

U.S. Trustee Panel: Inside Perspective

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**STATEMENT OF THE U.S. TRUSTEE PROGRAM'S POSITION ON LEGAL ISSUES
ARISING UNDER THE CHAPTER 7 MEANS TEST**

Following is a line-by-line summary of Form 22A and various recurring disposable income issues likely to arise in chapter 7 under the BAPCPA provisions of 11 U.S.C. § 707(b). The summary gives the position of the United States Trustee Program (USTP) on these issues. For ease of reference, the USTP positions are listed in summary fashion without citation to legal authority. The referenced lines are those on the Form 22A. Unless a circuit court has decided an issue to the contrary, United States Trustees should, absent unusual circumstances, maintain these positions when interpreting section 707(b).

Line 1A, Declaration of Disabled Veterans

- Must have at least 30% disability from service or released/discharged due to disability.
- Debt primarily incurred during period of active duty/homeland defense activity.
- Only if BOTH conditions apply is debtor exempt from further completing Form 22A.

Line 1B, Declaration of Non-Consumer Debts

- Less than 50% of total scheduled debt was incurred for personal, household or family purposes.
- Purpose of debt is judged at the time the debt was incurred.
- Home mortgages are typically consumer debt.
- Most tax debts are not typically consumer debt.

Line 1C, Declaration of Reservists and National Guard Exclusion

- Must be either a member of a reserve component or National Guard; AND
- Must have been on active duty or performing a homeland defense activity for at least
- 90 days.
- Exclusion applies after the minimum 90 day period of service, and for 540 days after the service ends.
- Exclusion applies only to cases filed between December 19, 2008 and December 18, 2011, unless extended by Congress.

Line 2, Filing Status

- The only four options permitted are those listed on the Form 22A.
- No option for legally separated but filing joint case; joint cases generally should be treated as a single household for means test purposes.
 - May be asserted as special circumstances to rebut the presumption of abuse under section 707(b)(2)(B).
 - May be considered by the UST when stating the reasons under section 704(b)(2) that a motion to dismiss is not appropriate.
 - Information should be consistent with household size on Schedule 1.

Line 3, Gross wages, salary, tips, bonuses, overtime, commissions.

- Includes pay/shift differentials.
- Includes income, whether or not taxable.
- Figures are gross amounts, before any deductions.

Lines 4 & 5, Business and real property income and expenses.

- Must be "ordinary and necessary," i.e., a reasonable operating expense.
- Depreciation is not included.
- Line "c" cannot be a negative number.

Line 6, Interest, dividends, and royalties.

- Includes automatic dividend reinvestment program.

Line 7, Pension and retirement income.

- Does not include Social Security payments.
- Includes all other retirement, including government, 401(k), and IRA.

Line 8, Any amounts paid by another person or entity, on a regular basis, for the household expenses of the debtor or the debtor's dependents, including child or spousal support.

- Includes payments made monthly, quarterly, or annually.
- Includes payments regardless of written agreement with contributor.
- Includes payments from roommate, partner, parent, or relative, regardless of whether living with debtor.
- Includes payments made directly to creditors on behalf of debtor, e.g., rent, car, or insurance.
- Does not include payments from non-filing spouse (which are already included as income in Column B).

Line 9, Unemployment compensation.

- Unemployment compensation is not a "benefit under SSA" and should be included; USTP opposes any entry in the boxes to the left of Columns A and B.

Line 10, Income from all other sources.

- Includes net gambling, cash gifts, litigation proceeds, and trust income.
- Includes private disability income.
- Does not include SSA benefits.
- Does not include tax refunds.
- Does not include loan proceeds.
- Whether it meets IRS test for income could be relevant, but whether it is taxable income or non-taxable income is not a factor.

Line 14, Applicable median family income.

- "Applicable state" is state of residence at filing.
- If married and two different households, residence is where most family members reside.
- If no plurality of family members are in anyone state, use state of spouse with highest income.
- "Household size" is the debtor, debtor's spouse, and any dependents that the debtor could claim under IRS dependency tests. The USTP uses the same IRS test for the definition of both "household" and "family." IRS Publication 501 explains the IRS tests for "dependent."
- The USTP departs from the IRS dependent test (as does the IRS when it determines family size for collection purposes) in cases justifying "reasonable exceptions" (e.g. a long standing economic unit of unmarried individuals and their children). However, if an individual is counted as a family member for median income purposes, that individual's income should be included as income on Part II of Form 22A.

