Introduction

Once a Chapter 7 case has been fully administered, it is time for the trustee to submit the final report to the United States Trustee. Before submitting the report, the trustee should be confident that there are no legal issues that could cause the United States Trustee to return the report or, worse yet, object to it. This article highlights a number of legal issues that trustees should keep in mind when preparing a final report in a Chapter 7 case.

Some of the issues discussed below pertain to every Chapter 7 final report. Other issues, however, arise only in complex cases. For purposes of this article, a complex case is defined as one that was either commenced involuntarily or converted from another chapter. Of course, while the issues identified below are important and recurring, they should not be considered exhaustive. For your convenience, a quick checklist of the final report issues discussed here appears at

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\textsuperscript{1}All views expressed in this article are those of the author and do not necessarily represent the views of, and should not be attributed to, the Department of Justice or the United States Trustee Program.
General Issues

1. IS THE FINAL REPORT PREMATURE?

The trustee submits the final report when the case is fully administered. As a working definition, a case may be considered “fully administered” once all assets have been reduced to cash, all claims objections resolved and all applicable tax returns accepted. Therefore, it is premature to submit the final report if some property still needs to be reduced to cash, if abandonments need to be done (other than at case closing), if a bar date for claims has not been set and expired, if there are unresolved claims objections, if any fee applications remain to be submitted, or if adversary proceedings that may result in cash for the estate have not been concluded. Remember that the pendency of dischargeability complaints or objections to discharge ordinarily should not delay case closing, because they have no effect on the dividend creditors will receive from the estate.

2. IS THE APPROPRIATE FEE BEING REQUESTED?

The trustee’s fee request is submitted as part of the final report. The compensation requested is subject to 11 U.S.C. §326. Amendments to §326 have changed the maximum allowable fee over time. One scale applies to cases filed from October 1, 1979, through October 7, 1984. Another
applies for cases filed from October 8, 1984, through October 21, 1994. The current one applies only to cases filed on or after October 22, 1994. To avoid an objection, request the appropriate fee for the date your case was filed.\textsuperscript{2}

Remember that the fee limitation of \$326 cannot be circumvented by use of 11 U.S.C. \$506(c). That section permits a trustee to surcharge secured creditors for benefits conferred by the estate upon their collateral. Section 506(c), however, is not a compensation statute and funds recovered pursuant to it inure to the estate. The trustee receives fees pursuant to 11 U.S.C. \$330 as capped by \$326 and those fees cannot exceed the percentage permitted therein.\textsuperscript{3}

3. IS THE REQUESTED FEE IN CONFORMITY WITH UNITED STATES TRUSTEE FEE GUIDELINES?

The Executive Office for United States Trustees has promulgated guidelines for reviewing fee applications and reimbursement of expenses filed under \$330.\textsuperscript{4} To avoid an objection, the trustee’s fee request should conform to the guidelines. Because Guideline I., F. allows for regional variations in format, an applicant should consult with the

\textsuperscript{2}See, e.g., \textit{In re H&S Motor Freight Inc.}, 23 F.3d 1431 (8\textsuperscript{th} Cir. 1994).


\textsuperscript{4}61 F.R. 24889-01.
Be sure that trustee time does not appear in the fee requests of other professionals, such as the trustee's accountants or attorneys. Also keep in mind that while the time spent by a paraprofessional may be used to justify allowance of the trustee’s statutory cap, paraprofessional time is not separately compensable.

4. HAS CASH BEEN MANAGED APPROPRIATELY?

The estate account should not have been depleted by unauthorized bank charges or debits, such as service charges or fees for supplying check stock or providing computer software and hardware. The trustee should attempt to have the bank reverse any such charges before submitting the final report.

The trustee should have had estate funds invested during the pendency of the case. If the trustee has lost an amount of interest, the trustee’s own fees may be surcharged for the loss. In the final report, the trustee should explain why interest was not earned. Further, the trustee should consider voluntarily reducing fees requested in order to avoid being surcharged.

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6. See, generally, In re Jenkins, 130 F.3d 1335 (9th Cir. 1997).
surcharged for the loss.\textsuperscript{7}

5. HAVE THE APPROPRIATE TAX RETURNS BEEN FILED AND TAXES PAID?

In corporate cases the trustee must file tax returns or obtain waivers from the IRS, regardless of whether the corporation has income. Where the estate’s gross income equals or exceeds the exemption amount plus the standard deduction, federal and state tax returns also have to be filed in individual cases. The final report should note that tax returns have been filed and accepted, that a tax waiver was obtained, or that no tax return was necessary given the debtor’s tax status.\textsuperscript{8}

Trustees also are required to do the appropriate withholding when paying wage claims. The proposed or pre-distribution report should identify how the withholdings were computed and show both the gross and net amount of wage claims to be paid.

