to debtor and non-estate funds paid to 3<sup>rd</sup> parties. The amount of net receipts equals total disbursements, which may be the basis for computing the maximum trustee fee.

**SECURED CLAIMS<sup>14</sup>:**

**Real Estate:** Funds disbursed to all prepetition lien holders, except for tax liens.

**Personal Property & Intangibles:** Funds disbursed to all prepetition lien holders, except for tax liens.

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<sup>13</sup>In some instances (e.g. real estate sales), the trustee may receive a “net” check (i.e., the gross sales price less payments to secured creditors, real estate commissions, closing costs, etc.). The gross sales price is to be reported under Gross Receipts and the deductions are to be reported in the appropriate categories for the claims and the administrative expenses, as applicable.

<sup>14</sup>Secured claims do not include liens for administrative expenses for purposes of this form.



Internal Revenue Service  
Tax Liens:

Funds disbursed to all prepetition lien holders. (Do not include payment of tax claims which became due after petition date. Said tax payments should be included in Chapter 11 or Chapter 7 tax categories, depending on the date the taxes became due.)

Other Governmental  
Tax Liens:

Funds disbursed to all prepetition lien holders. (Do not include payment of tax claims which became due after petition date. Said tax payments should be included in Chapter 11 or Chapter 7 tax categories, depending on the date the taxes became due.)

**TOTAL SECURED CLAIMS:** The sum of total secured claims by column.

PRIORITY CLAIMS:

CHAPTER 7  
ADMINISTRATIVE FEES  
507(a)(1) and CHARGES  
under Title 28, Chapter 123:

Trustee Fees: Total fees paid to trustee pursuant to § 330(a).

Trustee Expenses: Total interim and final expense reimbursements paid directly to the trustee pursuant to § 330(a).

Legal Fees & Expenses:

Trustee’s Firm Legal  
Fees: All legal fees paid to trustee or trustee’s firm.

Trustee’s Firm Legal  
Expenses: All legal expenses paid to trustee or trustee’s firm.

Other Firm’s Legal  
Fees: All legal fees paid to other firms.

Other Firm’s Legal  
Expenses: All legal expenses paid to other firms.

Accounting Fees & Expenses:

Trustee’s Firm  
Accounting Fees: All accounting fees paid to trustee or trustee’s firm.

Trustee's Firm Accounting Expenses:	All accounting expenses paid to trustee or trustee's firm.
Other Firm's Accounting Fees:	All accounting fees paid to other firms.
Other Firm's Accounting Expenses:	All accounting expenses paid to other firms.
Real Estate Commissions:	All commissions and expenses paid to professionals for the sale of real property.
Auctioneer/Liquidator Fees:	All fees paid to auctioneer or liquidator of personal property.
Auctioneer/Liquidator Expenses:	All expenses paid to auctioneer or liquidator of personal property.
Other Professional Fees/ Expenses:	All other professional fees and expenses paid. (In order to be included in this category, fees and expenses must be paid only to professional employed pursuant to § 327 of the Code, and not be included in one of the other fee and expenses categories. For example, professional fees and expenses for appraisers and expert witnesses should be included in this category.)
Expenses of Operating Business in Chapter 7:	All costs of operating a business pursuant to Bankruptcy Court order, except professional fees and expenses specifically listed above. Includes payroll taxes paid in connection with operating a business in chapter 7.
Other Expenses:	All other allowed expenses not otherwise included under Trustee Expenses, including bond premiums and other costs paid directly by the estate, but not including taxes, court costs, and unpaid United States Trustee fees.
Income Taxes - Internal Revenue Service:	All income taxes which first become due to the IRS after the bankruptcy petition filing date.
Other State or Local Taxes:	Other state or local taxes which first become due after the bankruptcy petition filing date.
United States Trustee Fees:	All U.S. Trustee Chapter 11 fees paid by the trustee in chapter 7 proceeding.

