By Donald L. Swanson

Small Business Trustee as a Mediator-ish Facilitator: A Proposal

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Section 1183(b)(7) of the Small Business Reorganization Act of 2019 (SBRA) states, "The trustee shall ... (7) facilitate the development of a consensual plan of reorganization." However, the precise meaning of the statutory phrase "facilitate the development of a plan" is uncertain.

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Mediation Role and Concerns

The U.S. Trustee's Office recently indicated that mediation experience would be a useful background for a small business trustee.[1] Such an indication makes perfect sense, because "facilitating" a "consensual" arrangement is what mediators do and what mediation is all about.

However, there are concerns about a small business trustee serving in the formal role of a mediator, since the trustee is not entirely disinterested. This is due to the fact that a small business trustee's duties include the following directives that create a disinterestedness problem:

- to "investigate" the (1) acts, conduct, assets, liabilities and financial condition of the debtor, (2) operation of the debtor's business, (3) desirability of the continuance of such business, and (4) any other matter relevant to the case or to the plan formulation;
- to "file a statement of any investigation" regarding (1) any fact ascertained pertaining to fraud, dishonesty, incompetence, misconduct, mismanagement or irregularity in the management of the affairs of the debtor; and (2) any cause of action available to the bankruptcy estate;
- to "transmit a copy or a summary of any such statement" to interested persons designated by the court; and
- "if advisable," to oppose the discharge of the debtor.

Such duties and responsibilities would seem to disqualify a small business trustee as a formal mediator under any standard of disinterestedness. Yet, a small business trustee has a statutory duty to facilitate.

The Facilitation Proposal

Here is a proposal on one way that a small business trustee might facilitate the development of a reorganization plan, in a mediator-ish way, despite concerns over disinterestedness.

Immediately following the debtor's § 341 meeting, the debtor, creditors and small business trustee should adjourn to a separate meeting room to engage in a facilitation meeting. The meeting would be held in joint session (as opposed to a caucus format), chaired by the small business trustee and subject to the confidentiality provisions of Rule 408 of the Federal Rules of Evidence (FRE).[2] Here is an agenda for the facilitation meeting:

1. The debtor explains the intended course of action and terms of a proposed reorganization plan;
2. Creditors explain their views and suggestions about the debtor's intended course of action and proposed plan; and
3. Discussions ensue on the potential for a course of action and/or plan terms that might form the basis for an agreement among the parties.

Mediation Similarities and Differences

This proposal is similar to — but different from — a mediation in the following ways.

Similarities

A mediation brings parties together to discuss their disputes with a view toward reaching an agreed-upon resolution, led by a third person who, as between the disputing parties, is neutral and impartial. Such details accurately describe the proposed facilitation meeting.

Differences

There are two ways that a proposed facilitation meeting would be different from a formal mediation. First, a mediator must be disinterested and have no stake whatsoever in the parties' disputes,

1 In November 2019, the U.S. Trustee's Office issued a "Public Notice — Solicitation of Applications to Serve as Subchapter V Trustees" document that contains this sentence: "Those with business, managerial, consulting, *mediation*, and operational experience are encouraged to apply." (emphasis added).

2 FRE 408, "Compromise Offers and Negotiations," provides: "(a) Prohibited Uses. Evidence of the following is not admissible — on behalf of any party — either to prove or disprove the validity or amount of a disputed claim or to impeach by a prior inconsistent statement or a contradiction: (1) furnishing, promising, or offering — or accepting, promising to accept, or offering to accept — a valuable consideration in compromising or attempting to compromise the claim; and (2) conduct or a statement made during compromise negotiations about the claim — except when offered in a criminal case and when the negotiations related to a claim by a public office in the exercise of its regulatory, investigative, or enforcement authority. (b) Exceptions. The court may admit this evidence for another purpose, such as proving a witness's bias or prejudice, negating a contention of undue delay, or proving an effort to obstruct a criminal investigation or prosecution."

whereas the small business trustee has multiple responsibilities in the bankruptcy case that render the trustee interested to some degree — and not entirely disinterested. Second, a mediation must be conducted with the highest degree of confidentiality. Such expectations of confidentiality cannot be met in the proposed facilitation because of the trustee's investigation-related role and responsibilities in the case. Accordingly, the expectations of confidentiality can only be those under FRE 408, which are the confidentiality expectations commonly associated with ordinary negotiations between disputing parties.

Mediation Concerns

The term "mediation" has both a particular meaning and a general meaning. In particular, "mediation" refers to a negotiation session between disputing parties under the leadership of a neutral, impartial and disinterested third party. Any deviation by the mediator from neutrality, impartiality and disinterestedness is unacceptable and a disqualifying defect.

Generally, however, "mediation" is used as a catch-all term encompassing a variety of alternative-dispute-resolution (ADR) processes, some of which do not qualify as formal mediations. Unfortunately, this general use of the term "mediation" creates confusion and discord for ADR processes that cannot qualify as formal mediations.

The facilitation proposal above is a "mediation" only in the catch-all sense of the word, because the trustee cannot qualify as "disinterested." This is why this proposal uses the statutory term "facilitation" instead of "mediation."