Further, the trustee may need to file sales, excise, and other tax returns to establish the amount of the taxing authority’s claim.

6. HAVE SECURED CLAIMS BEEN ADDRESSED?

\textsuperscript{7}See In re Consupak, 87 B.R. 529 (Bankr. N.D. Ill. 1988).

Secured creditors are not required to file proofs of claims. Although secured debt is not mentioned in 11 U.S.C. §726, secured claims must be paid first if the secured creditors’ liens attach to cash held by the trustee—for example, if a creditor had a blanket lien on the debtor's assets. If an undersecured creditor has a lien on property that has not yet been abandoned, the trustee should abandon the property before closing to enable the creditor to assert an unsecured deficiency claim.

7. IS THE PROPOSED DISTRIBUTION TO CREDITORS CONSISTENT WITH SECTIONS 726 AND 507 OF THE BANKRUPTCY CODE?

Because 11 U.S.C. §507, the priority section, is amended from time to time with additional priorities being incorporated, it is important that the trustee's dividends conform to the priority scheme in place on the date the case was filed. Of course, the trustee must separately classify claims of different priority. For example, unsecured claims should not be lumped with tax claims. Note that with respect to tax claims, priority treatment is accorded notwithstanding tardiness.9

8. HAVE DUTIES OTHER THAN LIQUIDATION OF ASSETS BEEN PERFORMED?

Trustees are responsible for policing debtors’ attorneys’

9See In re Vecchio, 20 F.3d 555 (2d Cir. 1994).
fees for excessiveness, bankruptcy petition preparers for conformance to 11 U.S.C. §110 and debtors for appropriateness of discharge or dismissal in case of substantial abuse. Trustees are also required to refer instances of possible criminal violation. Although time spent performing these duties does not necessarily result in cash for the estate, it can be used to justify the trustee’s fee allowance. Such time should be recorded in the trustee’s fee application.

**Issues in Complex Cases**

9. **HAVE ISSUES PECULIAR TO THE INVOLUNTARY CASE BEEN ADDRESSED?**

Cases commenced by involuntary petitions may raise problems not found in Chapter 7 cases filed voluntarily. In some but not all cases a "custodian" may have been in place before the petition was filed. A typical custodian is an assignee for the benefit of creditors or receiver. Bankruptcy Rule 6002 requires a custodian to file an accounting and the court to rule on the propriety of the custodian's administration. The custodian's accounting and the court's order should be included in the final report. The trustee may have to compel the filing of these papers since they are often not filed voluntarily.

Creditors and their attorneys and/or accountants can be
compensated for filing the involuntary case. Their fee applications should be included with the final report, unless they already have been ruled on or were administratively barred.

10. HAVE ISSUES PECULIAR TO CASES WITH SUCCESSOR TRUSTEES BEEN ADDRESSED?

Cases involving two or more trustees also raise problems not ordinarily found in Chapter 7 cases. Bankruptcy Rule 2012(b) requires the successor trustee to “file” with the court an accounting of the prior trustee’s administration. This may be a separate document or part of the final report. The trustee should clearly differentiate between his or her administration and that of the predecessor trustee. Note that although the successor administration starts with what was received from the predecessor, the Rule 2012(b) accounting starts with what the predecessor received from the debtor or his or her predecessor.

Where the trustee served both as Chapter 11 trustee and Chapter 7 trustee, the trustee is technically his or her own successor because 11 U.S.C. §348(e) automatically terminates the service of a Chapter 11 trustee upon conversion. Accordingly, the final report should delineate and distinguish

\[^{10}\text{See 11 U.S.C. §503(b)(3) and (4).}\]
the Chapter 11 administration from the Chapter 7 administration. This may be important if there are enough funds to pay Chapter 7 costs of administration, but not enough to fully pay debtor-in-possession claims, including Chapter 11 trustee fees.

Keep in mind that while the Chapter 11 trustee may be reappointed as the Chapter 7 trustee, there is no legal requirement that this be done. Nor does such reappointment relieve the trustee from complying with the requirement, in Bankruptcy Rule 1019 and Chapter 8-35 of the Handbook for Chapter 7 Trustees, for the Chapter 7 trustee to submit a final report after a case is dismissed, converted, or reassigned.

