ABI Commission Hearings Held During NABT Convention in New Orleans

Editor's Note: *The Committee on Chapter 7 of the ABI Commission on Consumer Bankruptcy held a public meeting during the National Association of Bankruptcy Trustees (NABT) annual convention on Sept. 15 in New Orleans. The Commission invited stakeholders attending the event to make an oral statement and submit a written statement. The hearing had four panels, and this month's Legislative Update includes excerpts from selected testimonies. For more information and the full text of the testimonies, visit ConsumerCommission.abi.org.*

Members of the ABI Commission on Consumer Bankruptcy's Committee on Chapter 7 heard from trustees during the NABT convention in September.

H. Jason Gold (Nelson Mullins Riley & Scarborough LLP; Washington, D.C.)

H. Jason Gold

Increasing compensation for chapter 7 trustees in the 90 percent of the chapter 7 cases filed nationally in which there are no assets to administer is critical. The $60 no-asset fee has not been raised since 1994, while the responsibilities placed upon chapter 7 trustees have increased substantially. The increase is necessary, long overdue and essential to the operations of our bankruptcy system....

The Bankruptcy Trustee's Vital Role in Our System

The chapter 7 trustee is, in most cases, the face of the bankruptcy system to the consumer debtor. The trustee meets the debtor for the first time at the 341 meeting. But the initial work starts prior to that.

The trustee must review the bankruptcy petition, the schedules of assets and liabilities, and the statement of financial affairs, as well as the other required filings, prior to the 341 [meeting] in each of the cases assigned every month.

Then the trustee must determine that the debtor has met the requirement to state his/her intention with respect to encumbered property, ensure that the debtor has filed tax returns (along with a review of the most recent return), review the debtor's pay advices, review the debtor's bank statements, provide important notices to holders of domestic-support obligations about the bankruptcy filing, review the filings to see if the debtor is eligible under the means test for chapter 7 relief, [and] conduct the 341 meeting and examination, among the other statutory duties. In the 90 percent-plus cases that are "no-asset cases" and result in the filing of a "no distribution report," trustees nevertheless have continuing responsibilities and duties. All of this for $60 per case, and in those cases where the debtor is appearing in *forma pauperis*, for free. As can be seen, "no-asset" does not mean "no work."

Of course, certain responsibilities are more demanding and challenging than others. If the debtor served as an administrator of an employee benefit plan, the trustee [might] be obligated to continue to perform the duties required of that administrator. In health care bankruptcies, trustees [might] also have obligations to transfer patients from facilities that are being closed and to safeguard patient privacy and health care records.

Serving as a cop on the beat is also an essential part of the chapter 7 trustee function. The chapter 7 trustee is initially responsible for any determination of potential misconduct on the part of the debtor, including criminal activity to be reported to the U.S. Trustee for referral to the U.S. Attorney. Those debtors who seek to game the system are first rooted out by the chapter 7 bankruptcy trustee. Meeting this obligation is essential for the bankruptcy system to be properly policed.

The Economic Burdens on Trustees

The chapter 7 trustee executes the important public policy initiatives set forth in the Bankruptcy Code, serving a diverse constituency of creditors, the debtor, the bankruptcy court and the Office of the U.S. Trustee. There is much routine and mundane work. But there are often legal and factual issues presented that can be complicated and challenging. These tasks and responsibilities are not waived or reduced because the case is a no-asset case.

Over the course of my career and tenure as a chapter 7 trustee, there have been hundreds ... [of] cases where substantial amounts of time and out-of-pocket costs have been incurred to only realize at the end of the case that there is no recovery at all, and only the $60 fee is available as compensation. Trustees in smaller practices find this to be quite burdensome and unfair. Without an increase in compensation, experienced and effective trustees may not be able to continue to serve.

Conclusion

No segment of the legal system in our country touches more people than the bankruptcy process. And no player

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within that process reaches both debtors and creditors like the chapter 7 trustee. No system, however well designed, can be better than the people who operate within it. Therefore, we must retain and attract competent, honest and committed trustees. As designed, our present system simply will not work effectively without them. In other insolvency systems around the world, government officials on a public payroll handle the duties of administration, oversight, monitoring and investigation. But our system relies on private parties to provide these functions, at a fraction of the cost to the system and the taxpayers.