Court Costs:	All costs paid by the trustee to the Bankruptcy Court, including noticing fees, filing fees, etc.
TOTAL CHAPTER 7 ADMINISTRATIVE FEES & CHARGES:	The sum of chapter 7 administrative fees and charges by column.
TOTAL PRIOR CHAPTER ADMINISTRATIVE FEES 507(a)(1):	See Part B below.
WAGES §507(a)(3):	Wages, salaries, or commissions, including vacation, severance, and sick leave pay earned by an individual. (See Code for specific requirements)
CONTRIBUTIONS: EMPLOYEE BENEFIT PLANS §507(a)(4):	Payments to an employee benefit plan. (See Code for specific requirements.)
ALIMONY & CHILD SUPPORT §507(a)(7):	Payments to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for, or support of such spouse or child. (See Code for specific requirements)
CLAIMS OF GOVERNMENTAL UNITS §507(a)(8):	Payments to governmental units, only to the extent that such claims are for – (a) a tax on or measured by income or gross receipts; (b) a property tax; (c) a tax required to be collected or withheld for which the debtor is liable; (d) an employment tax; (e) an excise tax; (f) a customs duty arising out of the importation of merchandise; or (g) a penalty related to a claim specified in §507(a)(8). (See Code for specific requirements.)
OTHER §507(a)(2), (5), (6), & (9):	(See Code)
<b>TOTAL PRIORITY CLAIMS:</b>	The sum of total priority claims by column.
<b>GENERAL UNSECURED CLAIMS:</b>	All unsecured claims paid.
<b>TOTAL DISBURSEMENTS:</b>	The sum of total secured, priority, and unsecured claims by column.

**PART B**

PRIOR CHAPTER  
ADMINISTRATIVE FEES  
§507(a)(1):

PART B (Prior Chapter Administrative) instructions are essentially the same as the PART A (Chapter 7 Administrative) instructions. Note that chapter 11 payroll taxes paid during the pendency of chapter 7 should be reported under “Operating Expenses” in Part B.

Set #1, 8/18/99  
Updated, 12/2/99

**DISTRIBUTION REPORT FOR CLOSED ASSET CASES (FORM 4)  
QUESTIONS AND ANSWERS**

- 1) Where should the chapter 11 payroll taxes (e.g., 941 taxes) paid during the pendency of chapter 7 appear on the Form 4 for a converted case?**

These payroll taxes should be reported under “Operating Expenses” in the section titled “Prior Chapter Administrative Fees.”

- 2) What about payroll taxes paid in connection with an operating chapter 7 case?**

If payroll taxes are paid in connection with operating a business in chapter 7, the taxes should be reported under “Expenses of Operating Business in Chapter 7.”

- 3) An attorney is alleging a claim on all funds pursuant to an attorney’s charging lien. If the attorney is successful, he will never have formally filed a claim and yet will have funds disbursed to him. How is this situation reported on Form 4?**

The distribution to the attorney should be reported as though the attorney had filed a claim. The amount allowed is included under “Claims” and the amount distributed is included under “\$ Amount Paid.”

- 4) Which date should be inserted in the Form 4 header?**

The date prepared by the trustee.

- 5) Where should the trustee report the interest paid to each type of claim as provided in § 726(a)(5).**

The amounts reported under “\$ Amount Paid” should include any interest paid to the creditor.

- 6) Would a § 506(c) expense allowed to a trustee fall under “Other Expenses”?**

Not necessarily. The fact that a creditor reimburses the expense does not make any difference. A § 506(c) expense should be categorized the same as any other expense on

Form 4. This may be “Other Expenses” much of the time, but if the expense is for professionals, it should be classified under the appropriate category.

**7) What is the difference between “Trustee Expenses” and “Other Expenses”?**

“Trustee Expenses” consists of expenses originally incurred out-of-pocket by the trustee for which the trustee received reimbursement under § 330(a).

“Other Expenses” covers allowed expenses not otherwise included in the other categories on Form 4. It includes the cost of storage, insurance, locks, etc., paid directly to the provider by the estate. It specifically excludes fees and expenses paid to the trustee pursuant to § 330(a), attorney and professional fees and expenses, expenses of operating a business in a chapter 7 case, taxes, court costs, and United States Trustee fees.

Set #2, 12/2/99

**DISTRIBUTION REPORT FOR CLOSED ASSET CASES (FORM 4)  
QUESTIONS AND ANSWERS**

- 8) **With respect to sales of real estate and other transactions where a “net” check is remitted to the trustee, how are the gross receipts and deductions (e.g., constructive disbursements) to be reported on Form 4?**

The gross proceeds from the sale (e.g., real estate sale, auction) are to be reported under Gross Receipts, regardless of the amount actually remitted to the trustee. The deductions (e.g., payments to secured creditors, commissions, closing costs) are to be reported in the applicable claims or administrative expense categories. See page 1 of the Form 4 Instructions.

