VOLUME 2

CHAPTER 7 CASE ADMINISTRATION

CHAPTER 2-1: THE TRUSTEE PANEL AND TRUSTEE APPOINTMENTS

2-1.0 KEY TERMS

"CAR" means Case Administration Review.

"CFTC" means Commodity Futures Trading Corporation.

"CPA" means certified public accountant.

"EOUST" means Executive Office for U.S. Trustees.

"*Handbook*" means *Handbook for Chapter 7 Trustees*.

"NDR" means trustee report of no distribution.

"Office of the General Counsel" means Office of the General Counsel in the Executive Office for U.S. Trustees.

"PII" means personally identifiable information.

"PDA" means personal digital assistant.

"SEC" means Securities and Exchange Commission.

"SIPC" means Securities Investor Protection Corporation.

"TDR" means trustee distribution report or final account.

"TIR" means trustee interim report, consisting of an Individual Estate Property Record and Report (Form 1), a Cash Receipts and Disbursements Record (Form 2), and a Summary Interim Asset Report (Form 3).

"TIR-RP" means trustee interim report automated review program.

"TFR" means trustee final report.

2-1.1 ESTABLISHMENT OF THE CHAPTER 7 PANEL

The United States Trustee[1] is authorized by law to establish a panel of private trustees. 28 U.S.C. § 586. Members of the panel are appointed by the United States Trustee to serve as interim trustees in chapter 7 cases. 11 U.S.C. § 701(a)(1).[2]

The United States Trustee determines the composition of the panel and may change the size of the panel. In determining the optimum size, the United States Trustee should consider the primary goals of ensuring the prompt, competent, and complete administration of chapter 7 cases and the fair and equitable distribution of case assignments. The United States Trustee should periodically examine the panel and determine if a change in size and composition of the panel is warranted. The size of the panel is largely determined by the number of chapter 7 filings in an area, but geography and other local factors can also influence panel size. The United States Trustee should make every reasonable effort to ensure panel size allows each trustee adequate time to comply with the trustee's duties in each case. The United States Trustee also should maintain the panel in a reasonable size to allow proper supervision. The caseload should be of a size to motivate the trustee and encourage the liquidation of assets. The United States Trustee should avoid any appearance that membership is being limited simply to guarantee the trustees' level of compensation. Providing increased diversity among the panel is also a valid consideration in determining panel size. The United States Trustee should periodically review the size of the panel and the filing statistics to see if a change is warranted.

2-1.2 RECRUITMENT AND ADVERTISEMENT

The United States Trustee shall maintain and conduct an open system for the solicitation of persons interested in serving on the panel of trustees. The United States Trustee should actively encourage broad representation among trustees. To accomplish this goal, the United States Trustee should meet and speak with culturally diverse organizations and community groups to remove real or perceived barriers to participating in the bankruptcy process and to broaden the awareness of opportunities the system affords.

To fill a vacancy on the panel or to expand the panel, the United States Trustee should forward an advertisement and solicitation package to the Office of Oversight together with a memorandum/letter setting forth why additional panel members are necessary. The solicitation package includes a proposed notice, a list

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[1] All references to the United States Trustee shall include the United States Trustee's designee, unless otherwise indicated.

[2] All statutory references herein refer to the Bankruptcy Code, 11 U.S.C. § 101 et seq., unless otherwise indicated.

of non-traditional contacts or sources in the community, and a description of proposed outreach efforts to encourage a diverse pool of applicants. The Program has adopted standard public vacancy notices to attract a diverse pool of qualified applicants. All advertisements must conform to these notices, which may be obtained from the Office of Oversight.

The United States Trustee must send a copy of the advertisement along with a list of proposed publications to the Office of Oversight for review and suggestions. Upon a determination by the United States Trustee, and after review by the Office of Oversight, the Administrative Officer or such other person as the United States Trustee shall designate will place the advertisement with the various publications. The Office of Oversight will post the vacancy announcement on the Program's Website. Local posting of announcements is handled by the United States Trustee. The United States Trustee will also provide information concerning the vacancy to any local professional groups for notice to their membership where possible. All appointments for panel membership are to be advertised for a reasonable period of time.

The United States Trustee must follow the advertising policy set forth herein and avoid making a selection without fully advertising and noticing the opening. If a new vacancy occurs within a reasonably short period of time after the advertisement and posting of a vacancy, the United States Trustee may use that notice to replace the additional vacancy, provided that the information of the previous notice is accurate for the new vacancy. If more than 12 months have passed, the United States Trustee must re-advertise the vacancy. The United States Trustee may re-advertise sooner, if deemed necessary.

2-1.3 QUALIFICATIONS FOR CHAPTER 7 PANEL MEMBERSHIP

The United States Trustee should actively encourage talented, qualified persons, who need not be attorneys, to apply for panel membership. Particular efforts should be made to appoint a panel representative of the diversity of the local community.

2-1.3.1 Qualifications for Panel Membership, 28 C.F.R. § 58.3

The applicant must possess all of the qualifications established by the Attorney General of the United States under 28 U.S.C. § 586(d) and published at 28 C.F.R. § 58.3. Panel members must also be able to satisfy the eligibility requirements of section 321 for serving in a case. Anyone who was employed by the United States Trustee Program within the preceding one-year period is not eligible for appointment. 28 C.F.R § 58.3. Prior to appointment, each person must be interviewed and informed of the performance expected, as well as the method by which that person will be assigned cases.

2-1.3.2 Eligibility to Serve in a Case, 11 U.S.C. § 321

In addition to considering qualifications for panel membership, the United States Trustee should ascertain a candidate's general eligibility to serve in cases. Eligibility requirements are set forth in section 321. Specifically, a trustee must:

1. Be competent to perform the duties of a chapter 7 trustee;

2. Reside or have an office in the district where the cases are pending or in an adjacent district; and

3. Be an individual or a corporation authorized by corporate charter or by-laws to act as a trustee.

While corporations are eligible under section 321 for appointment as interim trustees in specific cases, each individual in a corporation who performs the duties of a trustee must individually satisfy the requirements of 28 C.F.R. § 58.3. In view of the fiduciary duties of the trustee, the responsibility of the individual trustee to preside at meeting of creditors, possible complications as to coverage under blanket or separate bonds, and possible increases in expenses imposed on estates, corporate entities are rarely appointed. The regulation provides that no professional corporation, partnership, or similar entity organized for the practice of law or accounting is eligible for appointment as a chapter 7 trustee.

2-1.4 APPOINTMENT TO THE PANEL

2-1.4.1 Appointment

When the United States Trustee selects a person for appointment to the panel, a security package must be completed and forwarded by facsimile or overnight mail to the Office of Oversight for initial review. After the United States Trustee has confirmed with the Executive Office for U.S. Trustees (EOUST) that the applicant's background investigation package is complete and suitable, the appointment is prepared by the United States Trustee in the form prescribed by the EOUST. If the United States Trustee cannot issue the appointment because of a conflict, the appointment will be issued by the EOUST and signed by the Deputy Director for Field Operations. A copy of the appointment shall be sent to the Office of Oversight.

The Office of Oversight retains a copy of all applications and maintains a roster of all panel members. That office must be notified of any change of name or address of a panel member and of any resignation, removal, or suspension of a member.

The trustee's appointment is subject to the satisfactory completion of an initial and subsequent periodic background checks. The appointment may be suspended or terminated at any time pursuant to 28 C.F.R. § 58.6.

2-1.4.2 Security Clearances

Trustees are appointed to the panel subject to completion of a satisfactory background investigation which includes a name and fingerprint check and a report on credit history. The proposed appointee must submit a Background Questionnaire, Form SF-85P (Questionnaire for Public Trust Positions), Form DOJ-488B (Tax Check Waiver), 2 FD-258 cards (Fingerprint Cards), Form I-9 (Employment Eligibility Verification), Financial Account Release Form, Computer and Software Vendor Release, Optional Form 306 (Declaration for Federal Employment), and Form DOJ-555(a) (Disclosure and Authorization pertaining to Consumer Reports Pursuant to the Fair Credit Reporting Act, 15 U.S.C. § 1681) to the United States Trustee. After the United States Trustee has reviewed the documents for completeness and accuracy, they should be transmitted to the Office of Oversight for final processing. Upon acceptance of the forms, the applicant may be appointed, conditioned on the completion of a satisfactory background investigation. The Office of Oversight will notify the United States Trustee of any background information that requires additional clarification by the trustee applicant. The resolution of questionable information may require an affidavit by the applicant or other clarification.

Panel and non-panel trustees must provide an Update to Background Questionnaire annually. It can be submitted with the trustee's annual Trustee Interim Report, or the United States Trustee may ask all trustees to submit the form annually at the same time.

Panel and non-panel trustees are also subject to reinvestigation every five years or the United States Trustee may request a reinvestigation earlier, if there is a valid reason. The trustees must submit Form SF-85P, Form DOJ-488B, Form 306, Form DOJ-555a, and 2 FD-258 Cards for the reinvestigation. These forms are reviewed and processed following the procedures described above for the initial background check.