Statutory fees have been increased from time to time for court-appointed counsel to the criminally accused, to jurors and [to] others. But the $60 no-asset fee to trustees, as quasi-judicial officers of the bankruptcy courts, has not been increased in decades. Given the vital role that bankruptcy trustees play in the bankruptcy system, I urge the Commission to include in its report a recommendation that Congress increase this fee to $120.

N. Neville Reid (Fox Swibel Levin & Carroll LLP; Chicago)

N. Neville Reid

First, trustees incur substantial nonpayment risk over extended periods of time in performing their fiduciary duties, and the fee increase, while not eliminating that risk, will lessen the financial burden of that risk. Trustees are required by law to investigate assets, many of which include potential litigation claims against parties that illegally received historical transfers from the debtor, such as fraudulent conveyances. Frequently, the targets of these investigations are well funded and hostile parties unwilling to settle with the trustee until after they have forced the trustee to expend substantial time in protracted litigation, including expensive discovery disputes. There is usually not enough cash in the bankruptcy estate to adequately fund the trustee's investigation and litigation of these potential claims, and often the cases are too small to attract litigation funding from third parties. Finally, even if the trustee obtains a judgment and can collect on some of it or manages to liquidate other assets, the trustee usually does not seek full recovery of her fees and costs of administering his bankruptcy estate, just in order to enable her to make a distribution of estate funds to the creditors. The fee increase, as applied to the broad array of cases in which the trustee investigates assets but has to write off substantial time or collects nothing at all, will lessen the financial burden of those write-offs.

Second, the fee increase at least begins to correct an asymmetry in the bankruptcy system as between the trustee and similarly situated professionals. The trustee compensation has been flat in absolute terms for [more than] 20 years, but has actually declined in real terms due to the fact that it is not indexed for inflation and general prices have increased a total of 65 percent between 1994 and 2017 ... there are very few professions in which a worker is expected to take on more tasks, as trustees have, and receive over 50 percent less in real compensation over 23 years of his/her career. By contrast, attorneys representing debtors in chapter 7 cases have seen increases in their fees at least since the enactment of BAPCPA. According to one study published in 2012 (by **Lois Lupica** ... [of] the University of Maine Law School), the mean debtor attorneys' fees charged in no-asset chapter 7 cases [have] increased by 48 percent since the enactment of BAPCPA.

Finally, the trustee fee increase achieves these aforementioned benefits without unduly burdening debtors. While the trustee fee increase is funded by a parallel $60 increase in the chapter 7 filing fee, debtors who cannot afford the overall fee will still have the ability, as they do now, to obtain approval of an installment plan to pay the filing fee over time, or a waiver of the fee, as circumstances warrant. From a broader, system-wide perspective, any incremental burden on debtors from the filing fee increase is more than offset by the continued substantial benefits they experience from the bankruptcy system and the work of trustees. In 2016, for example, chapter 7 debtors in the aggregate filed petitions listing [more than] $137 billion in net general unsecured liabilities. The overwhelming majority of this debt has been or will be discharged, all to the debtors' substantial benefit. In addition, many debtors will continue to receive certain benefits from the trustees' investigative and asset-collection efforts, in that net proceeds received from those efforts are first applied to the debtors' priority claims, which include tax liabilities that would otherwise be nondischargeable. Each year, trustee collections result in payment of millions of dollars to federal, state and local taxing authorities, amounts [that] would likely not have been paid otherwise given that debtors typically have less ability, motivation or legal tools as trustees do to investigate and liquidate assets for the benefit of their creditors.

Raymond J. Obuchowski (Obuchowski Law Office; Bethel, Vt.)

With the enactment of BAPCPA, the implementation of the waiver of the § 1930 filing fee commenced.... [In 1998, the Federal Judicial Center conducted a study of the] Chapter 7 Filing Fee Waiver Program....

Chapter 7 trustees are not compensated in IFP cases, and the enactment of the fee-waiver program was an "unfunded mandate." Further, the failure to compensate trustees for their work is neither appropriate or fair, nor was nonpayment ever contemplated as part of the program....

As a general matter, trustees don't oppose the fee-waiver program; they just oppose the imposition of an involuntary tithing by a law that fails to provide for the compensation for services provided.