- 9) **With respect to submission of the electronic Form 4, we understand that trustees will be able to submit the data files on diskette or by e-mail. Does there need to be a separate data file for each Form 4, or may the trustee combine several Form 4s in a single data file? (Since trustees sometimes submit Trustee Distribution Reports (TDRs) in batches, it would be helpful if a single data file could contain the Form 4 that goes with each TDR included in the batch.)**

The Program will be able to handle either situation. Trustees have the choice of submitting a separate electronic file for each Form 4, or they may include several Form 4s in one electronic file.

- 10) **The sample Form 4 does not show the dollar amounts with cents (e.g., 1.23). However, the electronic Form 4 specifications require that each dollar data field be reported to two decimal places. Please clarify this apparent inconsistency.**

The sample Form 4 was for illustrative purposes. Effective January 1, 2000, the dollar amounts on both the hard copy and electronic versions of Form 4 must include the cents, so that the amounts exactly match the TDR amounts.

- 11) **Please provide further clarification in regard to Q and A #5. In many jurisdictions, it appears to be an accepted and prevalent practice to treat interest separately from the claim itself. In this situation, the software vendor plans to tell its customers to treat all interest paid as unsecured interest reportable under “General Unsecured Claims.” Otherwise, it would cause a serious programming problem because the software cannot categorize interest one way for the courts and another way for Form 4. Is this vendor’s plan acceptable?**

Yes. Both reporting methods are acceptable, pending further review by the Chapter 7 Subcommittee.

- 12) **Please clarify how the trustee’s name must appear in the electronically transmitted Form 4.**

Field #5 (Last Name) Field #6 (First Initial, with period) BOTH UPPERCASE  
 WARD J.

- 13) **Please clarify how the Version Number must appear in the electronically transmitted Form 4.**

Field #1 (Version) This is a text field, with a length of 3 spaces. The version number is a left-justified single digit.  
 1

- 14) **Please indicate where the following types of distributions would be reported on Form 4:**

<u>Question</u>	<u>Answer</u>
<b>Accountant for the Debtor</b>	Ch. 7 Admin: Other Professional Fees/Expenses
<b>Chapter 11 Wage Claims</b>	Prior Ch. Admin: Operating Expenses
<b>Subordinated General Unsecured &amp; Late Filed Claims</b>	General Unsecured Claims
<b>Chapter 7 Wage Claims</b>	Wages 507(a)(3) if prepetition wages Expenses of Operating Business in Chapter 7 if postpetition wages

- 15) **Please define the term “liquidator.” Is a liquidator a professional?**

The liquidator is a professional who may be hired to settle the affairs of a business by selling its assets to pay creditors. These professionals may advertise their services as “auctioneers/liquidators.” In a bankruptcy case, the liquidator essentially performs the same functions as an auctioneer and should be treated as such for purposes of reporting the chapter 7 distribution statistics.



**16) Is an “agent” or “administrative assistant” hired by the trustee to sell an asset a “liquidator?”**

Such a person could be a liquidator. It depends on the tasks assigned. If the person is an employee of the trustee’s office, full or part-time, payment for duties performed which are not overhead will be a trustee expense and, if allowed, reimbursed to the trustee. If the agent or administrative assistant is hired pursuant to court order and will be paid pursuant to court order from assets of the estate, such payments should be recorded as “Other Expenses,” unless the person falls within the definition of professional or liquidator (as described in Q and A #15). In those instances, the payment will be recorded in the appropriate specific category.

**17) Where should real property taxes be reported?**

Prepetition real property tax claims are reported under “Secured Claims: Other Governmental Tax Liens.” Postpetition real property taxes are reported under “Ch. 7 Admin.: Other State or Local Taxes.”