2-1.4.3 Term of Appointment

This section has been superseded**.**

2-1.4.4 Renewal of Appointment

This section has been superseded**.**

2-1.4.5 Trustee Performance Review

The United States Trustee must prepare a written performance review at least every two years[3] in the format prescribed by the EOUST. More frequent reviews

[3]Biennial performance reviews are not required for non-panel trustees.

might be appropriate, however, for new trustees or if performance issues arise. A copy of the performance review shall be provided to the trustee and to the Office of Oversight.

The goal of the performance review is to provide information about the trustee's competency, adherence to fiduciary standards, and commitment to pursue assets for the benefit of creditors.

Each trustee is monitored on an ongoing basis by a performance review team designated by the United States Trustee or Assistant United States Trustee. The team and others with trustee supervision responsibility routinely document the trustee's performance in correspondence to the trustee, memos to the file, audits, and other reviews. This information is collected in a trustee oversight file and summarized in the trustee's performance review. See Manual 2-2 for the factors that are covered in the performance review.

2-1.4.6 Suspension and Termination of the Appointment

The United States Trustee shall notify the panel trustee in writing of any decision to suspend or terminate the trustee's appointment to the panel pursuant to 28 C.F.R. § 58.6. The notice shall state the reasons for the decision and should refer to, or be accompanied by copies of, pertinent materials upon which the United States Trustee has relied and any prior communications in which the United States Trustee has advised the trustee of the potential action. The notice must be sent to the office of the trustee by overnight courier, for delivery the next business day, with a copy to the Office of Oversight. The United States Trustee should review the administrative procedures for suspension and termination at 28 C.F.R. § 58.6 and consult with the Assistant Director for Oversight before taking this action to make sure that the notice and reasons are in compliance. The trustee's appeal rights upon notice of suspension or termination may extend the trustee's case assignments unless an interim directive is issued by the United States Trustee.

2-1.4.7 Training

The United States Trustee should develop a training program for new trustees and provide training to all new panel trustees. New trustees should receive thorough training on the *Handbook* and be familiar with the duties of a trustee and the United States Trustee's reporting requirements before being assigned cases. Assigning a mentor for new trustees and allowing a new trustee to observe and talk to panel veterans will aid in acclimating the new trustee. As part of the training process, the United States Trustee should make every effort to attend the trustee's section 341 meetings to provide on-site training and assistance. The United States Trustee should consider assigning the new trustee a reduced caseload during the initial learning process. The United States Trustee should meet with a new trustee periodically during the first year to review case administration, reporting, internal controls, and other matters of concern to the United States Trustee or the trustee.

The United States Trustee also should provide ongoing training for trustees in the following areas:

1. United States Trustee policies and procedures, e.g., preparation of no-asset reports, trustee final reports (TFRs), trustee distribution reports (TDRs), and trustee interim reports (TIRs);

2. Bankruptcy fraud and abuse to include the identification and reporting of potential bankruptcy crimes;

3. Bond and bank depository requirements;

4. Internal accounting controls and the prevention of defalcation of estate funds;

5. Legal issues encountered by trustees;

6. Securing and liquidating assets;

7. Conducting a meeting of creditors;

8. Ethical standards for trustees, including conflicts of interest and the appropriate declination of cases;

9 Diversity; and

10. Other requirements of the *Handbook*.

The United States Trustee should provide at least four hours of training per year for panel trustees in one or more sessions. This training often qualifies for continuing education credit, and the United States Trustee may wish to investigate this possibility. In conducting this training, outside presenters and trustees may provide practical information and are usually well received.

2-1.5 APPOINTMENT AND QUALIFICATION OF INTERIM TRUSTEES

Section 701 of the Bankruptcy Code mandates that the United States Trustee appoint one disinterested panel member to serve as interim trustee in a chapter 7 case immediately after the order for relief. Section 701(a). See Manual 2-1.6.6 regarding the appointment of an interim trustee in an involuntary case.

To qualify to serve, the trustee must furnish a bond in favor of the United States that is conditioned on the faithful performance of the trustee's duties. Section 322. Unless the United States Trustee directs otherwise, a panel trustee covered by a regional or district blanket bond does not have to file a separate bond in each case. See Manual 7-2 for bonding requirements.

The interim trustee serves until a trustee is elected under section 702 and qualifies under section 322. If no trustee is elected, then the interim trustee becomes the trustee under section 702(d). The interim trustee has all the duties and powers of a permanent trustee. See Manual 2-1.6.9 for trustee elections.

2-1.6 ASSIGNMENT OF CASES

2-1.6.1 Blind Rotation

The United States Trustee Program seeks to appoint panel members to chapter 7 cases in a fair and equitable basis by using a single, blind rotation system that includes all asset and no-asset cases. A blind rotation system is a system under which each trustee receives an approximately equal number of cases that are representative of the universe of cases filed, and a debtor cannot time the filing to avoid or select a specific trustee. As cases are filed, they should be assigned to panel members in a manner predetermined by the United States Trustee.

A system of blind rotation avoids the appearance of favoritism and eliminates the need to make individual judgments about case assignments. Over a reasonable period of time, this system normally results in asset cases being fairly and equally distributed among the panel. Because the order of assignment is not available to the public, the blind rotation also reduces the likelihood that debtors can engage in "trustee shopping"–that is, timing the filing of a petition in order to have or avoid a specific trustee appointed in the case. The United States Trustee should review the processing of chapter 7 cases periodically to evaluate the efficiency and fairness of assignment procedures.

Cases converted from chapter 13 to chapter 7 should also be assigned to trustees under a system of blind rotation. Although the predecessor chapter 13 trustee is eligible for appointment, that trustee should not be continued absent consultation and approval by the Office of Oversight.

A trustee serving in chapter 11 is eligible to be continued when the case converts to chapter 7, even if the chapter 11 trustee is not a member of the panel. The United States Trustee should consider the unique circumstances of each case in determining whether to continue the chapter 11 trustee or appoint a trustee from the chapter 7 panel. If the United States Trustee decides to appoint a trustee from the panel, the system of selection should be blind.

2-1.6.2 Exceptions to Rotation

Exceptions to the blind rotation system may be warranted on occasion. Reasons that warrant such exceptions include:

1. The unique characteristics of a specific case, including the conflict of a trustee;

2. The goal of achieving equity in the assignment of cases among panel members;

3. Suspension of a trustee from case assignments;

4. Previous service in a reopened or converted case;

5. Geographic considerations; and

6. Training for new panel members.

Any exception from the rotation system must be recorded and approved by the United States Trustee. A suggested method of recording exceptions is for each office to keep a log of the exceptions to rotation, in addition to any memoranda regarding the individual cases. This log and any other documentation of the exception to blind rotation should be made available for review upon request by a trustee or any interested party or member of the public.

2-1.6.3 Notice and Acceptance of the Appointment

Interim trustees are sent a notice of appointment. A panel member who is covered by a regional or district blanket bond is deemed to have accepted the appointment unless the appointment is rejected within five days after receipt of the notice. If a trustee cannot accept the appointment, e.g., where the trustee has a conflict of interest or was an examiner in the case, then the trustee must expressly reject the appointment. Fed. R. Bankr. P. 2008. See Manual 2-1.6.4.

If the person selected is not covered by a regional or district blanket bond,[4] the trustee shall notify the court and the United States Trustee in writing of acceptance within five days after receipt of the notice of selection or shall be deemed to have rejected the appointment. If applicable, a copy of the trustee's acceptance of appointment should accompany the notice of appointment, so that the form can be filed in the clerk's office. The trustee must also provide a copy of the trustee's bond to the United States Trustee and the court.

[4]Usually the panel trustees will be covered by the regional or district blanket bond, and this may only apply to elected trustees. However, there are other circumstances in which a trustee may not be covered by the regional or district blanket bond, such as a non-panel trustee who was serving in a converted case and is appointed to serve as the chapter 7 trustee.

2-1.6.4 Declination of Appointment

A trustee is expected to accept all cases assigned, unless there is a conflict of interest or other extraordinary circumstance.

A trustee should be familiar with sections 101(4), 101(13), and 701(a), and must decline any appointment in which a trustee has a conflict of interest or lacks disinterestedness. A trustee's timely declination of cases or dockets and the reasons given, as well as a trustee's acknowledgment and evaluation of conflicts of interests, should be in writing and maintained by the United States Trustee for use in evaluating the appropriateness of the trustee's declinations. See Manual 2-1.6.7 for further discussion of conflicts of interest.

2-1.6.5 Non-Panel Trustees in Converted Cases

When a case converts to chapter 7, the trustee administering the case immediately prior to conversion may be appointed by the United States Trustee to serve as the interim trustee, regardless of whether the person is a member of the chapter 7 panel. Section 701(a)(1). Upon conversion of a chapter 11 case in which a trustee was serving, the United States Trustee will assess the advisability of reappointing the chapter 11 trustee to serve as the chapter 7 trustee. The United States Trustee should consider the trustee's performance as the chapter 11 trustee, including compliance with the reporting requirements, and the trustee's ability to carry out the duties of a chapter 7 trustee in the case. Appointing the chapter 11 trustee to serve in the chapter 7 case does not relieve the trustee of the reporting requirements under Fed. R. Bankr. P. 1019, and the United States Trustee should ensure that the trustee complies with this rule.