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Raymond J. Obuchowski

To put in brief perspective, in the period of Oct. 1, 2007, through Sept. 30, 2016, there were 7,108,564 individual chapter 7 cases filed. IFP cases in which the fee was waived totaled 231,288 cases, or the equivalent of approximately $77.4 million of filing fees. Of that amount, $13.8 million represents the trustee portion of the unpaid filing fee. Based on an arbitrary average number of trustees serving during that period at 1,100 trustees, this equates to slightly [more than] $1,400 per trustee of unpaid fees per year. Effectively, chapter 7 trustees have contributed nearly $14 million to the fee-waiver program in the past 10 years....

The Fee Waiver Program, as ... described in the FJC study, was not meant to be an unfunded mandate. The study suggested "the most straightforward way to fund a national program would be for Congress to increase the judiciary's appropriation by this amount, which represents 2/10 of 1 percent of the judiciary's total 1997 fiscal appropriation."

The report further suggested a secondary method requesting authorization for the application of the U.S. Treasury share of the filing fee to a "no year" account to fund the program, the caveat of the study being that it might be insufficient dependent upon future circumstances as filing rates. However, based on the current number of cases and even at the increased fee, it appears this would still work.

What I request this Commission to consider in the preparation of its report [is] to include the recommendations from the 1998 FJC study ... to address the "unfunded mandate" which in turn addresses the nonpayment of chapter 7 trustees in fee-waiver cases.

James B. Angell (Howard Stallings From Atkins Angell & Davis, PA; Raleigh, N.C.)


James B. Angell

I would like to address the committee regarding the practice of a trustee employing his/her own law firm as attorney for the trustee.... As a preliminary matter, it is important to note that 11 U.S.C. § 327(d) permits the bankruptcy court to authorize the trustee to act as attorney or accountant for the estate if such authorization is "in the best interests of the estate." In each district, our Bankruptcy Administrator is responsible for supervising trustees and for reviewing applications for attorneys' fees for attorneys for the trustee....

A trustee and counsel fulfill different roles. The trustee's role is generally (1) to enhance the estate and review claims to make the greatest possible distribution to creditors, and (2) to oversee the procedural aspects of the case to ensure that debtors are compliant, are properly entitled to a discharge, and sometimes to assist in referring the case for criminal prosecution....

An attorney's role is to prosecute adversary proceedings and contested matters as directed by the trustee. An attorney deals with formulating claims, drafting pleadings, formulating discovery, motion and trial procedures, and sometimes with legal matters pertaining to transactions by the estate.... An attorney is generally compensated on an hourly basis, although the Bankruptcy Code permits compensation on a contingent-fee basis in an appropriate case. There are several policy concerns that support a trustee employing himself/herself as counsel[.]

Case Efficiency

A trustee who serves as trustee/attorney has greater information about the case than an outside attorney....

Requiring the trustee to employ outside counsel requires educating counsel as to the debtor's business, manner of operation, business documents, relationships, principals, etc., which requires time from both the trustee and from outside counsel. In addition, as the case progresses, hiring outside counsel deprives counsel of direct and immediate contact with the trustee's paralegals, who are often a fountain of information regarding the case....

Roles "Informing" Each Other; Integrated Case Strategy

Over [the] long term, the trustee's service as trustee/attorney yields tangible benefits. A 341 meeting is generally an informational session; however, it is also an opportunity to question the debtor under oath. Lawsuits [might] be won before they are filed if the trustee is familiar with the requirements of trial and the elements of causes of action by asking the debtor-specific and detailed questions, as a lawyer would do at trial. The more experience [that] the trustee has as lawyer, the greater knowledge base [that] the trustee has in questioning the debtor at the 341 meeting, seeking documents or preserving records. Although the 341 meeting is not an attorney activity, the trustee [might] begin implementing legal strategy in the case at an early stage to obtain legal advantages....

Greater Supervision by [the] Trustee

A trustee is better able to supervise the attorneys in his[/her] own office, where he/she can see what they are working on and assist in developing theories or strategies. Supervising an attorney in another office is a different matter as the trustee must then "micro manage" the litigation in order to have the same ability to supervise....

Greater Supervision of [the] Trustee

Section 327(d) is permissive to the bankruptcy court. It may authorize a trustee to serve as counsel for the estate — the bankruptcy judge has discretion as to whether or not a particular trustee is properly serving the estate as counsel, whether due to overbilling, incompetence or other factors. Thus, the bankruptcy court may discontinue the practice as to all trustees in its district or as to particular trustees as it

H. Jason Gold, N. Neville Reid and Raymond J. Obuchowski (l-r) were among those who spoke to the Consumer Commission on the urgency of increasing compensation for bankruptcy trustees.

sees fit. The courts should retain this discretion as it affects the efficiency and effectiveness of the cases before them, just as they retain discretion as to the amount of attorneys' fees applied for.