**APPENDIX 2-11 Sample Surety Bond Form***June 16, 1998 draft***BANKRUPTCY DEPOSITORY BOND IN FAVOR OF THE UNITED STATES  
(11 U.S.C. § 345)**

Bond #: \_\_\_\_\_

KNOW ALL MEN BY THESE PRESENTS:

That we, \_\_\_\_\_ (the "Principal"), with its principal office at \_\_\_\_\_, which acts as a depository bank for certain funds of bankruptcy estates administered under chapters 7, 11, 12, or 13 of title 11 of the United States Code (the "Bankruptcy Code") in the United States District Court for the \_\_\_\_\_ District of \_\_\_\_\_, including the United States Bankruptcy Court for said district (collectively, the "Court"), as Principal, *and* \_\_\_\_\_ (the "Surety"), with its principal office at \_\_\_\_\_, and duly authorized to transact business in the state of \_\_\_\_\_, as Surety, are held and firmly bound, in conformity with 11 U.S.C. § 345, unto the United States of America in the aggregate penal sum of \_\_\_\_\_ Dollars No/100-dollars (\$ \_\_\_\_\_), for the payment of which, well and truly to be made, we bind ourselves, our heirs, executors, successors, assigns, and our administrators, jointly and severally, by these presents.

THE CONDITION OF THIS OBLIGATION IS SUCH THAT:

WHEREAS, certain persons serve as trustees in cases arising under chapters 7, 11, 12, or 13 of the Bankruptcy Code (the "Trustees"), and certain persons remain in control of estates in certain reorganization cases under chapter 11 of the Bankruptcy Code (the "Debtors-in-Possession"); and

WHEREAS, certain Trustees and/or Debtors-in-Possession have asked the Principal to act as a depository for certain monies belonging to the bankruptcy estates being administered in the cases pending before the Court; and

WHEREAS, the Principal and the Surety must comply with 11 U.S.C. § 345;

NOW THEREFORE, the condition of the above obligation is such that if the Principal shall faithfully account for and repay all monies deposited with the Principal, as a depository for monies belonging to the bankruptcy estates being administered by the Trustees and Debtors-in-Possession in bankruptcy cases pending before the Court, and if the Principal also shall faithfully fulfill all of its obligations under 11 U.S.C. § 345, then this obligation shall be null and void; otherwise it shall remain in full force and effect, subject to the following conditions:

- 1. In the event of the failure of the Principal to satisfy the conditions above during the period of this bond ("Default"), the United States Trustee, on behalf of the United States of America, shall make reasonable efforts to provide written notice to the Surety to:

Attention: \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_

Failure to provide notice shall not constitute a waiver of the United States' rights or the rights of those on whose behalf the United States may be acting.

- 2. The Surety need not make payment under this bond on that portion of any deposit held by the Principal that is paid by the Federal Deposit Insurance Corporation as a deposit pursuant to title 12 of the United States Code.

- 3. The Surety may cancel this bond at any time by giving ninety (90) days notice in writing by registered mail to the United States to:

United States Trustee  
 Region \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_  
 \_\_\_\_\_

In the event such notice is sent, the Surety's liability under this bond shall terminate at the expiration of ninety (90) days from the date of receipt of such notice, but such termination shall not relieve the Surety of liability for Defaults arising prior to the effective date of such cancellation.

The Principal and the Surety agree that they shall not amend, modify, or vary any term of this bond, including, but not limited to, the amount of the penal sum, without the prior written consent of the United States Trustee for Region \_\_.

The Surety hereby represents and warrants that it is an acceptable Surety under, and is in full compliance with, sections 9304 and 9308 of title 31 of the United States Code and Treasury Department Circular 570. Surety hereby binds itself to notify the United States Trustee for Region \_\_ immediately if, for any reason, it should cease being in full compliance with either section 9304 or 9308 of title 31 of the United States Code or with Treasury Department Circular 570.

Signed, Sealed and Dated this \_\_ of \_\_\_\_, \_\_\_\_.

By: \_\_\_\_\_

By: \_\_\_\_\_

President **[of the Principal]** Attorney-In-Fact **[of the Surety]**

**APPENDIX 2-12 Sample Blanket Bond Form**

UNITED STATES BANKRUPTCY COURT  
DISTRICT[S] OF \_\_\_\_\_

\_\_\_\_\_ BLANKET BOND  
OF PANEL TRUSTEES/INTERIM TRUSTEES IN CHAPTER 7 CASES

**POLICY No. 000-00-0001**

KNOW ALL MEN BY THESE PRESENTS: That individually, we the Principals listed in Endorsement "A" attached hereto, and those who may from time to time be added to said endorsement, by amendment, and \_\_\_\_\_ Insurance Company of \_\_\_\_\_, incorporated in the state of \_\_\_\_\_, as Surety, are held and firmly bound unto the United States of America in the amounts stated in said schedule as to each named principal, in lawful money of the United States, to be paid to the United States, for which payment, well and truly to be made, we bind ourselves and our heirs, executors, administrators and successors by these presents. Provided, however, that each Trustee shall be liable only for his or her individual responsibilities as Trustee.