Ethics of Mediation and Other ADR Processes

Professional ethics for a formal mediation are well developed and defined, and the tenets of such ethics are held by many with doctrinaire certitude and rigor. However, professional ethics for other types of ADR processes (*i.e.*, those that cannot qualify as a formal mediation — referred to herein as "mediation-ish" processes) are not well defined. Here are some examples:

- A voluntary negotiation session among a group of disputing parties, led by one of the disputing parties, is a mediation-ish ADR process, but it is not a mediation in the formal sense of the word because the leader of the negotiations has a stake in the outcome.
- A judicial settlement conference led by the presiding judge for the case is a mediation-ish ADR process. However, it is not a formal mediation because the judge in the settlement conference and the judge who will ultimately decide the case are the same person. Such a judge may well be neutral and disinterested in the settlement conference, but that judge is not impartial due to his/her decision-making tasks that lie ahead (*i.e.*, the judge will be taking sides in the end).
- An early neutral evaluation is a mediation-ish ADR process, but it is not a formal mediation because the evaluator — like the judge in the settlement conference — is likely to take sides in the end.

The fact that each of the aforementioned examples fails to qualify as a formal mediation might be an interesting observation, but it is an irrelevant one. The relevant question in each of such examples is the following: Will the mediation-ish ADR process help the parties reach a resolution of their disputes? If the answer is in the affirmative, then the parties should use that process. If the answer is in the negative, they should not.

This facilitation proposal is, similarly, a mediation-ish ADR process that cannot qualify as a formal mediation. However, if the process helps debtors and creditors reach a consensual reorganization plan (and the author believes it will), then it is a process that should be pursued.

Duties Imposed by a Statute

Is it acceptable to utilize a facilitator to develop a consensual reorganization plan? Is it acceptable if the facilitator has a set of duties and responsibilities, imposed by a statute, in the bankruptcy case that impairs disinterestedness? The answer to both questions is "yes," because Congress has declared it be so, with the force of a law of the land.

Accordingly, it is now the duty of all bankruptcy professionals to do what we can to help make Congress's directives work. In addition, professional-responsibility considerations need to be adjusted to meet what Congress requires.

Some Practical Issues to Be Considered

There are some practical issues relating to the facilitation proposal that should be considered. The joint-session format means that all parties and the facilitator are in the same room during the facilitation session. A caucus format (*i.e.*, the mediator meets separately with each party) is not to be used. Why? A caucus meeting between a party and the mediator during a formal mediation session is where the highest levels of confidentiality are required.

It is precisely because of the facilitator's investigative role and responsibilities in the bankruptcy case that the highest levels of confidentiality cannot be assured or expected in the facilitation meeting. It is also why confidentiality expectations, in the proposed facilitation, are only that of what FRE 408 provides for negotiating parties.

The timing of these efforts matters, and conducting them early is important. The time immediately following the § 341 meeting is an excellent occasion for the proposed facilitation meeting. Logistically, the debtor always attends the § 341 meeting. According to the U.S. Trustee's Office, a small business trustee is to also attend the § 341 meeting. Creditors who care (*e.g.*, the primary secured creditors) are often in attendance as well. So, a facilitation meeting immediately following the § 341 meeting should make perfect logistical sense for all involved.

Further, studies have shown that early mediation efforts, in disputes before a court, have much greater success than later efforts.[3] As parties litigate their differences, their positions become entrenched and less flexible, thus making settlement more difficult to accomplish. For example, each disputed motion or discovery battle serves to decrease the odds of settlement. Accordingly, a facilitation meeting

3 *See, e.g.*, Dorcas Quek Anderson, Eunice Chua & Ngo Tra My, "How Should the Courts Know Whether a Dispute Is Ready and Suitable for Mediation? An Empirical Analysis of the Singapore Courts' Referral of Civil Disputes to Mediation," 23 *Harvard Negotiation Law Review* 265 (August 2018).

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tied to an early event in the bankruptcy case (*i.e.*, the § 341 meeting) should be an optimum time for holding facilitated settlement discussions.

Notably, one impediment to an early mediation effort is typically the need for discovery before the parties can fully understand the issues in the case. This impediment makes sense in a lawsuit where issues of liability prevail, along with questions about the amount of damages. In a small business reorganization, however, the vast majority of claims are based on promissory notes and invoices, for which liability is largely undisputed, and the amount of damages is a simple exercise in arithmetic. The real question in such a case is typically about collectability — not liability or damages. Accordingly, the need for discovery in the early stages of a chapter 11 small business case is minimal.

The proposed agenda for the joint session is something the author has seen work many times. At the beginning of such a session, expressions of concern often go something like: "This will never work; you'll just make people mad," "The parties will never be civil to each other," or "There is no conceivable path to a resolution here." In the author's experience, each such expression of concern is faulty: Parties do not get mad; they can discuss their disputes civilly, and resolutions often appear out of nowhere — just when everything looks bleak.

It would be possible for the small business trustee to encourage parties to hire a private mediator or judicial mediator to ensure that the facilitation effort qualifies as a formal mediation. However, such an approach would make the process more cumbersome and heighten its cost, whereas the creation of efficiencies is an obvious goal for the small business legislation (*e.g.*, most disclosure statement obligations are eliminated[4]), as is the minimization of costs (*e.g.*, U.S. Trustee's quarterly fees are eliminated[5]).

Conclusion

Kudos to Congress for imposing the responsibility for "facilitating the development of a consensual plan" upon the small business trustee. This appears to be a great benefit to the small business reorganization system. It is now the task of all bankruptcy professionals to make the system that Congress has established work. Hopefully, the facilitation meeting proposed herein can be one step in doing just that. abi

4 *See, e.g.*, § 1190 of the Small Business Reorganization Act of 2019.
5 *See, e.g.*, § 4(b)(3) of the Small Business Reorganization Act of 2019.