Line 17, Marital adjustment.

- All income of the non-debtor spouse should be included, except the following expenses of the non-debtor spouse may be excluded:
 - withholding taxes;
 - student loan payments;
 - prior support obligations;
 - debt payments on which only the non-filing spouse is legally liable and where the consideration for the loan exclusively benefits the non-filing spouse. (Credit cards used to pay for household expenses may not be deducted on Line 17).

Line 19A, National Standards: food, apparel and services, housekeeping supplies, personal care, and miscellaneous.

- The following expenses are covered by the National Standards and may not be counted separately elsewhere:
 - apparel and services (includes shoes and clothing, laundry and dry cleaning, and shoe repair);
 - meals at home or away (unless unreimbursed business expenses);
 - housekeeping supplies (includes laundry and cleaning supplies; other household products such as cleaning and toilet tissue, paper towels and napkins; lawn and garden supplies; postage and stationary; and other miscellaneous household supplies);
 - personal care products and services (includes hair care products, haircuts and beautician services, oral hygiene products and articles, shaving needs, cosmetics, perfume, bath preparations, deodorants, feminine hygiene products, electric personal care appliances, personal care services, and repair of personal care appliances)
 - miscellaneous personal expenses.
- National Standard amount that may be claimed is based on the debtor, the debtor's dependents, and the debtor's spouse in a joint case if the spouse is not otherwise a dependent.

Line 19B, National Standards: health care.

- National Standard amounts may be claimed based on debtor, debtor's dependents, debtor's spouse, and the age of household members.
- Actual mounts expended by the debtor exceeding the National Standards that are required for the health and welfare of the debtor, debtor's dependents, and debtor's spouse, which are not reimbursed by insurance or paid by a health savings account, may be claimed on line 31.

Line 20A, Local Standards: housing and utilities; non-mortgage expenses.

- Based on county of residence; see line 14 for resolving multiple residences.
- The following expenses are covered by the Local Standards and may not be counted elsewhere:
 - maintenance and repair;
 - homeowner association dues;
 - condominium fees;
 - gas, electricity, water, heating oil, bottled gas, trash and garbage collection, wood and other fuels, septic cleaning;
 - basic telephone and cell phone service.

Line 20B, Local Standards: housing and utilities, mortgage/rent expense.

- Based on county of residence; see line 14 for resolving multiple residences.
- The following are included in the Local Standard and may not be counted elsewhere, except as provided on lines 42 and 43:
 - principal and interest on mortgage loan;
 - rent;
 - homeowners/renters insurance;
 - local property taxes.
- Line 20B(b) is the same figure as line 42 for house payments.
- Debtor may not "double dip," that is take the full amount of the Local Standard for mortgage/rent on line 20B(a) and then fail to deduct the monthly mortgage payment on line 20B(b). The overall effect of disallowing double-dipping is to allow the debtor to take only the higher of the actual mortgage payment or the Local Standard.
- If the home is being surrendered, the debtor may not include the mortgage payment on lines 42 and 43, and may not deduct the mortgage payment on line 20B(b). The debtor may, however, claim the full amount of the Local Standard for housing on line 20A.
- Debtors and joint debtors are entitled to only one Local Standard mortgage/rent payment, even if maintaining two separate households.
- Vacation homes do not entitle a debtor to the Local Standard on line 20B.
- Debtor may not claim a Local Standard on line 20B when the debtor:
 - is and has been living with a friend or relative for an extended period of time at no cost;
 - is and has been living in military or other employer-paid housing.

Line 21, Local Standards: housing and utilities; adjustment.

- This line is often used improperly by debtors to claim housing expenses in excess of the IRS standards; USTP policy is to object to that use of line 21.
- This line is occasionally used by debtors who claim that Form 22A incorrectly captures the separation of the IRS housing Local Standard into two components, a mortgage component and a non-mortgage component; the USTP will object to that use of line 21.

Line 22A, Local Standards: transportation, vehicle operation/public transportation expense.

- Based on metro area or region.
- See line 14 to resolve multiple residences.
- The Local Standard for vehicle operation may be taken when the debtor owns, leases, or pays the operating expenses on a vehicle.
- The Local Standard for vehicle operation for zero vehicles may be taken if the debtor does not own, operate, or pay operating expenses on any vehicle.
- A vehicle must be "street ready" and licensable.