2-1.6.6 Involuntary Chapter 7 Cases

The United States Trustee should not appoint an interim trustee in an involuntary chapter 7 case until the order for relief is entered. However, if the court orders the appointment of a trustee pursuant to section 303(g), the United States Trustee should appoint an interim trustee in accordance with section 701. If it appears that assets are being dissipated and that an order for relief will be entered, the United States Trustee should consider moving for the appointment of an interim trustee under section 303(g), if the creditors do not.

2-1.6.7 Conflicts of Interest

The *Handbook* contains guidance for the trustees on the conflicts of interest that preclude a trustee from accepting an appointment, as well as the trustee's duty to disclose various matters that might give rise to a conflict to the United States Trustee. The United States Trustee should ensure that trustees comply with their duty as set out in *Handbook Chapter 2.K*.

Fed. R. Bankr. P. 2008 allows the appointment of one trustee in jointly administered cases. The existence of inter-debtor claims in jointly administered cases must be examined closely because such claims do not automatically disqualify the trustee. See, e.g., *In re BH & P Inc.*, 949 F.2d 1300 (3d Cir. 1991). However, these cases should be monitored because conflicts can develop and require the appointment of separate trustees.

In districts in which the standing chapter 13 trustee is also a panel trustee, appointment of the chapter 7 trustee in cases converted from chapter 13 should be monitored so that the chapter 13 trustee is not appointed as the chapter 7 trustee.

2-1.6.8 United States Trustee Serving as Case Trustee

The provisions of 28 U.S.C. § 586(a)(2) and 11 U.S.C. § 701(a)(2) authorize the United States Trustee to serve in a case where no panel member is willing to serve. This situation should rarely occur because the *Handbook* provides that a trustee is not to decline appointments, except for conflicts or other extraordinary circumstances. However, there may be instances, such as a trustee's resignation or possible embezzlement, in which the United States Trustee would need to serve.

If the United States Trustee serves as the case trustee, no bond is required. Section 322(b)(1). Any compensation to which the United States Trustee is entitled will be paid to the clerk of the bankruptcy court and then paid into the United States Trustee System Fund. Section 330(d).

2-1.6.9 Election of Trustees

The election of chapter 7 trustees is covered in some detail in the Bankruptcy Code and Rules. Often the United States Trustee will receive advance warning that an election may be called at a meeting of creditors. In that eventuality, the United States Trustee should be familiar with the rules governing an election and be prepared to preside at the meeting.

2-1.6.9.1 Eligibility to Request an Election and to Vote

Creditors in a chapter 7 case may request the opportunity to elect a trustee at the section 341 meeting. The election is properly requested if creditors having 20 percent in amount of the eligible claims request the election. To request an election and to vote in an election, a creditor must:

1. Hold an allowable, undisputed, fixed, liquidated, non-priority unsecured claim of a kind entitled to distribution under section 726(a)(2)-(4), 752(a), 766(h), or 766(i);[5]

[5]Undersecured creditors may bifurcate their secured and unsecured claims for purposes of requesting an election and voting under section 702. Similarly, creditors with both liquidated and unliquidated claims may assert the liquidated portion of their claims for purposes of determining eligibility

2. Not have an interest materially adverse, other than an equity interest that is not substantial in relation to the creditor's interest as a creditor, to the interest of creditors entitled to distribution;

3. Not be an insider; and

4. Have "filed a proof of claim or a writing setting forth facts evidencing a right to vote pursuant to § 702(a) unless objection is made to the claim or the proof of claim is insufficient on its face." Fed. R. Bankr. P. 2003.

A candidate for trustee is elected if the candidate receives the votes of creditors holding the majority in amount of those claims voted. See section 702 and Fed. R. Bankr. P. 2003.

2-1.6.9.2 Trustee Election Procedure

If an election is requested the United States Trustee presides over the election. This eliminates the possible conflict of the interim trustee presiding while having an interest in the outcome of the election. Neither the Bankruptcy Code nor Rules require creditors to provide any advance notice of an intent to request an election. If the creditors move to elect a trustee during the section 341 meeting without prior notice, the interim trustee adjourns the meeting and notifies the United States Trustee, who shall preside over the election then or at a later date. If the clerk of the bankruptcy court has notified creditors that no proof of claim is required in the case pursuant to Fed. R. Bankr. P. 2002(e), the United States Trustee should consider continuing the meeting of creditors and notifying the creditors of the requested election and of the need to file a proof of claim in order to participate in the election.

The following procedure is recommended. The presiding officer should note for the record:

1. The name of the case;

2. The case number;

3. The date;

4. The names of the creditors requesting an election;

5. The amount of each requesting creditor's claim, whether the claim is documented by a proof of claim or other writing, and whether a written or oral objection has been made to the claim;

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to vote for a chapter 7 trustee. See *In re Klein*, 119 B.R. 971, 981-82 (N.D. Ill. 1990), *appeal dism'd*, 940 F.2d 1075 (7th Cir. 1991).

6. Any individual(s) representing a requesting party;

7. Each nomination for trustee; and

8. Whether there are any objections to the election, identifying the objector and the reason for each objection.

The next critical step is to determine the total amount of general unsecured claims eligible to vote.[6] For this purpose, the total amount of "Unsecured Claims Without Priority" set forth on the summary page of the debtor's schedules should be used. Unless an objection is raised, this total should be the basis from which to determine the 20 percent required for an election. In the absence of schedules, the debtor should provide, under oath, the amount of non-priority, unsecured claims eligible to vote.

In computing the 20 percent quorum, the United States Trustee should give due consideration to information provided by the debtor and creditors as to the unsecured portions of partially secured debts that are to be included, and to unsecured debts that must be excluded from the computation as disputed, unliquidated, due to insiders, or due to one having an interest materially adverse to other creditors, as required by § 702. In any event, the methodology used in determining the total should be reported, along with any objections.

The next step in determining whether the necessary 20 percent of claims has requested an election is to identify each party requesting the election and determine the amount of the claims represented, and, if other persons' claims are represented, assuring that an appropriate affidavit pursuant to Fed. R. Bankr. P. 2006 and supporting proxies are presented. If the presiding officer determines that the 20 percent requisite is not met, the parties are to be informed of that determination. The election process will continue so that the court will have a full report of what transpired or what would have transpired had the 20 percent requisite been met.

If there are objections or disputes that are not resolved by agreement of the parties, the parties should be informed that the election will be held subject to the right of creditors to seek resolution of the underlying dispute by the court.

The presiding officer should then proceed with the election, soliciting from the parties the names of the candidates they wish to nominate. After the nominations,

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[6]There is a difference of opinion as to the determination of the 20 percent threshold. One view is that only 20 percent of the claims that have actually been filed are needed. *In re Lake States*, 173 B.R. 642 (Bankr. N.D. Ill. 1994) *leave to appeal denied*, *Michael v. Fisher*, 185 B.R. 259 (N.D. Ill. 1995). Other cases hold there must be 20 percent of the eligible claims, regardless of whether filed at the time of election. *In re Oxborrow*, 104 B.R. 356 (E.D. Wash.1989), *aff'd*, 913 F.2d 751 (9th Cir. 1990). The United States Trustee should be familiar with the case law of the district in which the election is held.

the presiding officer shall hold a vote for the election of a trustee. The candidate who receives the votes of creditors holding a majority in amount of the claims voted is the elected trustee. The number of creditors voting for or against a candidate is irrelevant, because only the dollar amount of the claims is counted for voting purposes.

The final step is to report the name of the candidate receiving the most votes and to announce that the interim trustee will remain in office until the objection period in Fed. R. Bankr. P. 2003(d) has expired and the elected trustee has qualified. If there are any disputes or objections raised, the presiding officer should announce that the report of the United States Trustee will be delivered to the court as soon as possible following the election. Parties should also be advised that those who complete a sign-up sheet will be provided notice of the United States Trustee's report and that creditors may move, within 14 days after the report is filed, for resolution of any election dispute by the court, as provided by Fed. R. Bankr. P. 2003(d).

The parties should also be informed that if no motion is made to resolve a dispute within the time allowed by Fed. R. Bankr. P. 2003(d), the interim trustee will become the trustee by operation of law.

When the election is concluded, the interim trustee or the United States Trustee may examine the debtor or allow the creditors to examine the debtor. However, the United States Trustee should consider continuing the examination of the debtor until the election report is filed and any election dispute is resolved, so the elected trustee may conduct the examination. Once all parties in interest have had an opportunity to examine the debtor, the meeting should be concluded.