THE CONDITION OF THIS OBLIGATION IS SUCH THAT:

WHEREAS, the United States Trustee for Region \_\_, has appointed or will appoint Trustees in cases commenced under Chapter 7, Title 11, United States Code; and

WHEREAS, the said Principals listed in Endorsement "A" attached or subsequently added thereto by amendment may hereafter be appointed to serve as such Trustee in one or more such cases;

NOW, THEREFORE, if the said Principals listed in Endorsement "A" attached or subsequently added thereto as Trustee as aforesaid shall obey such orders as the United States Bankruptcy Court or any other court of competent jurisdiction may make in relation to the trust undertaken by said Trustee, and shall faithfully and truly account for all moneys, assets and effects of each estate created by the commencement of each case in which he has been appointed or will be appointed, and shall in all respects faithfully perform all his official duties as Trustee, then this obligation to be void; otherwise, to remain in full force and effect.

The liability of the Surety hereunder shall not exceed the amount stated in said Endorsement "A" for any one case as to each named principal, or the aggregate amount stated in said Endorsement "A" as to each named principal for all cases on which claims are asserted as to each named Principal regardless of the number of years this bond is in effect and regardless of the number of cases involved.

This bond shall remain in full force and effect with respect to all cases pending in Region \_\_\_\_, in which the said Principals listed in Endorsement "A" attached or subsequently added thereto have been appointed, until the Surety has terminated further liability after 120 days written notice served to the United States Trustee and the Clerk of the United States Bankruptcy Court of the District of \_\_\_\_\_, or until released by the United States Trustee for Region \_\_\_\_. The surety further agrees that a 120-day written notice will be served on the United States Trustee and the Clerk of the United States Bankruptcy Court of the District of \_\_\_\_\_ prior to any change in rating or change in coverage endorsements.

SIGNED AND SEALED this \_\_ day of \_\_\_\_\_, 20\_\_.

Witness or attest:

\_\_\_\_\_ INSURANCE COMPANY

\_\_\_\_\_

By: \_\_\_\_\_

ACCEPTED:

UNITED STATES TRUSTEE

By:

**ENDORSEMENT "A"**  
**OF THE BLANKET BOND**  
**OF PANEL TRUSTEES/INTERIM TRUSTEES IN CHAPTER 7 CASES**

This Endorsement "A" is attached and made a part of Blanket Trustee's Bond No. BIS 000-00-0001 dated the \_\_ day of \_\_\_\_\_, 20\_\_, as submitted to the United States Trustee and filed with the Clerk of the United States Bankruptcy Court of the District of \_\_\_\_\_.

Principal	Limit Per Case	Aggregate Limit
Trustee A	\$750,000	\$5,000,000
Trustee B	\$750,000	\$5,000,000
Trustee C	\$750,000	\$5,000,000
Trustee D	\$750,000	\$5,000,000
Trustee E	\$750,000	\$5,000,000

Witness or attest:

\_\_\_\_\_

\_\_\_\_\_ INSURANCE COMPANY

By: \_\_\_\_\_

ACCEPTED:

UNITED STATES TRUSTEE

By:

Power of Attorney

INSURANCE COMPANY

KNOW ALL MEN BY THESE PRESENTS: That the Insurance Company, a corporation of the State of, by, Vice President, and, Assistant Secretary, in pursuance of authority granted by Article, Section, of the By-Laws of said Company, which are set forth on the reverse side hereof and are hereby certified to be in full force and effect on the date hereof, does hereby nominate, constitute and appoint

its true and lawful agent and Attorney-in-Fact, to make, execute, seal, and deliver, for, and on its behalf as surety, and as its act and deed: any and all bonds and undertakings. And the execution of such bonds or undertakings in pursuance of these presents, shall be as binding upon said Company, as fully and amply, to all intents and purposes, as if they had been duly executed and acknowledged by the regularly elected officers of the Company at its office in, in their own proper persons.