- A vehicle designed without an engine does not qualify, e.g., camper or trailer.
- Debtors located outside of the Fifth, Seventh, and Eighth Circuits who operate vehicles not subject to a loan or lease may deduct an additional \$200 if the vehicle is owned by the debtor, and is older than six (6) model years or has more than 75,000 miles.

Line 22B, Local Standards: transportation, additional public transportation expense.

- If debtor claims vehicle operating expense for one or more vehicles on Line 22A, debtor may only claim additional public transportation expense if reasonable and necessary for the health and welfare of the debtor, debtor's dependents, and debtor's spouse, or for the production of income.
- If additional public transportation expense is applicable, it is capped by Local Standard amount for public transportation.

Lines 23 & 24, Local Standards: transportation ownership/lease expenses.

- Outside the Fifth, Seventh, and Eighth circuits, debtor cannot claim the vehicle ownership expense if the debtor does not have a secured loan or a lease on the vehicle.
- In the Fifth, Seventh, and Eighth circuits debtor may claim this expense if the debtor owns a vehicle regardless of whether the debtor has a loan or lease payment. However, if the debtor owns a vehicle free and clear the USTP position is that the lack of any actual ownership expense may be considered in determining whether the case constitutes an abuse under the totality of the debtor's financial circumstances pursuant to section 707(b)(3)(B).
- If the vehicle is being surrendered without replacement, the debtor may not claim the expense. *But see* discussion regarding line 42.
- If the vehicle is borrowed, the debtor may not claim the expense.
- Debtor may not "double dip," that is take the full amount of the vehicle ownership expense on line 23(a) and then fail to deduct the monthly lien payment on line 23(b). The overall effect is to allow the debtor to take the higher of the actual loan or lease payment and vehicle ownership expense.
- A debtor whose household contains a single driver is generally entitled to an ownership expense for only one vehicle.

Line 25, Other Necessary Expenses: taxes.

- Based on monthly amount of actual taxes owed, not taxes withheld.
- Includes FICA, Social Security, Medicare, state and local taxes.
- Non-debtor spouse's taxes is not included if "backed out" on line 17.

Line 26, Other Necessary Expenses: involuntary deductions for employment.

- Includes retirement, union dues, uniform costs, work shoes.

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- Does not include voluntary 401(k) contributions, voluntary 401(k) loan repayments, or other voluntary retirement or profit sharing deductions.
- Does not include United Way or charitable contributions.
- Does not include elective insurance.

Line 27, Other Necessary Expenses: life insurance.

- Includes only amounts for term insurance on the debtor's life.
- If the policy is whole life, debtor must determine what portion of the premium is attributable to term coverage.
- Does not include premiums on policies for non-debtor spouse or children.

Line 28, Other Necessary Expenses: court-ordered payments.

- Includes the current monthly amount of support and alimony, not any past due amounts, which are entered on line 44.
- Does not include purely voluntary amounts for which there is no legal obligation.

Line 29, Other Necessary Expenses: education for employment or for a physically or mentally challenged child.

- Employment education must be as a condition of employment.
- Expenses for challenged children must be for "health or welfare."
- Expenses for challenged children cannot be otherwise provided by public school system.
- Expenses for challenged children cannot be already included on line 30 or 38.

Line 30, Other Necessary Expenses: childcare.

- These are actual expenses only.
- Includes babysitting, nursery school, daycare, preschool.
- Premium daycare may be permitted, depending on the justification.
- May not be permitted if one parent is "stay at home;" depends on the circumstances.

Line 31, Other Necessary Expenses: health care.

- Includes only unreimbursed, out-of-pocket expenses, exceeding the National Standard amounts provided for at line 19B, including items traditionally reimbursable through a flexible spending or "cafeteria" medical saving plan. For example:
 - deductibles
 - medications
 - therapy
 - co-pays
- Does not include payments for health insurance or health savings account; those are covered by line 34.

- Does not include elective or cosmetic surgery.
- May not duplicate items on line 34.

Line 32, Other Necessary Expenses: telecommunication services.

- Does not include basic phone or cell service, which is included in the Local Standards on line 20A.
- Pagers, call waiting, long distance, caller ID, and internet may be included, depending on amount and circumstance; test is whether "necessary for health and welfare or production of income."
- Does not include business expenses already deducted on line 4b or 5b.