Further, the disincentive to overbill as attorney for the estate is two-fold for the trustee/attorney. If the trustee/attorney is seen to be overbilling the estate, then not only may attorneys' fees be denied in the instant case, but the bankruptcy court may deny the trustee to employ himself/herself in future cases.

Steven Weiss (Shatz, Schwartz and Fentin, PC; Springfield, Mass.)

Steven Weiss

I want to speak first about concerns apparently raised by the consumer bankruptcy bar about the propriety of having trustees employ their firms for legal or accounting services. This has been the practice in Massachusetts during my tenure as trustee. Not only do I fail to see it as a problem, I strongly believe that it strongly benefits the administration of bankruptcy cases, particularly the smaller ones....

[T]he majority of cases in which my colleagues in western Massachusetts and I are able to recover assets for creditors are relatively small consumer cases. While I have not conducted a statistical analysis, I would estimate that my average cases result in recoveries of $10,000 to $20,000, and sometimes less. But it's worth emphasizing that creditors in consumer cases are equally entitled to the benefits of the administration of bankruptcy cases, and also that the percentage distributions to creditors in small cases typically exceed the percentages in the larger ones.

Unlike business liquidations, attempting to recover assets in consumer bankruptcy cases is almost always contingent work. Rare is the case in which a debtor files for chapter 7 relief expecting that his/her case is anything other than a "no-asset" case. Instead, the recoveries usually come from the investigations of trustees and their counsel: objections to exemptions, location of undisclosed assets, avoidance of preferential and fraudulent transfers and avoidance of unperfected liens. These efforts are almost always vigorously opposed. And, if the trustee and counsel are unsuccessful, their services go unpaid....

I am willing to accept the risk of nonpayment or reduced payment for my firm as part of the realities of being a panel trustee. Conversely, if I were not able to hire my own firm, and had to hire outside counsel, I am sure they would not be so receptive....

Even if there is a recovery, but the legal fees would eat up most of the potential distribution, I routinely reduce our firm's legal fees to ensure a meaningful distribution. I do not think outside counsel would be so sympathetic. In other words, I think that in many of my cases, those small contingent recoveries will not be pursued.

In addition to these practical realities, there are also institutional protections against any conflicts or potential abuse. As this Commission is well aware, trustee administration and fees for bankruptcy professionals are highly scrutinized. Pursuant to our local rules and practice, I keep separate time records for my services performed as trustee and as counsel. Those records are reviewed by the U.S. Trustee when I submit my final account before distribution. They are then reviewed by the bankruptcy judge, and they are ... available to creditors.

William G. Schwab (William G. Schwab & Associates; Lehighton, Pa.)

William G. Schwab

One of the things that I want to discuss today is the noncompensated duties and activities that trustees do that becomes doable only because I am also appointing myself as attorney for the trustee — a role in which I recognize that I will get compensated for approximately only 58 percent of my billable hours doing attorney for trustee, and 58 percent reflects the actual write-down in 2016. Trustee time write-down is higher.... But part of our job as trustee is also to uphold the integrity of the bankruptcy system. As a result, I also frequently monitor debtors' attorneys and their activities....

We frequently also have to bring 727 actions where I have object to discharges. What attorney would accept me as a client when I have to tell him/her, [that] there is no money in the case[?] One recent case was where [the] person sold a free-and-clear mobile home four days after the bankruptcy was filed and then spent the vast majority of the money she received, leaving the innocent purchasers who had spent their entire life savings holding the bag. My representation will go uncompensated for the 727 action. There is not enough money involved for a criminal prosecution.

Where I'm located, I have only a few creditor ... attorneys, and they [only] dabble in bankruptcy. If I want competent counsel, I have to represent myself or have to go to Philadelphia to hire counsel at $400 to $500 per hour. In the smaller-asset case, how can I afford an average fee of $75 to 250,000, which is what I've been charged in larger cases? They don't discount fees. In short, without me being both trustee and attorney for [the] trustee, only the larger cases will be administered. abi