A Primer on the Roles of the Office of the US Trustee and Individual Trustees in Bankruptcy Proceedings

by Paul A. Avron

Paul A. Avron is a partner at Berger Singerman LLP, resident in its Boca Raton, Fla., office. His practice focuses on corporate restructuring and appellate litigation in state and federal courts, both prosecuting and defending appeals.

A common theme in bankruptcy is transparency. A directly related theme running through the bankruptcy process is oversight provided by various actors, public and private. Included within this group of actors are the Office of the U.S. Trustee (UST), and individual trustees, whether appointed to serve in cases under Chapter 7, 11, or 13 of the Bankruptcy Code.[1] This article briefly discusses these actors who work to ensure transparency and the proper functioning of the bankruptcy process for all debtors, creditors, and other stakeholders.

Office of the US Trustee

The UST is a division of the U.S. Department of Justice. According to § 307 of the Bankruptcy Code, the UST "may raise and be heard on any issue in any case or proceeding under [the code] but may not file a plan pursuant to [Chapter 11 of the code]." This broad grant of authority by Congress provides the UST with the statutory right to be heard on any issue in any case in which it wishes to be heard. The UST is not an economic stakeholder in bankruptcy proceedings like creditors, but it serves the important function of oversight, roughly akin to an amicus party, in assisting bankruptcy judges efficiently and effectively perform their functions. Certainly, USTs take positions on various issues in the bankruptcy cases in which that office involves itself, but the general concept is that the UST helps facilitate the smooth functioning of the bankruptcy process as a whole.

The UST is most frequently involved in Chapter 11 reorganization cases, both individual and corporate Chapter 11 cases. Specifically, the UST is most frequently involved in Chapter 11 cases shortly after the filings and prior to the time that, mostly in significant cases, a committee of unofficial creditors is appointed to help protect the rights of unsecured creditors, many of which cannot afford the cost of retaining their own counsel when compared against the debt they are owed. The UST can, and sometimes does, remain actively involved in Chapter 11 cases even after the appointment of a creditor's committee, usually to the consternation of actual economic stakeholders whose views on a particular issue may diverge widely.

The UST also conducts what are referred to as "341 meetings," which is the first meeting of creditors contemplated by code § 341. In these 341 meetings, the individual debtor or a representative of a corporate debtor testifies under oath in response to questions by the UST (and creditors) principally concerning his, her, or its assets and liabilities and any pending litigation.

Finally, the UST appoints Chapter 11 trustees, a process discussed below.

Chapter 11 Trustees

Relief under Chapter 11 of the code is available to individuals and corporate entities. Code § 1107(a) contemplates that, with limited exceptions, Chapter 11 debtors have all of the rights and powers and are to perform the functions and duties of a trustee serving in a bankruptcy case. Those functions and duties are set forth in code § 704(a), which governs Chapter 7 cases. Thus, the presumption is that Chapter 11 debtors manage their properties and their affairs in bankruptcy.

There are circumstances where bankruptcy courts appoint individuals to serve as Chapter 11 trustees who, for various reasons, step in to manage the Chapter 11 debtors, most frequently when those debtors are corporate entities, instead of then-existing management. Generally speaking, bankruptcy judges are required to appoint Chapter 11 trustees under code § 1104(a)(1) based on the existence of "cause," including fraud, dishonesty, or gross mismanagement by current management, whether before or after the Chapter 11 filing or § 1104(a)(2) if such an appointment would be in the interests of creditors, owners of the debtors, and other interests of bankruptcy estates.

Chapter 11 trustees can also be appointed under § 1112(b)(1) where bankruptcy courts conclude that

such an appointment is preferable to dismissing a Chapter 11 case or converting it to a straight-liquidation case under Chapter 7 of the code. Code § 1112(b)(4) lists several factors that constitute "cause" for the appointment of a Chapter 11 trustee.