2-1.6.9.3 Voting by Proxy

Voting by proxy at a meeting of creditors is permitted, provided the authority of the agent, attorney, or proxy is evidenced by a power of attorney executed pursuant to Fed. R. Bankr. P. 9010(c). A proxy is a written power of attorney authorizing any entity to vote the claim or otherwise act as the owner's attorney in fact in connection with the administration of the estate. Fed. R. Bankr. P. 2006(c) states that a proxy may be solicited only in writing, and only by:

1. A creditor holding an allowable unsecured claim against the estate on the date of the filing of the petition;

2. A committee elected pursuant to section 705;

3. A committee of creditors selected by a majority in number and amount in claims of creditors (a) whose claims are not contingent or unliquidated; (b) who are not disqualified from voting under section 702(a), and (c) who were present or represented at the meeting of which all creditors having claims of over $500 or the 100 creditors having the largest claims had at

least five days§ notice in writing and of which meeting written minutes were kept and are available reporting the names of the creditors present or represented and voting and the amounts of their claims; or

4. A bona fide trade or credit association, but such association may solicit only creditors who were its members or subscribers in good standing and had allowable unsecured claims on the date of the filing of the petition.

Fed. R. Bankr. P. 2006(d) prohibits solicitation:

1. In any interest other than that of general creditors;

2. By or on behalf of any custodian;

3. By the interim trustee or by or on behalf of any entity not qualified to vote under section 702(a);

4. By or on behalf of an attorney at law; or

5. By or on behalf of a transferee of a claim for collection only.

Before the voting commences at the meeting of creditors, or at any other time as the court may direct, a holder of two or more proxies must file and transmit to the United States Trustee a verified list of the proxies to be voted and the verified statement required by Fed. R. Bankr. P. 2006(e) discussing the facts and circumstances surrounding the execution and delivery of each proxy. On motion of any party in interest or on its own initiative, the court may determine whether there has been a failure to comply with the provisions of Fed. R. Bankr. P. 2006 or any other impropriety in connection with the solicitation or voting of a proxy. After notice and a hearing, the court may reject any proxy for cause, vacate any order entered in consequence of the voting of any proxy that should have been rejected, or take any other appropriate action.

2-1.6.9.4 Election Reports

Whether or not there is an objection to an election, an election report must be prepared by the United States Trustee and filed with the court as soon as possible after the election. Fed. R. Bankr. P. 2003(d). If the election is undisputed, the United States Trustee should file a report of undisputed election and notify the elected trustee of his or her selection and how to qualify for office by posting the requisite bond.

If the election is disputed, the United States Trustee must file with the court a report of disputed election. The United States Trustee cannot resolve any dispute in the election process. Although Fed. R. Bankr. P. 2003(d) does not specify what facts should be contained in the report other than the fact that a dispute exists, Fed. R. Bankr. P. 2003(b)(3) states that "in the event of an objection to the amount

or allowability of a claim for the purpose of voting, unless the court orders otherwise, the United States trustee shall tabulate the votes for each alternative presented by the dispute and, if resolution of such dispute is necessary to determine the result of the election, the tabulations for each alternative shall be reported to the court." Fed. R. Bankr. P. 2007.1(b)(3)(B), which is applicable to chapter 11 disputed elections, is instructive concerning the format of a chapter 7 report and provides that the report should inform the "court of the nature of the dispute, and listing the name and address of any candidate elected under any alternative presented by the dispute." The report of election should be concise and objective, and all relevant documents received at the meeting should be attached as exhibits to the report.

2-1.6.9.5 Disputed Elections

The United States Trustee cannot resolve any dispute in the election process. The United States Trustee, as the presiding officer, must promptly inform the court through an election report that a dispute exists. Pending the resolution of the dispute, the interim trustee shall continue to serve. If no motion for resolution of such election dispute is made within 14 days after the election report is filed, the interim trustee shall serve as the trustee in the case. Fed. R. Bankr. P. 2003(d).

2-1.6.9.6 Qualification of Elected Trustees

The elected trustee is considered qualified once the trustee has returned a notice of acceptance of election, accompanied by a bond. See section 322. Fed. R. Bankr. P. 2008 requires the United States Trustee to notify the person elected concerning how to qualify and the amount of the bond.

2-1.6.9.7 Duties and Responsibilities of Elected Trustees

The statutory duties of an elected trustee are the same as the duties of an interim trustee who becomes trustee by operation of section 702(d). An elected trustee must also comply with the requirements of the United States Trustee and will be requested to submit to a background investigation. If the trustee refuses to submit to a background investigation, the United States Trustee should contact the Assistant Director for Oversight.

The United States Trustee may wish to provide the *Handbook* to the elected trustee, with a letter advising the trustee of the United States Trustee's reporting and other requirements.

2-1.7 SUCCESSOR TRUSTEES – RESIGNATION, REMOVAL OR DEATH

2-1.7.1 General

If a trustee resigns from current cases, is removed, or dies, the United States Trustee should notify the Office of Oversight immediately. The Office of Oversight will consult with the United States Trustee about the need for an audit of the trustee's financial records and case administration, the appointment of a successor, and a protocol for the transfer of bank accounts and other estate assets.

When a trustee dies, resigns, or is removed from a case under section 324, the creditors have a right to elect, in the manner specified in section 702, a person to serve as successor trustee. In the event an election is requested, the United States Trustee should call a special meeting of creditors for the purpose of electing a successor trustee. Fed. R. Bankr. P. 2003(f). The procedures set forth in section 702 must be strictly observed when electing a successor trustee. See Manual 2-1.6.9.2. Any person elected by the creditors must be eligible under section 321 to serve as trustee.

Pending the election of a successor trustee, the United States Trustee should appoint an interim trustee under section 703(b) to preserve or prevent loss to the estate. The interim trustee must be a disinterested person who is a member of the panel of private trustees established under 28 U.S.C. § 586(a)(1).

Section 703(c) provides that if creditors do not elect a successor trustee, or if a trustee is needed in a case reopened under section 350, the United States Trustee shall appoint one disinterested person who is a member of the panel of private trustees established under 28 U.S.C. § 586(a)(1) to serve as trustee in the case. This section appears to apply only if the United States Trustee has not appointed an interim trustee under section 703(b). If creditors do not elect a successor trustee in the manner specified in section 702, the interim trustee appointed under section 703(b) should serve as successor trustee by operation of section 702(d). If creditors elect a successor trustee under section 703(a), the services of an interim trustee appointed under section 703(b) terminate when the successor trustee qualifies under section 322.

2-1.7.2 Death of a Trustee

If a trustee dies, the United States Trustee should, after consultation with the Office of Oversight:

1. Appoint a successor trustee for each of the estates of the decedent trustee, section 703;

2. Ensure that the successor trustee contacts the representative of the decedent trustee's estate;

3. Ensure that the successor trustee obtains any and all books, records, and files of the decedent trustee and files a report of the administration of the estate by the decedent trustee; and

4. Verify that appropriate and timely notices in the case are given to the deceased trustee§s estate. See section 326(c), which limits the aggregate trustee compensation to that available to a single trustee. The United States Trustee should ensure that any dispute between the deceased trustee§s estate and the successor trustee over the division of fees that cannot be resolved fairly and equitably is presented to the court for resolution.

2-1.8 REOPENED CASES

The United States Trustee should not appoint a trustee in a reopened case unless ordered by the court. Fed. R. Bankr. P. 5010. The United States Trustee may move for the appointment or reappointment of a trustee in the reopened case if it appears necessary. The United States Trustee should have in place procedures to monitor motions to reopen cases so that trustees do not resume duties in reopened cases without a court determination that a trustee is necessary in the reopened case. Fed. R. Bankr. P. 5010.

In a reopened case, the United States Trustee may appoint the successor trustee through the blind rotation, but appointing the trustee who previously served in the case is a reason for departing from the blind rotation. If the previous trustee served well in the case, the United States Trustee may wish to reappoint that person as trustee. On the other hand, if there is a concern about reappointing the previous trustee, the United States Trustee may choose to use the blind rotation to appoint a trustee. If the previous trustee is no longer a member of the panel of private trustees, that trustee may not be reappointed in a reopened case.

CHAPTER 2-2: TRUSTEE SUPERVISION AND EVALUATION

2-2.1 GENERAL

The primary functions of the United States Trustee in chapter 7 cases are the establishment, maintenance, and supervision of panels of trustees and the monitoring and supervision of the administration of cases under chapter 7 of the Bankruptcy Code. Accordingly, the goal of the United States Trustee in chapter 7 cases is to establish a system that will allow for the complete, economical, equitable, and expeditious administration of cases, while allowing the trustee to exercise appropriate business and professional judgment in performing the trustee's fiduciary duty.