Line 34, Health Insurance, Disability Insurance, and Health Savings Account Expenses.

- Includes actual expense for debtor, spouse, and dependents.
- Does not include flexible spending account or "cafeteria" medical saving plan contributions, which should be deducted as excess costs on line 31 to the extent they exceed to line 19B IRS standard amounts.

Line 35, Continued contributions to the care of household or family members.

- Includes only actual, not anticipated expenses.
- Family member must live with the debtor or be a member of the debtor's immediate family, i.e., parent, grandparent, sibling, child, grandchild.
- Elderly, chronically ill, or disabled person must be unable to pay the expense.

Line 36, Protection against family violence.

- Include only ongoing expenses related to a real threat.
- Legal costs related to a restraining order may qualify.
- Home security system costs will not qualify in all cases.
- Nature of expense, but not the amount, must be kept confidential by the court.

Line 37, Home energy costs.

- Insert the amount by which the twelve-month average home energy costs exceed line 20A.
- Amount claimed is unlimited, but must be documented.

Line 38, Education expenses for dependent children under 18.

- Includes public or private elementary or secondary education.
- Does not include college or preschool education.
- Child must be under 18 at filing.
- Amount may not exceed \$147.92 per child.

- Expenses must be documented.
- Cannot duplicate expenses claimed on line 30.
- Does not include school lunches, which are included in National Standards on line 19A.
- Can include home schooling expenses.

Line 39, Additional food and clothing expense.

- The USTP Web site breaks out the food/clothing standard for application of the 5 percent limit.
- Expenses must be actual, not merely anticipated.
- Special dietary and allergy restrictions can be covered.
- Documentation is required.

Line 40, Continued charitable contributions.

- Contribution is limited to 15 percent of gross income.
- The USTP position is that charitable contributions under section 707(b) are available to both below median and above median debtors. The Religious Liberty and Charitable Donation Clarification Act of 2006, Pub. L. 109-439 clarifies the Bankruptcy Code to ensure that above-median debtors may make continued charitable contributions.

Line 42, Future payments on secured claims.

- Total all payments coming due in the 60 months following filing and divide by 60.
- In the case of a variable rate loan, use the loan rate in effect on the petition date to calculate the payments.
- In the case of a "balloon" payment within 60 months, use the full amount of the balloon to calculate the average payment.
- Does not include property subject to a lease rather than a loan.
- Includes all secured debt, even "toys" and luxury items. Although the USTP position is to allow secured payments for luxury items on this line, the Program believes that luxury expenses may demonstrate that a petition was filed in bad faith warranting dismissal of the case under section 707(b)(3)(A), and may be considered in determining the totality of the debtors financial circumstances under section 707(b)(3)(B).
- Includes a secured loan payment, even when the value of the collateral is less than the amount of the loan.
- Outside the First Circuit, does not include payments when the debtor intends to surrender the collateral securing the loan.
- In the First Circuit, debtor may include payments on line 42 when the debtor intends to surrender the collateral securing the loan. However, the USTP position is that the failure of the debtor to continue to make the payments post-petition in surrendering

the property may be considered in determining the totality of the debtor's financial circumstances under section 707(b)(3)(B).

Line 43, Other payments on secured claims.

- Does not include arrearage on luxury items; the item must be "necessary for the support of the debtor or dependents."
- See line 42 for a discussion of when the collateral is surrendered.

Line 44, Payments on prepetition priority claims.

- The total of priority debt includes only amounts due as of filing.
- Does not include figures already listed on line 28.

Line 45, Chapter 13 administrative expenses.

- Debtor must project a hypothetical chapter 13 plan payment to calculate the figure on line 45a. The USTP does not insist on mathematical exactitude and allows a reasonable estimation of the hypothetical chapter 13 plan payment.
- Generally the plan payment should be calculated based on the amount of monthly disposable income suggested by the completion of the means test, or shown on Schedules I and J.
- The multiplier for line 45b is found on the USTP Web site by state.

Line 56, Other Expenses.

- Generally this line should be used to assert special circumstances to rebut the presumption of abuse under section 707(b)(2)(B).
- Also may provide information for the UST to consider under section 704(b)(2) when determining whether a motion to dismiss is appropriate.
- Should not be included by debtor in calculating disposable income on line 51, or in determining whether the presumption of abuse arises on lines 52-55.