Chapter 13 Trustee

Chapter 13 cases are available only to individuals with certain restrictions based on the amount of debt. In Chapter 13 cases, individuals generally keep their property and operate during their cases under a plan of reorganization that contemplates monthly payments to creditors over a 60-month period, after which their non-home mortgage debts are discharged. Code § 1302(a) contemplates that the UST will appoint an individual in each federal juridical district of the country to serve as a "standing trustee" who essentially functions as the overseer of Chapter 13 cases in each such district. These standing trustees, in large part, run Chapter 13 cases from start to finish with minimal input from bankruptcy judges. Having said that, there are numerous issues that must be resolved by bankruptcy judges, including whether Chapter 13 plans meet the requirements for confirmation.

The functions of the Chapter 13 "standing trustee" include acting as a disbursing agent for creditors during the plan process and to represent the unsecured creditor class in terms of ensuring that the debtor pays as much as possible to unsecured creditors. Also in Chapter 13, certain taxes and student loans are not dischargeable at the conclusion of the plan process.

Chapter 7 Trustee

In Chapter 7 cases, available to individuals and corporate entities, individuals from pre-approved panels are appointed to serve as trustees. The function of Chapter 7 is to liquidate a debtor's assets that are non-exempt under applicable law, make distributions to creditors based on those assets, and pursue viable litigation claims that the debtors were pursuing prior to their bankruptcy filings. Chapter 7 of the code serves a purely liquidation function. The rights and powers and duties and functions of Chapter 7 trustees are set forth in § 704(a)(1)-(12).

Chapter 11 debtors, whether individuals or corporate entities, can liquidate their assets like that done in Chapter 7, which is generally done so Chapter 11 debtors can do so on terms that hopefully serve to maximize the value of their assets for the benefits of their creditors.

Conclusion

There are many stakeholders in the bankruptcy process, regardless of the particular chapter of the code a particular case is filed under, and the UST and the various trustees and standing trustees discussed above serve to facilitate the functioning of the process for everyone's best interests. The roles of these actors differ based on the applicable chapter of the code and the facts of the applicable law governing those cases. ⊙

Endnote

[1]All references to the "code" are to Title 11 of the U.S. Code.

President's Message *continued from page 3*

C. Permit other more experienced counsel of record the ability to provide some assistance to the newer attorney who is arguing the motion, where appropriate during oral argument.

Like Judge Torres, Judge Burke is explicit in his expectations: "All attorneys, including newer attorneys, will be held to the highest professional standards." And he further says that the court "draws no inference from a party's decision not to have a newer attorney argue any particular motion before the Court."

The benefits of these orders are obvious, especially to junior lawyers who don't normally receive an opportunity to stand up in in federal court. Part of what drew many of us to become litigators was the opportunity to try cases and argue motions. With the availability of trials and hearings dwindling, the orders mentioned provide much-desired—and some would say much-needed—experience for junior lawyers. The rules would also seem to lead to a greater opportunity for oral argument, generally, which most litigators and at least some clients would appreciate.

On the other hand, some judges have expressed concern that such orders would influence clients' choice of counsel or that they actually could increase the cost of litigation if unnecessary hearings were scheduled or if inexperienced counsel required more preparation for the hearing. As Judge Burke's order foreshadows, some fear that allowing or refusing to allow a junior lawyer to argue a motion could lead to inferences about the importance of motion to that party. All of these concerns seem to have been considered and, at least to some degree, mitigated by the judges' orders, but all remain valid.

Recognizing this still-nascent trend, as well as the continuing dearth of opportunities for junior lawyers to get meaningful courtroom opportunities, the FBA has created a task force, led by Sixth Circuit Vice President Glen McMurry, to study the various incarnations of these standing orders and their effects—intended and unintended. At the same time the Task Force will explore other ideas designed to help our junior lawyers get courtroom experience. We expect that the Task Force ultimately will propose best practices and model standing orders for consideration and potential adoption by our federal judges.

It is our hope that, working together, the FBA and our federal judges will create opportunities for the next generation of lawyers to "stand up" in federal court. ⊙

Editorial Policy

The Federal Lawyer is the magazine of the Federal Bar Association. It serves the needs of the association and its members, as well as those of the legal profession as a whole and the public.

The Federal Lawyer is edited by members of its Editorial Board, who are all members of the Federal Bar Association. Editorial and publication decisions are based on the board's judgment.

The views expressed in *The Federal Lawyer* are those of the authors and do not necessarily reflect the views of the association or of the Editorial Board. Articles and letters to the editor in response are welcome.