Trustee supervision is an ongoing process. It requires monitoring the trustee's caseload and the trustee's service as a fiduciary in each case. The standard against which a trustee's performance should be evaluated is found in the Bankruptcy

Code, Bankruptcy Rules, local rules, case law in the jurisdiction, and the *Handbook*. Trustee supervision and performance evaluation take into account the factors described in this chapter, including but not limited to:

1. Civil and criminal enforcement;

2. The trustee's performance in meetings of creditors and in court;

3. The trustee's supervision of professionals;

4. The size and age of the trustee's caseload;

5. The trustee's progress in closing cases;

6. The trustee's maximization of funds distributed to creditors;

7. The accuracy, timeliness, and completeness of the trustee's NDRs, TFRs, TDRs, TIRs, and operating chapter 7 reports;

8. The trustee's procedures for safeguarding estate assets;

9. The trustee's judgment in determining whether to administer assets;

10. The trustee's compliance with banking and bonding policies and procedures;

11. The trustee's cooperation and responsiveness regarding audits, examinations, and reviews;

12. The trustee's conduct in administering the trustee's cases, including dealing with debtors, creditors, attorneys, the court, and the United States Trustee; and

13. The number and nature of complaints against the trustee as well as the trustee's responsiveness in addressing the complaints.

Effective supervision begins when a trustee is assigned to a case and continues throughout the administration of the case. A trustee's performance in each case provides the framework for evaluating the administration of the entire caseload.

The Program's trustee monitoring system collects, integrates, and analyzes information from a variety of sources. A trustee oversight file is created for each trustee and maintained in the local United States Trustee's office by the performance review team. This file should contain the trustee's performance reviews; memoranda concerning remedial actions, if any; and all supporting documentation relied upon to prepare performance reviews or take remedial actions. Supporting documentation includes: correspondence with the trustee

regarding interim reports, final reports and accounts, case closing, and other matters; memoranda summarizing the review of meetings of creditors, court performance, and retention and compensation requests; the results of audits, examinations, or reviews; copies of relevant pleadings; information on objections to discharge and section 707(b) and criminal referrals; public complaints and their disposition; and any other information utilized in support of the performance review or remedial action. The trustee oversight file also must contain all correspondence and documentation in support of the suspension or termination of the trustee's appointment pursuant to 28 C.F.R. § 58.6. See Manual 2-3.

The information in a trustee oversight file is used to prepare a biennial (or more frequent) performance review that documents the trustee's competency, commitment, and integrity in discharging the trustee's fiduciary obligations. The conclusions and recommendations contained in a trustee's performance review must be fully supported by the documentation in the trustee oversight file. The trustee will receive a copy of the performance review and may discuss it with the United States Trustee personally.

Any pattern of case administration that deviates from standards must be brought to the trustee's attention for immediate corrective action. Any written response by the trustee concerning issues raised in the performance review will become part of the trustee oversight file. The trustee oversight file will be made available to the trustee for review, upon request, except for work papers, intra-agency correspondence, and records or information compiled or used for law enforcement purposes. A trustee's request under the Freedom of Information Act for his or her complete file must be in writing and forwarded to the Office of the General Counsel.

Trustee oversight files and case records must be retained and disposed of in accordance with the Program's record retention requirements.

2-2.2 MONITORING TRUSTEE PERFORMANCE AT MEETINGS OF CREDITORS

At least annually, the United States Trustee should select for review cases assigned to each trustee, monitor the section 341 meeting by attending in person or listening to recordings of the meetings, evaluate whether appropriate questions were asked, whether the length of the meeting and thoroughness of the questioning was adequate in view of the nature and complexity of the case, whether irregularities in petitions were identified, and whether the trustee's demeanor toward all parties was appropriate and professional. The reviewer should note whether necessary follow-up deadlines were imposed. The United States Trustee has developed a list of questions required to be asked on the record at the meeting of creditors. See the *Handbook Supplementary Materials*. The trustee must establish on the record that each debtor is aware of the provisions of section 341(d). The results of the review must be documented in writing and retained in the trustee oversight file.

2-2.2.1 Duty to Preside at Meeting

Section 341(a) states that the United States Trustee shall preside at the meeting of creditors. The meeting of creditors provided for in section 341(a) is the official forum where the debtor must appear and answer under oath questions from the trustee, creditors, and other parties in interest regarding the estate. The trustee is the presiding officer at the section 341 meeting as designee of the United States Trustee. The trustee may not delegate the duty to preside at the section 341 meeting. The trustee must seek prior approval, confirmed in writing, from the United States Trustee if the trustee is unable to preside at a scheduled meeting. If the United States Trustee designates another to serve at the section 341 meeting, the trustee is responsible for ensuring that the designated presiding officer is qualified and trained to conduct the meeting. The United States Trustee must confirm that the trustee is presiding appropriately at the section 341 meetings and is not using substitutes without United State Trustee approval.

The United States Trustee should confirm the trustee's compliance with procedures for approving a debtor's alternative appearance at a creditors' meeting when extenuating circumstances prevents the debtor from appearing in person. Extenuating circumstances may include military service, terminal illness, or incarceration. In such instances, a debtor's appearance at a meeting of creditors may be secured by alternative means, such as a telephonic meeting under oath. A trustee may not unilaterally waive a debtor's appearance at the creditors' meeting.

The United States Trustee should also confirm that, when a trustee becomes aware of a debtor's disability, including hearing impairment, the trustee notifies the United States Trustee immediately so that reasonable accommodations can be made. The United States Trustee should have procedures in place to address the special needs of debtors. This includes making arrangements for sign interpreters for debtors. The cost of providing a sign interpreter is paid for by the Program.

The United States Trustee should confirm that the trustee is following Program policy when conducting a meeting for non-English-speaking or Limited English Proficient debtors.

2-2.2.2 Conducting the Meeting

The United States Trustee must confirm that trustees conduct the meeting in an orderly, yet flexible manner, and provide for questioning of the debtor as to matters affecting the debtor's financial affairs and conduct. The trustee's demeanor toward all parties should be appropriate and professional.

The United States Trustee must also confirm that a trustee examines the debtor to the extent appropriate to determine the existence of estate assets, transfers, exemptions, prior filings, possible fraud, abuse, and other matters.

Paraprofessionals, such as a paralegal or a petition preparer, may not sit next to the debtor at the table, advise the debtor, or stand in for the debtor's attorney at the meeting. Representatives of the media are permitted to be present, but no one is permitted to televise, photograph, or electronically record the proceedings other than certified court reporters. Questions by creditors and other parties in interest are allowed. Individuals who represent creditors but who are not attorneys may be present at the meeting. Generally, the trustee should permit these persons to examine the debtor. Some jurisdictions, however, may view this as the unauthorized practice of law. The United States Trustee should instruct the trustee regarding local practices.

The United States Trustee should verify that the trustee refrains from answering questions seeking legal advice during the section 341 meeting and avoids actions that would result in the perception that the trustee is a judge or has judicial power. If an election is requested, the trustee should follow the procedures set forth in Manual 2-1.6.9.

The United States Trustee should also verify that the trustee exercises appropriate control over the demeanor of the debtors, attorneys, and creditors during the course of the meeting. Uncooperative or recalcitrant debtors should be reminded by the trustee of their duties under section 521 and Fed. R. Bankr. P. 4002, especially the duty to cooperate with the trustee in the administration of the estate. Questioning should not be allowed to deteriorate to a level constituting harassment or to focus exclusively on the dischargeability of a particular debt.

All section 341 meetings must be electronically recorded. The trustee is responsible for ensuring that the recording equipment is operating properly. The trustee should announce that testimony is being recorded and must require parties to speak clearly. The spelling of the names of any parties formally entering their appearance on the record should be obtained in case a transcript is requested at a later date.

The United States Trustee should develop a protocol for ensuring appropriate chain of custody for recordings of the section 341 meeting. The United States Trustee also should verify that the trustee records all meetings using equipment provided by the Program and that the recordings are audible. The recordings shall be delivered to the United States Trustee as soon as practicable after the conclusion of the day's meetings. There may be circumstances, such as when a trustee is in a remote location, where it may be appropriate for the trustee to make a copy of the original recording prior to forwarding it to the United States Trustee. Where this occurs, the trustee shall complete a signed affidavit to ensure the integrity of the recording is maintained and fully admissible in a court of law, if required. The recording must be retained by the United States Trustee for two years. Fed. R. Bankr. P. 2003(c).

Depending upon the requirements of the United States Trustee, the trustee also may be required to complete a record of the proceeding, such as a minute sheet, for each case. f required, a copy must be filed promptly with the United States

Trustee and with the clerk of the bankruptcy court, if the clerk so requests. The trustee must retain a copy.

The trustee must administer the oath to each debtor individually, not to the debtors collectively. Pursuant to section 341(d), the trustee must establish on the record that the debtor acknowledges an awareness of:

1. The potential consequences of seeking a discharge in bankruptcy, including the effects that this action may have on the debtor's credit history;

2. The ability to file a bankruptcy petition under a different chapter of the Bankruptcy Code;

3. The effect of receiving a discharge of debts under chapter 7 of the Bankruptcy Code; and

4. The effect of reaffirming a debt, including the debtor's knowledge of the provisions of section 524(d).

This information is contained in the information sheet furnished by the United States Trustee. The trustee must verify on the record that the debtor has received and read the information sheet. If the debtor responds in the negative, the trustee must provide a copy of the information sheet and adjourn the meeting to the end of the calendar or another appropriate time. The meeting cannot be concluded until the information has been conveyed.