April 23, 2010

U.S. TRUSTEE PROGRAM HELPFUL LINKS

Means Testing

<http://www.justice.gov/ust/eo/bapcpa/meanstesting.htm>

<http://www.justice.gov/ust/eo/bapcpa/index.htm>

IRS Standards

<http://www.irs.gov/irm/part5/index.html>

<http://www.irs.gov/individuals/article/0,,id=96543,00.html>

Financial Analysis Handbook

<http://www.irs.gov/irm/part5/ch15s01.html#d0e193751>

Treatment of Non-Business Transportation Expense

<http://www.irs.gov/irm/part5/ch08s05.html#d0e84811>

On Our Watch

BY CLIFFORD J. WHITE III¹

Why U.S. Trustee Enforcement Should Not Yield to Debtor and Creditor Preferences

This year marks the 25th anniversary of the nationwide expansion of the U.S. Trustee Program (USTP). From its inception as a pilot project established in the Bankruptcy Reform Act of 1978 through numerous congressional amendments that expanded the role of the USTP, it has served, in the words of our legislative history, as the “watchdog” of the bankruptcy system. Although the USTP’s duties have expanded over the years, our essential mission has remained constant: to promote the integrity and efficiency of the bankruptcy system by enforcing the law as Congress has written it—and to do so with prudence, discretion and sound judgment.

Stakeholders in the bankruptcy system often have differing views on when and how U.S. Trustees should assert their broad authorities in a particular case. Indeed, U.S. Trustees exercise civil prosecutorial discretion every day. These decisions are designed to achieve our legislative purpose by reflecting both national USTP priorities and the district-by-district needs of the bankruptcy system. This article describes some of the basic principles and objectives that guide our prosecutorial discretion.²

Legislative Background

The statutory basis for the USTP’s role in bankruptcy cases starts, but does not end, with the Bankruptcy Reform Act of 1978. The USTP was initially established as a pilot program in 18 judicial districts. Many of the U.S. Trustees’ current duties and authorities were expressly added in later amendments. Importantly, 11 U.S.C. § 307, which allows a U.S. Trustee to appear and be heard on nearly any issue in any case or proceeding under title 11, was enacted in 1986. In the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), the USTP was given new substantive authorities, such as supervising the means test and approving prebankruptcy credit-counseling agencies. Congress also

directed U.S. Trustees to seek the appointment of chapter 11 trustees in cases where there are reasonable grounds to believe that certain types of misconduct have occurred. These additional duties and authorities reflect Congress’s desire for the U.S. Trustee to play an increasingly active role in policing the bankruptcy system.

Prosecutorial Discretion

U.S. Trustees recognize the importance of exercising prosecutorial discretion, and they do so every day. Not every variation from strict legal requirements mandates an enforcement action or a remedy. An enforcement agency must look at both the facts and circumstances of each case, as well as the broader system-wide impact of the conduct or violation. USTP enforcement decisions are driven by the fact that Congress designed the bankruptcy system to operate for the benefit of all stakeholders—the debtor, its employees, large creditors, small creditors and the general public. For instance, U.S. Trustees generally should not participate in true two-party disputes. In deciding whether to object to a motion or to take an enforcement action, U.S. Trustees ask many questions, which can include: Will the resolution of the matter implicate rights of other parties or of any institutional interest of the bankruptcy system? If the parties propose a settlement, does the statute allow the court to approve the agreed-upon relief? Might the court’s adjudication set a troubling precedent?

In determining when to become involved in an issue or a dispute, U.S. Trustees bear in mind their essential mission to promote compliance with the law. The bankruptcy laws are more than a default set of rules that parties can choose whether or not to follow. In so many areas, Congress has made public policy choices that may not be contravened by agreement. The public interest is served by consistent application of the Bankruptcy Code as written, rather than by a system where anything goes as long as the biggest economic interests in the case agree and no one else notices or can afford to complain.

U.S. Trustees will not seek to substitute their business judgment for that of the debtor and creditors, but corporate debtors and large creditors do not have license to rewrite the laws passed by



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¹ The author extends his deepest appreciation to colleague **Walter Theus** for his work on this article.

² In late 2012, the author participated in ABI’s Winter Leadership Conference Great Debates session on the topic of “Should the U.S. Trustee’s enforcement role in chapter 11 cases yield to creditor preferences?” This article is an adaptation of those remarks prepared for the debate, and the conference materials are available at materials.abi.org/material/great-debates.