The said Assistant Secretary does hereby certify that the extract set forth on the reverse side hereof is a true copy of Article, Section, of the By-Laws of said Company, and is now in force.

IN WITNESS WHEREOF, the said Vice President and Assistant Secretary have hereunto subscribed their names and affixed the Corporate Seal of the said Insurance Company, this day of, 20.

Assistant Secretary Vice President [SEAL]

On this day of, 20, before the subscriber, a Notary Public of the State of, in and for the City of, duly commissioned and qualified, came the above-named Vice President and Assistant Secretary of the Insurance Company, to me personally known to be the individuals and officers described in and who executed the preceding instrument, and they each acknowledged the execution of the same, and being by me duly sworn, severally and each for himself depose and saith, that they are the said officers of the Company aforesaid, and that the seal affixed to the preceding instrument is the Corporate Seal of said Company, and that the said Corporate Seal and their signatures as such officers were duly affixed and subscribed to the said instrument by the authority and direction of the said Corporation.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed my Official Seal, at the City of, the day and year first above written.

Notary Public Commission Expires

CERTIFICATE

I, the undersigned, Assistant Secretary of the Insurance Company, do hereby certify that the original Power of Attorney of which the foregoing is a full, true, and correct copy, is in full force and effect on the date of this certificate; and I do further certify that the Vice President who executed the said Power of Attorney was one of the additional Vice Presidents specially authorized by the Board of Directors to appoint any Attorney-in-Fact as provided in Article, Section, of the By-Laws of the Insurance Company.

This Certificate may be signed by facsimile under and by authority of the following resolution of the Board of Directors of the \_\_\_\_\_ Insurance Company at a meeting duly called and held on the \_\_\_ day of \_\_\_\_\_, 20\_\_.

RESOLVED: "That the facsimile or mechanically reproduced signature of any Assistant Secretary of the Company, whether made heretofore or hereafter, wherever appearing upon a certified copy of any power of attorney issued by the Company, shall be valid and binding upon the Company with the same force and effect as though manually affixed."

IN TESTIMONY WHEREOF: I have hereunto subscribed my name and affixed the corporate seal of said Company, this \_\_\_ day of \_\_\_\_\_, 2000.

\_\_\_\_\_  
*Assistant Secretary*

*(on reverse)*

EXTRACT FROM BY-LAWS OF \_\_\_\_\_ INSURANCE COMPANY

"Article \_\_, Section \_\_, The Chairman of the Board, or the President, or any Executive Vice President, or any of the Senior Vice Presidents or Vice Presidents specially authorized to do so by the Board of Directors or by the Executive Committee, shall have power, by and with the concurrence of the Secretary or any one of the Assistant Secretaries, to appoint Resident Vice Presidents, Assistant Vice Presidents and Attorneys-in-Fact as the business of the Company may require, or to authorize any person or persons to execute on behalf of the Company any bonds, undertakings, recognizances, stipulations, policies, contracts, agreements, deeds, and releases and assignments of judgements, decrees, mortgages and instruments in the nature of mortgages....and to affix the seal of the Company thereto."



## APPENDIX 2-13 Chapter 7 Consequential Deficiencies

The United States Trustee Program's list of consequential deficiencies includes, but is not limited to:

### Banking

1. Commingled funds\*
2. Unauthorized depository
3. Missing bank statements\*
4. Missing cancelled checks\*
5. Estate funds not invested when appropriate
6. Inability to perform an accounting "proof of cash"\*
7. Improper or unauthorized bank account transfers or unexplained transactions on bank statements\*
8. Incomplete or missing bank reconciliations\*

### Receipts

1. Incoming checks not restrictively endorsed immediately upon receipt
2. Daily receipts log not maintained
3. Untimely deposits\*
4. Receipts not deposited\*
5. Sales/liquidations without notice or court order
6. No supporting documentation for receipts\*

### Recordkeeping

1. Non-existent reports\*
2. Liquidation or abandonment omitted from Form 1
3. Asset omitted from Form 1
4. Transaction (receipt, disbursement) omitted from Form 2
5. Inaccurate payees/payers, transactions descriptions, or amounts on Form 2