If, during the meeting, the debtor asserts the Fifth Amendment privilege against self-incrimination, the trustee should proceed with the questions. At the conclusion of the questioning, the trustee must continue the meeting and must immediately inform the United States Trustee. The United States Trustee will, if appropriate, advise the United States Attorney of the debtor's assertion of the privilege. Authority to seek immunity on behalf of the debtor rests with the United States Attorney and only the district court can grant the request.

2-2.2.3 Rescheduling and Continuances

Continuances of section 341 meetings are not mandated by the Bankruptcy Code and should be granted only under exceptional circumstances. The United States Trustee should instruct trustees regarding the local rules and practices governing debtor rescheduling requests and continuances.

The trustee should not routinely continue section 341 meetings when the debtor appears. If a trustee must continue the meeting, however, the trustee must, if at all possible, announce the continued date to all parties present at the initial meeting and advise the United States Trustee and, if necessary, the clerk of the bankruptcy court, of the continued date.

Any continued or rescheduled meeting should be held before the time for objection to discharge has expired unless the trustee has obtained an extension of time to object to the debtor's discharge. The debtor should not receive a discharge unless the debtor has been examined at the meeting of creditors. If the debtor does not appear at a continued or rescheduled meeting, the trustee should ensure that action is taken for dismissal, unless dismissal would not be in the best interest of the estate.

2-2.2.4 Non-Attendance by Attorneys

When the debtor's attorney fails to appear, the trustee may either continue the meeting or proceed with questioning the debtor. Generally, the better practice is to continue the meeting. In some circumstances, it may be appropriate to proceed, but the trustee should only do so if local law and applicable rules of professional conduct in the jurisdiction clearly permit examination of the debtor.

The unjustified failure of an attorney to appear at the meeting justifies a trustee's motion under 11 U.S.C. § 329(b) to compel a refund by debtor's counsel of compensation received. Repeated unjustified failure to appear should be reported to the United States Trustee.

The United States Trustee should ensure that trustees deal appropriately with unrepresented debtors.

2-2.2.5 Non-Attendance by Debtors

The debtor or, in a case of a partnership or corporation, a designated representative of the partnership or corporation, must attend the section 341 meeting. When spouses have filed jointly, the Bankruptcy Code requires both debtors to be present at the meeting. The United States Trustee should verify the trustee's use of the following remedies for a debtor's failure to appear:

1. Continuing the meeting to another calendar date and notifying the United States Trustee and, if necessary, the clerk of the bankruptcy court, of the new date;

2. Filing a motion to dismiss the case; or

3. Filing an application to designate an individual to perform the duties of the debtor if the debtor is not a natural person. Fed. R. Bankr. P. 9001(5). If that individual fails to appear at the meeting, the trustee should seek an order to compel attendance.

The trustee should inform the United States Trustee of any requests by a debtor to be excused from appearing in person at the section 341 meeting. The United States Trustee should contact the Office of the General Counsel for guidance in order to address such requests properly.

2-2.2.6 Reaffirmation

To combat abuses in the reaffirmation process, the United States Trustee should:

1. Post signs in section 341 meeting rooms notifying debtors concerning the effect of reaffirmation. Example: "Notice: Any agreements to repay debts ARE NOT VALID unless filed with the Bankruptcy Court. Repayment agreements signed by debtors who do not have attorneys ARE NOT VALID unless filed with and approved by the Bankruptcy Court.";

2. Verify that the trustees are orally examining debtors at section 341 meetings as required by section 341(d) to ensure that debtors are aware of, among other things, the effect of reaffirming a debt and the requirements of section 524(d);

3. Prohibit creditors from soliciting reaffirmations, redemptions, or the surrender of property "off the record" in the section 341 meeting room. This would not, however, prohibit the trustee from ensuring that the debtor carried out the debtor's stated intentions under section 521(2)(B); and

4. Seek a disgorgement of fees when debtors' attorneys fail to fulfill their duties under section 524(c). To prevent creating a disincentive to contesting dischargeability actions and to discourage debtors§ attorneys from encouraging reaffirmations to avoid the litigation, the United States Trustee should recognize the attorney's right to a reasonable fee for defending dischargeability complaints.

These steps will enable the United States Trustee to exercise greater control over section 341 meetings, reduce the potential for reaffirmation abuse, and increase the likelihood that debtors will understand the reaffirmation process and the effect of reaffirmation as required by section 341(d).

2-2.3 MONITORING THE SIZE AND AGE OF THE TRUSTEE'S CASELOAD & PROGRESS IN CLOSING CASES

In addition to the discussion in this section, United States Trustee personnel should be familiar with the *Amended Memorandum of Understanding Between the Executive Office for United States Trustees and the Administrative Office of the United States Courts Regarding Case Closing and Post-Confirmation Chapter 11 Monitoring* (AMOU). Many of the time frames and responsibilities vis-a-vis filing final reports were established in the AMOU.

2-2.3.1 No-Asset Cases

If a trustee determines that no meaningful distribution for the benefit of creditors can be derived from a liquidation of the debtor's assets, a report of no distribution

(NDR) is to be filed timely with the court and the United States Trustee. Section 704(9). The United States Trustee must ensure that the trustee's form NDR conforms to the uniform national format prescribed by the United States Trustee Program. The trustee shall file the NDR with the court within 60 days of the section 341 meeting.

A trustee's failure to timely and properly file NDRs should be addressed by an appropriate remedial action.

The United States Trustee should ensure that trustees administer cases whenever a meaningful distribution can be made to creditors, and do not administer cases in which no meaningful distribution is expected.

2-2.3.2 Securing Estate Property

The trustee must promptly secure possession of estate assets and preserve the assets for the benefit of creditors. The United States Trustee should verify that the trustee effectively identifies and inventories assets, and takes appropriate action to control and preserve estate property. See Chapter 4 in the *Handbook*.

The United States Trustee should review notices of abandonment and final reports to determine whether the decision to abandon or not to administer an asset was in the estate's best interest. If no determination can be made on the basis of information supplied, the United States Trustee should require additional information in the notice or final report. The United States Trustee should review abandonments at the earliest opportunity, and, if it appears that the decision to abandon or not administer an asset was not in the estate's best interest, object or take other appropriate action.

The United States Trustee should verify that the trustee takes necessary and appropriate action to abate or prevent environmental contamination by or to estate property. If property of the estate has no value and may be hazardous to the health or safety of the general public, the trustee should give immediate consideration to abandoning property under section 554(a). Before abandoning the property, however, the trustee should take all precautions possible in light of the available assets of the estate and consult with appropriate federal, state, and local authorities.

2-2.3.3 Reviewing Trustee Interim Reports

Section 704(2) and Fed. R. Bankr. P. 2015(a) requires the trustee to be accountable for all property of an estate received by the trustee and to report on the administration of the estate. To properly perform these duties and to effectively administer an asset case, all trustees must use a uniform record keeping and reporting system that has been established by the United States Trustee Program. This system consists of three distinct reports:

1. An Individual Estate Property Record and Report (Form 1);

2. A Cash Receipts and Disbursements Record (Form 2); and

3. A Summary Interim Asset Report (Form 3), referred to collectively as the trustee interim report (TIR).

The instructions for completing Forms 1, 2, and 3 are contained in the *Handbook Supplementary Materials*. Following is a brief description of each Form.

2-2.3.3.1 Form 1

The Individual Estate Property Record and Report (Form 1) provides a blueprint for each asset case. It details all estate assets, both scheduled and unscheduled, and reflects the status of their disposition. It compares the debtor's opinion of each scheduled asset's value, the trustee's estimated net value to the estate for each estate asset, and the actual value realized by the trustee. It also supports the decision regarding administration of each asset. For assets not administered, Form 1 reflects abandonments, whether past or future, formal or informal. For assets administered or to be administered, Form 1 reflects amounts realized and the anticipated remaining value of assets not completely liquidated.

Form 1 must be prepared and maintained for each case that is either expected to be or declared to be an asset case by the trustee, each case in which the trustee has received funds of the estate, and each case in which an NDR has not been filed and 120 days have passed since the initial examination of the debtor at the section 341 meeting. All assets of the debtor must be listed from the petition, schedules, and statement of affairs. All unscheduled assets identified by the trustee also must be recorded.

In a case converted from another chapter, assets reported in the final report required by FRBP 1019(5), or in any schedules submitted post-conversion, should be listed. If no such report or schedules are filed, the assets remaining in the case are to be listed. Form 1 should list all property of the estate not administered by the prior trustee or debtor in possession, as well as the funds on hand at the time of conversion. The trustee should maintain a record in the estate file describing how the assets listed on Form 1 were determined. To create this record, the trustee could annotate the original schedules to indicate which assets remained at the time of conversion.

If the trustee is serving as a successor trustee in a chapter 7 case, Form 1 should account for all property listed on the debtor's original and amended schedules and statement(s) of financial affairs, as well as any assets identified by the prior and successor trustees that were not listed by the debtor. The partial or full administration of assets by the prior trustee should be explained in Notes to Form 1 or under Major Activities Affecting Case Closing. Sample Case #2 in the *Handbook Supplementary Materials* illustrates this Form 1 presentation.