Congress and signed by the President. A U.S. Trustee's prudential decision not to contest an apparent violation of the Bankruptcy Code or Rules in a particular case does not mean that this violation is immune from objection in future cases.

Prudential considerations are part and parcel of the decision-making process of every enforcement agency. Once an enforcement agency decides to exercise its discretion to bring an action or to take a position on a legal or factual issue, the court should promptly adjudicate the issue regardless of whether the court disagrees with the agency's decision to act. The court's responsibility is to decide the dispute before it on the facts and the law, without regard to the identity or economic stake of the parties to the dispute.

Protecting All Stakeholders

Enforcing the law and advancing economic interests in a case are not inconsistent, unless the efforts to advance the economic interests contravene the law. This false dichotomy is most frequently suggested when strict application of the law would upset an agreement between powerful constituencies in the case, such as the debtor's entrenched management and major institutional creditors. Unlike many other areas of the law, bankruptcy implicates a multiplicity of interests. The interests of management of the debtor company and its largest creditors are often aligned against the interests of other parties in the case—sometimes against employees, small creditors and other major parties, such as privately managed investment funds. The public also has an interest in compliance with the law.

This multiplicity of interests in bankruptcy is one of the major reasons that Congress established the U.S. Trustee role as a neutral party to protect all interests—including less-powerful economic interests and the public interest. The USTP's independence is at the core of its existence and justifies its unique role in the system. The USTP is the only party in a case that acts as a disinterested party to protect the integrity of the bankruptcy system. We recognize that other parties have interests they understandably want to vindicate. But when the solutions crafted by those parties are outside the law or require the court to enter an order beyond its powers, it is the USTP's responsibility to object.

If the USTP were to limit its involvement to issues that had been joined by economic stakeholders, it would not police a wide variety of important areas. The following are examples of the types of enforcement actions that the USTP may undertake, even in the absence of economic stakeholder involvement.³

Venue

U.S. Trustees may seek the transfer of venue when appropriate under the statutory scheme. In one fact pattern, the debtor manufactures a venue by creating a nonoperating affiliate with few, if any, assets on the eve of bankruptcy. No creditor objects, but to ensure that the court has an opportunity to exercise its statutory discretion under the "interests of justice" test, the U.S. Trustee does object. If the USTP were powerless to act in this case, debtors would be able to forum-

shop and to ignore the venue parameters set by Congress.⁴ Congress did not write venue laws with an exception permitting debtors to file anywhere as long as the economic interests agree. Congress also did not create a watchdog unable to act independently to enforce the law as written. There is no better standard for the USTP to uphold than the "interests of justice"—and we will continue to do that even if it means we must act alone.

The Bankruptcy Code is not a set of suggestions to be followed when adherence is convenient. We are all well advised to respect the Code and thereby enhance public confidence in the system that we serve.

Appointment of a Trustee

Another USTP enforcement action that is often held up for scrutiny is the motion to appoint a chapter 11 trustee. Debtors sometimes claim that the appointment of a trustee will destroy the business or that any change in control will interfere with a sale or otherwise result in a catastrophe. These arguments should be closely examined. The trustee's appointment might be catastrophic for top management, but not for the creditors, the employees and the public.

Examine the following fact pattern: The debtor and the largest creditor file a motion to authorize a quick sale even though management of the company is guilty of pre-petition wrongdoing. Then, to defeat the U.S. Trustee's motion for a trustee, the company board's and largest lender install a chief restructuring officer (CRO) to manage the quick sale. The U.S. Trustee opposes the CRO because the board is tainted by pre-petition conduct and the CRO cannot be independent of the board. The only cure is the appointment of an independent chapter 11 trustee to look out for the interests of all stakeholders.

Consider one more fact pattern: The debtor successfully installs a CRO to defeat a motion for a trustee. Ultimately, the debtor's business cannot be sold as a going-concern and all employees are laid off. In such a case, it is difficult to see how deference to incumbent management benefited stakeholders.