11. HAVE ISSUES RAISED BY ESTATE SURPLUS OR INSOLVENCY BEEN ADDRESSED?

Surplus and insolvent estates raise unique issues. When the estate has a surplus and there are sufficient funds to pay creditors in full, interest at the legal rate must be provided to them before funds are turned over to the debtor. When the estate is insolvent and lacks sufficient funds to pay Chapter 7 costs of administration in full, the trustee and associated professionals will have to share pro rata with the bankruptcy clerk and, if applicable, the United States Trustee. If any
professionals previously received interim compensation, the trustee should move to disgorge such sums so that all may share pro rata.\textsuperscript{11}

12. HAVE ISSUES ARISING IN CONVERTED CASES BEEN ADDRESSED?

Cases converted from Chapters 11, 12, and 13 raise problems not found in other Chapter 7 cases. First, those cases are not ready to close until the final report and schedule of post-petition debts are filed pursuant to Rule 1019(5), the bar date has been set and expired for such claims, and the claims have been reviewed and determined. A copy of the Rule 1019(5) report should be included in the final report. Note that this report is in addition to the final report filed by the standing trustee pursuant to the same rule.

Second, professional fees incurred before conversion must be dealt with in the final report, if they have not already been determined by the court. If professionals have received retainers or had their retention approved by the court, their fee applications should be included with the final report or an administrative bar date order should be included to justify not paying them. Professional fees cannot simply be paid

through filing a proof of claim, as they require a judicial determination for their allowance.

Remember that in cases converted from Chapter 11 prior to August 1, 1987, creditors did not need to file proofs of claims in order to receive a dividend. If the Chapter 11 debtor listed the claims as undisputed, the trustee must pay them.\textsuperscript{12}

Finally, in cases converted from Chapter 11 there are often unpaid United States Trustee quarterly fees. These amounts have the same priority as Chapter 7 costs of administration and clerk of court fees.\textsuperscript{13} Therefore, if the estate is insolvent, Chapter 7 costs of administration must share pro rata with the United States Trustee. These fees should not be overlooked in the trustee’s proposed distributions.

**Conclusion**

Trustees must exercise professional judgment in implementing the suggestions set forth in this article. For the most part, however, addressing these issues should result in trustees’ final reports being processed more smoothly and

\textsuperscript{12}See *In re Fesco Plastics Corp.*, 908 F.2d 240 (7th Cir. 1990); *Matter of DeVries Grain & Fertilizer Inc.*, 12 F.3d 101 (7th Cir. 1993).

\textsuperscript{13}See *In re Endy*, 104 F.3d 1154 (9th Cir. 1997); *In re Juhl Enterprises Inc.*, 921 F.2d 800 (8th Cir. 1990).
cases being closed more quickly.
SELECTED LEGAL ISSUES
IN CHAPTER 7 FINAL REPORTS – QUICK CHECKLIST

GENERAL ISSUES

Y  N

__ __  1.  IS THE FINAL REPORT PREMATURE?

__ __  2.  IS THE APPROPRIATE FEE BEING REQUESTED?

__ __  3.  IS THE TRUSTEE'S FEE REQUEST IN CONFORMITY WITH UNITED STATES TRUSTEE FEE GUIDELINES?

__ __  4.  HAS THE CASH BEEN MANAGED APPROPRIATELY?

__ __  5.  HAVE APPROPRIATE TAX RETURNS BEEN FILED AND PAYMENTS MADE?

__ __  6.  HAVE SECURED CLAIMS BEEN ADDRESSED?

__ __  7.  IS THE PROPOSED DISTRIBUTION TO CREDITORS CONSISTENT WITH SECTIONS 726 AND 507 OF THE BANKRUPTCY CODE?

__ __  8.  HAVE DUTIES OTHER THAN LIQUIDATION OF ASSETS BEEN PERFORMED?

ISSUES SPECIFIC TO COMPLEX CASES

Y  N

__ __  9.  HAVE ISSUES PECULIAR TO INVOLUNTARY CASES BEEN ADDRESSED?

__ __  10. HAVE ISSUES PECULIAR TO CASES WITH SUCCESSOR TRUSTEES BEEN ADDRESSED?

__ __  11. HAVE ISSUES RAISED BY ESTATE SURPLUS OR INSOLVENCY BEEN ADDRESSED?

__ __  12. HAVE ISSUES ARISING IN CONVERTED CASES BEEN ADDRESSED?