2-2.3.3.2 Form 2

The Estate Cash Receipts and Disbursements Record (Form 2) is a combination checkbook/journal. A separate Form 2 is maintained for each checking account, money market account, savings account, and/or Certificate of Deposit that is opened on behalf of the bankruptcy estate. It shows all receipts, disbursements, and bank account transfers for each account. All transactions must be entered on Form 2, in chronological order, as soon as they occur. The trustee should not wait and enter transactions from the monthly bank statements. No Form 2 is necessary until the bank account is opened.

If the trustee is serving in a case converted from another chapter, Form 2 should begin with the balance turned over by the previous trustee or debtor in possession.

If the trustee is serving as a successor trustee in a chapter 7 case, the trustee must ensure that prior trustee's bank accounts are closed and new accounts are opened in the successor trustee's name. The Form 2 for the new account(s) should begin with the balance turned over by the previous trustee, thereby remaining consistent with the successor trustee's bank statements. The successor trustee should obtain a download of the prior trustee's Form 2 data, when available. This will help the successor trustee prepare an accurate and complete data-enabled TFR and TDR when the case is ready to be closed. Sample Case #2 in the *Handbook Supplementary Materials* has been added to illustrate how a successor chapter 7 trustee should prepare Form 2.

2-2.3.3.3 Form 3

Form 3 lists all pending cases expected or declared to be asset cases by the trustee, all cases in which the trustee has received funds of an estate, and all cases in which an NDR has not been filed and 120 days have passed since the initial examination of the debtor at the section 341 meeting. Cases are entered in sequence by case number. Many of the entries on Form 3 are made from Form 1 and Form 2.

2-2.3.3.4 Chapter 7 Trustee Reporting Requirements

A trustee is required to submit Form 3 at least once every year, unless the United States Trustee requires that it be submitted more frequently. In addition to Form 3, a trustee must submit Forms 1 and 2 for each pending case unless:

1. A TDR was submitted for an asset case during the current or prior reporting period;

2. A TFR was submitted for an asset case during the current or prior reporting period;

3. A final report was filed for an asset case that was converted, dismissed, or reassigned during the current reporting period; or

4. An NDR was filed for an asset case during the current reporting period.

Such cases need only be listed on Form 3.

See *Handbook Chapter 5 and the Supplementary Materials*.

The trustee must submit the TIR within 30 days of the end of the reporting period. If a trustee cannot submit the TIR by the due date, the trustee should obtain a date-specific extension in writing from the United States Trustee prior to the deadline.

Fed. R. Bankr. P. 2012(b) requires a successor trustee to file with the court and transmit to the United States Trustee an accounting of the prior trustee's administration of the estate. This accounting must be a separate and distinct record of the activities that were solely within the control of the prior trustee. The Fed. R. Bankr. P. 2012(b) accounting ultimately may be the basis of a criminal investigation, surcharge of the prior trustee, or suspension or termination of the prior trustee's appointment, or the basis for an award of compensation to a decedent's estate. The rule does not have a deadline for submitting the accounting. Absent some evidence of defalcation or other harm to the estate, the accounting can be provided in conjunction with the submission by the successor trustee of the standard reports required by the United States Trustee.

2-2.3.3.5 Review by United States Trustee

The TIR provides information concerning a trustee's financial management, internal controls, organizational effort, and legal administration of the cases in which the trustee serves. The United States Trustee must complete the review of the TIR within 60 days of receipt, utilizing the TIR automated review program known as TIR-RP, and issue a written report to the trustee. The trustee must respond with 21 days.

The purpose of this review is to ensure adherence to fiduciary standards in the administration of the chapter 7 caseload. Particular emphasis should be given to the trustee's zeal and diligence in identifying, pursuing, and recovering assets for the benefit of creditors; timeliness in closing cases; compliance with reporting and other requirements of the United States Trustee; and performance of the trustee's responsibilities pursuant to section 704. Correspondence to and from the trustee documenting issues raised is part of the trustee oversight file. The TIR reports and related review notes may be retained separately.

Any major problems that surface in the review process must be discussed with the trustee. Trustees who are deficient in their administration of cases will be subject to a wide range of compliance measures by the United States Trustee or the court.

When a TIR will be subject to an independent audit, the TIR review conducted by the United States Trustee is limited to a review of Form 3 utilizing the TIR-RP. When the TIR is reviewed as part of a United States Trustee Field Examination, the field examination procedures are followed rather than the TIR review procedures. Audits and examinations are discussed at Manual 2-2.7.

2-2.3.4 Monitoring Operating Chapter 7 Cases

Under section 721, the court may authorize a trustee to operate the business of a debtor for a limited period of time. In order for the court to grant such a request, two basic requirements must be met. First, operation of the debtor's business must be in the best interest of the estate. Second, such operation must be consistent with the liquidation of the estate. Prior to seeking authority from the court to operate the business, the trustee must consult with the United States Trustee to discuss the nature of the operation, cash management controls, and the appropriate monthly operating business report form required by section 704(8).

If it is apparent that the estate would benefit from an extended period of operation, the United States Trustee should encourage the trustee to file a motion seeking conversion of the case to chapter 11 under section 706(b), and requesting the appointment of a chapter 11 trustee pursuant to section 1104(a). The trustee should determine whether a proposed plan of liquidation could satisfy the requirements of confirmation under section 1129. If so, and the trustee fails to request conversion of the case and the appointment of a chapter 11 trustee, the United States Trustee should take appropriate action to do so.

2-2.3.4.1 Review of Monthly Operating Reports by the United States Trustee

The United States Trustee should review the monthly operating report within 15 days of receipt to determine the adequacy of the trustee's bond; the proper and timely administration of the case; and the possibility of the sale of the business as a going concern or, in the alternative, conversion of the case to allow reorganization under chapter 11. Written notice of deficiencies or problems with a monthly operating report should be given to the trustee immediately upon review by the United States Trustee, along with deadlines for corrective action or additional information.

If a trustee fails to file the reports required by section 704(8) or if the reports demonstrate a loss to the estate, the United States Trustee should seek an order terminating the trustee's authority to operate the business or seek removal of the trustee if continued operation is in the estate's best interest.

Even when the court finds operation of a business will increase the estate's value without endangering the estate's assets, the trustee should seek to operate the business for the shortest practical period. The trustee should close the case, liquidate the business, or convert the case to a chapter 11 within a reasonable time – normally not to exceed one year from entry of the order authorizing the operation of the business.

Trustees who are deficient in their administration of operating cases will be subject to a wide range of compliance measures by the United States Trustee or the court.

If the trustee fails to maintain an adequate bond or file the requisite operating reports, or the reports demonstrate a loss to the estate, and the efforts of the United States Trustee to persuade the trustee to remedy these deficiencies or any others affecting the integrity of the administration of the case are not successful, then the United States Trustee should seek an order terminating the trustee's authority to operate the business or seek removal of the trustee if continued operation is in the estate's best interest.

2-2.3.5 Monitoring Case Progress

Section 704(1) provides that a trustee shall "close [an] estate as expeditiously as is compatible with the best interests of parties in interest." Delays in case closing diminish the return to creditors, undermine the creditors' and public's confidence in the bankruptcy system, increase the trustee's exposure to liability, raise the costs of administration, and expose the debtor to increased penalties and interest in cases involving non-dischargeable pre-petition tax liabilities. Delays also give rise to public criticism of the bankruptcy process.

In order to ensure that a trustee complies with the duty to close cases expeditiously under § 704(1), the United States Trustee monitors the number and age of open cases and the reasons they remain open. For United States Trustee reporting purposes, an "old" case is one that has been open more than three years. The United States Trustee will give heightened scrutiny to a trustee's administration of cases and should consider remedial actions when a trustee has an excess of old cases or is not expeditiously administering or closing cases. Traditionally, if the trustee's old cases were 10 percent or more of the trustee's total cases, this was viewed as an indicator of an excess of old cases, but the United States Trustee must consider the percentage of old cases, the number of old cases, general case progress, and other relevant factors in determining whether the trustee has an excess of old cases or is not expeditiously administering or closing cases.

The Office of Oversight provides quarterly caseload reports that show, by trustee, the number of cases open longer than three years and the age of the trustee's entire open caseload.

The United States Trustee must periodically review the processing of chapter 7 cases by field offices. The areas to be evaluated include:

1. The efficiency and fairness of the United States Trustee's intake and assignment procedures for new cases;

2. The efficiency of the case closing process, including the timely filing of final reports by trustees and the review conducted by the United States Trustee's office;

3. The impact of local rules of the court or local customs on efficient case administration;

4. The adequacy of the regional or district blanket bond and separate bond procedures; and

5. The educational and training needs of panel members.

Corrective actions should be taken to improve any areas of weakness. The United States Trustee should also work through proper channels, e.g., the local bar, the clerk of the bankruptcy court, or the chief judge of the bankruptcy court, to improve communications and other identified problems.