Executive Bonuses

U.S. Trustees frequently object to executive bonuses that do not comply with 11 U.S.C. § 503(c). Examine this common fact pattern: The debtor proposes to pay bonuses to keep executives and insiders on board during the sale or reorga-

⁴ Some commentators have highlighted the court's *dictum* in *In re Patriot Coal Corp.*, 482 B.R. 718, 744 (Bankr. S.D.N.Y. 2012), that the decision to grant the U.S. Trustee's motion might have been different had no party with an economic interest also challenged venue. Such a result, however, would clearly have been inconsistent with the ruling itself, which stated that the debtor's steps to manufacture venue were an "affront to...the integrity of the bankruptcy system"—as well as with the decision in *In re Winn-Dixie Stores Inc.*, Case No. 05-11063 (RDD) (Bankr. S.D.N.Y. Apr. 12, 2005), that the "interests of justice" trump the "convenience of the parties." For a summary of these cases, see Gregory W. Fox, "Patriot Coal: Interest of Justice Trumps Convenience of the Parties," *XXXII ABI Journal* 1, 20, 70-71, February 2013.

³ Unless otherwise noted, the following are composite examples and do not necessarily mirror the facts of any particular case.

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nization of the company. Only the U.S. Trustee objects. In response, the debtor recharacterizes the retention bonus as an easy-to-reach incentive bonus, and the U.S. Trustee objects to enforce the bonus restrictions in § 503(c).

Congress made the policy choice to strictly limit retention bonuses, and that choice should not be contravened by private interests. As case law holds, an incentive plan cannot be a “lay-up” but must be a “stretch” to qualify under § 503(c). The statute is a clear statement of congressional intent to rein in abusive bonus programs in bankruptcy, yet parties treat it as an inconvenient obstacle to overcome.

In one recent case, the court heard an executive bonus motion and its objections. While the matter was under advisement, the press reported that the debtor sent notices to employees under the Worker Adjustment and Retraining Notification (WARN) Act. Simple arithmetic showed that the total executive bonus amount sought by the debtor was the equivalent of more than \$31,000 for each employee reportedly facing a layoff. Even though the press report was not part of the court record or a basis for the court’s decision, it was troublesome.⁵

Professional Compensation

In yet another major area, review and approval of compensation requested by bankruptcy professionals, the U.S. Trustee is often the only party to object. Assume that the U.S. Trustee discovers that the debtor’s law firm routinely discounted its fees billed to the debtor before the bankruptcy filing, but the law firm neither discounted its fees for the bankruptcy engagement nor disclosed the pre-petition discount. Under 11 U.S.C. § 330, Congress requires that compensation be reasonable “based on the customary compensation charged by comparably skilled practitioners in cases other than cases under [title 11].” If the U.S. Trustee does not raise this important issue, it is likely that no party will.

Consider one more fact pattern relating to professional compensation: To break an impasse and settle all contested

issues, the debtor proposes that if certain creditors will withdraw their objections to the reorganization plan, the debtor will amend the plan to pay the attorneys’ fees of these creditors. The U.S. Trustee objects to enforce § 503’s requirements that limit when creditors can have their attorneys’ fees paid by the estate. That section binds creditors and debtors alike; neither the court nor the parties by agreement have the authority to alter that statutory scheme.

Consumer Bankruptcy

The previous examples were drawn from chapter 11 fact patterns, but the USTP also intervenes to protect the integrity of the bankruptcy system in consumer cases. For instance, in seeking to keep their homes, individual debtor homeowners are most often outmatched by large banks and their big law firms, even in situations where the banks and/or their attorneys have engaged in questionable lending, collection or foreclosure practices. In many of these cases, the banks will quickly settle with the homeowners and then combat U.S. Trustee efforts to remedy systemic problems by arguing that there is nothing left for the U.S. Trustee to investigate or remedy. The USTP has rejected this “no harm, no foul” defense against the investigation of potentially systemic violations and has actively participated in the negotiation of several major nationwide settlements designed to remedy collection abuses. Needless to say, the USTP has no economic interest, yet the USTP has investigated or taken court action in thousands of such cases.

Conclusion

The USTP will act in cases when parties seek to fundamentally contravene the law. In those cases, the USTP is obliged to police the system and to act as a “watchdog” over the integrity of the bankruptcy system. The Bankruptcy Code is not a set of suggestions to be followed when adherence is convenient. We are all well advised to respect the Code and thereby enhance public confidence in the system that we serve. **abi**

⁵ *In re Hawker Beechcraft Inc.*, 479 B.R. 308 (Bankr. S.D.N.Y. 2012) (order denying executive motion bonus).

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