### ADP System

1. Passwords not utilized or changed at least annually
2. ADP system not adequately protected from damage, unauthorized access, or tampering
3. No routine back up procedures

### Disbursements

1. Disbursements without court authorization
2. No supporting documentation\*
3. Checks not properly pre-numbered
4. Blank checks not adequately controlled\*
5. Disbursements by counter check or money order\*
6. Unauthorized disbursements by cashier's check or wire transfer\*
7. Checks not personally signed by trustee\*
8. Blank checks presigned by trustee prior to use\*
9. Checks altered or contain unusual endorsement\*
10. Checks not written to specific payee (i.e., payable to cash or bearer)

### Asset Administration

1. Scheduled and unscheduled assets not properly tracked on Form 1
2. Assets not timely investigated to determine value to estate
3. Estate assets not promptly inventoried, secured, or collected
4. Untimely asset liquidations
5. Trustee cannot account for all assets\*
6. Trustee does not adequately supervise auctioneer, liquidator, collection agent, attorney, or other person hired to collect or liquidate assets\*
7. Assets sold to insiders or related parties\*

### Other Internal Controls

1. Trustee does not adequately supervise employees\*
2. Estate files significantly disorganized
3. Missing files\*

\* For these deficiencies, follow-up office visits are required to verify implementation of corrective actions, unless the deficiency is a single isolated instance (e.g., missing bank statement).

**APPENDIX 2-14 Record Retention Schedule for Chapter 7 Trustee Oversight Files**

Type of File	File Disposition	File Destruction
<p><u>Trustee Oversight Files:</u></p> <p>1) Active Trustees</p> <p>2) Trustees No Longer Receiving Cases</p>	<p>Files are retained in the local United States Trustee office for 5 years. After 5 years, the United States Trustee may either scan the files or retire them to the Federal Archives Records Center (FARC).</p> <p>a. Trustees who are not receiving new case assignments, but still administer cases: follow the procedures for active trustees.</p> <p>b. Trustees who voluntarily resign or retire: their files may be scanned or retired to the FARC two years after closure of all cases.</p> <p>c. Deceased trustees: the records may be destroyed one year from the date of death.</p>	<p>If the records are scanned after 5 years, the United States Trustee may destroy the originals at that time. If the files are retired to the FARC, they will be destroyed after 5 years.</p> <p>a. Follow the procedures for active trustees.</p> <p>b. Follow the procedures for active trustees.</p> <p>c. The FARC may be instructed to destroy the archived files one year after the date of death.</p>
<p><i>Note: As further discussed in USTM 2-3.18 and Appendix 2-4, a trustee has the right to timely appeal a United States Trustee's decision to suspend or permanently terminate the assignment of cases under 28 C.F.R. § 58.6. If the appeal is denied by the Director and the trustee sues, the United States Trustee should retain all of the records which support the suspension/termination decision for one year after the litigation is concluded.</i></p>		
<p><u>180-Day Reports</u> (UST Manual 6-24)</p>	<p>Individual file folders are created for each trustee and contain the two most recent 180-day reports, including all supporting documentation and correspondence. Files beyond the two most recent reports should be retired to the FARC, at least annually or upon accumulation of one cubic foot.</p>	<p>The FARC will destroy the reports after 5 years.</p>
<p><u>§341(a) Meeting/Trustee Files:</u> These files contain calendars, rotations, exceptions to rotations, and reassignments. (UST Manual 6-24)</p>	<p>These files are not retired to the FARC.</p>	<p>Internal administration records and calendars, schedules, logs, etc., should be destroyed after two years where substantive information is involved, or if the records contain no substantive information, when no longer needed.</p>
<p><u>§341(a) Meeting Tapes</u> (UST Manual 6-24)</p>	<p>Tapes are retained for two years from the date of the §341(a) meeting or for a longer period if deemed necessary by the United States Trustee. A tape recording needed for further use, i.e., criminal proceedings, is to be officially transcribed and made part of the relevant case file and the tape is to be retained during the pendency of the referral. See UST Manual 6-24 for details.</p>	<p>After the two-year retention period, or later (when the United States Trustee determines that the basis for retention no longer exists), the tape may be erased or destroyed. Tapes of poor quality that cannot be reused may be discarded after the retention period.</p>