2-2.3.6 Reviewing Trustee Final Reports (TFRs)

When a case is ready to be closed, a chapter 7 trustee must prepare and file a final report (TFR) with the United States Trustee for review before it is filed with the court. The United States Trustee must ensure that the TFR used by the trustee conforms to the uniform national format prescribed by the Program. The uniform TFR is a data-enabled form that is submitted to the United States Trustee electronically. The United States Trustee is encouraged to review it electronically and not require the trustee to submit it in paper form.

The TFR is signed by the trustee under penalty of perjury and certifies that all assets have been liquidated or properly accounted for and that funds of the estate are available for distribution. The trustee's signature in the data-enabled TFR appears as "*s/John Doe, Trustee*." The procedures for maintaining a trustee's wet signature for the TFR are established according to local court rules.

The TFR must be prepared as soon as all monies have been collected, all claims have been reviewed or determined by the court, and the bar date has expired for creditors to file claims. The report must be filed prior to any distribution of funds to creditors, unless the court has previously ordered an interim distribution. In any event, the TFR must be filed before final distribution of all funds in the case. See Fed. R. Bankr. P. 5009.

All outstanding applications for professional compensation and expenses should be filed along with the TFR. The TFR enables the United States Trustee and any other party in interest to determine how the trustee proposes to disburse estate funds.

Generally, estate funds should be maintained in an interest-bearing account until the trustee is ready to distribute the funds to creditors. The difference between the distribution as calculated in the TFR and reported in the TDR should be footnoted in the TDR. No amended TFR should be filed. The trustee may receive a fee on the increase, if authorized by the court although many trustees waive the extra fee. If the balance of estate funds on hand is less than $5,000, the trustee has the discretion to move the funds to a non-interest bearing account when the TFR is filed with the United States Trustee. This amount may be adjusted at the United States Trustee's discretion. If there is a substantial delay in approval of the TFR, the trustee is expected to reinvest the funds, in accordance with the trustee's duty to maximize the return to creditors. Funds should not be invested after the final tax return is prepared if the cost of preparing an additional tax return would exceed the interest earned. Normally, this situation will be an issue only for corporate or partnership cases.

The TFR must set forth the distributions to be made under section 726. The United States Trustee must ensure that the trustee has distributed estate funds in the priority set forth in that statute.

The United States Trustee must review each TFR within 60 days of receipt to assess whether the trustee has properly and completely administered estate property. Deficiencies in the trustee's administration or other problems or mistakes will be brought to the trustee's attention for corrective action.

Upon completion of this review, the United States Trustee will file the TFR with the court. If there is a dispute between the United States Trustee and the trustee concerning the report, the TFR will be filed with an objection and the dispute resolved by hearing before the court. Concurrently with filing the TFR, the United States Trustee enters a certification on the docket indicating that the United States Trustee has reviewed the TFR and applications for compensation.

Under Fed. R. Bankr. P. 2002(f), the trustee is required to notice all creditors with a summary of the final report before making the distribution to the creditors, in cases where the amount to be distributed is $1,500 or more. The United States Trustee must ensure that the notice of final report (NFR) conforms to the uniform national form prescribed by the United States Trustee Program.

If no objections are lodged to the NFR, the trustee may make the distribution according to the final report.

2-2.3.6.1 Distribution

As part of the TFR review, the United States Trustee approves the trustee's proposed distribution of funds. Court orders are necessary prior to payment of trustee and professional fees and expenses and to resolve claims objections, but are not necessary for the general distribution of funds to creditors, absent any other objections to the trustee's final report. If no objections are filed, the trustee should immediately make disbursements upon the entry of any appropriate court order(s) and after any applicable appeal period has expired. Fed. R. Bankr. P. 3009. If the court modifies the fees and expenses, the trustee's revised dividend distribution report must be reviewed by the United States Trustee within 10 days of receipt. The final distribution to creditors must be paid within 30 days of the entry of the final orders on compensation and expenses.

The trustee may encounter a situation in which a creditor refuses a dividend payment because the debt was previously paid. Depending on the amount of any returned payments, the number of other creditors otherwise receiving distributions, and local court policy or procedure, the trustee may be required to redistribute returned funds to the other creditors. Because a supplemental distribution normally will occur prior to the submission of the TDR, the supplemental distribution should be included as part of the United States Trustee's review of the trustee's TDR.

Typically, distributions are made at the end of the case, but limited circumstances sometimes support an interim distribution to creditors. Interim distributions should occur only after claims are resolved and sufficient assets have been reserved to administer the estate. The United States Trustee must review and approve the trustee's proposed interim distribution of funds.

2-2.3.7 Reviewing Final Accounts/Trustee Distribution Reports (TDRs)

Within 125 days after the entry of an order allowing final compensation and expenses, a trustee must submit a TDR to the United States Trustee for review. The United States Trustee must ensure that the TDR used by the trustee conforms to the uniform national format prescribed by the Program. The uniform TDR is a data-enabled form that is submitted to the United States Trustee electronically. The United States Trustee is encouraged to review it electronically and not require the trustee to submit it in paper form.

The trustee signs the TDR under penalty of perjury certifying that the estate has been fully administered. Fed. R. Bankr. P. 5009. The trustee's signature in the data-enabled TDR appears as "*s/John Doe, Trustee*." The procedures for maintaining a trustee's wet signature for the TDR are established according to local court rules.

The United States Trustee must establish a procedure to monitor the timeliness of final distributions and the filing of TDRs.

The original bank statement(s) showing a zero balance and all original canceled checks, except those already submitted with the TFR, must be attached to the TDR. The trustee must certify that all funds have been disbursed consistent with the distribution report and that all checks have been negotiated or any remaining checks have been paid into the court and that the estate has been fully administered. Under section 347, if any checks remain outstanding 90 days after the final distribution, the trustee must stop payment on the checks and pay the monies into the Bankruptcy Court Registry Fund as unclaimed funds pursuant to Fed. R. Bankr. P. 3011. However, the trustee should make a good faith attempt to locate the creditors and re-issue the checks prior to submitting funds to the court registry.

The TDR is to be submitted to the United States Trustee, who must review it within 30 days of receipt. If any problems or discrepancies are detected, follow-up action should be taken. Once the reviewer is satisfied the distributions have been made properly by the trustee and that the TDR is correct, the TDR should be filed with the clerk of the bankruptcy court by the United States Trustee. The United States Trustee must enter on the docket a statement that the TDR has been reviewed and the United States Trustee has no objection to relief requested. If there is no timely objection by the United States Trustee or other party in interest, there shall be a presumption that the estate has been fully administered and the court may close the case.

Unless the clerk of the bankruptcy court requires custody, the canceled checks and zero bank statement may be retained by the United States Trustee or returned to the trustee. The bank statements and canceled checks must be retained for the two-year period specified in section 322(d), or as otherwise required by the Internal Revenue Service, whichever period is longer.

2-2.4 MONITORING TRUSTEE LEGAL ADMINISTRATION, PERFORMANCE IN COURT, AND SUPERVISION OF PROFESSIONALS

The United States Trustee reviews the trustee's employment and supervision of counsel, and management of litigation and legal issues. As part of that review, attention should be given to litigation analysis, the cost-benefit analysis of legal work and cause(s) of action, the control exercised over fees and expenses, and the quality of legal services rendered.

The United States Trustee, as part of the review of the trustee's legal administration, may attend court hearings in which the trustee or trustee's counsel appears. Special attention should be paid to the preparation, demeanor, and professional quality of legal service or presentation. The United States Trustee's review of the trustee's selection and monitoring of counsel for the trustee, pleadings drawn, and court performance of counsel shall be documented in writing.

2-2.4.1 Pleadings

The United States Trustee should review a trustee's pleadings for timeliness, sufficiency, and necessity. Pleadings to be scrutinized include employment applications, professional fee applications, motions to sell assets, motions to abandon assets, objections to exemptions, objections to discharge, and adversary complaints. All applications for fees are to be prepared in compliance with the *Guidelines for Reviewing Applications for Compensation and Reimbursement of Expenses*.

2-2.4.2 Court Performance

The United States Trustee should routinely observe a trustee's court appearances. Special attention should be paid to the preparation, demeanor, and professional quality of legal service or presentation. Findings should be documented in the oversight file.

2-2.4.3 Retention and Compensation of Professionals

The United States Trustee reviews the trustee's selection and monitoring of professionals. The employment must be appropriate under the circumstances of the case. The United State Trustee should scrutinize employment applications to determine whether the services of a professional are needed and the cost is warranted. The United States Trustee should also determine at the outset the level of professional work required and the estimated costs and benefits associated with the work. Routine employment of professionals and the use of boilerplate language justifying the employment should not be allowed. If there is any question as to the necessity for legal or accounting services, the United States Trustee should object to the employment application. A form application to employ the trustee as a professional in every case without specifying the necessity for the services to be provided is subject to an objection by the United States Trustee.

The employment application should evidence that the trustee analyzed the litigation or other work to be performed and determined the costs and benefits of the work prior to employing the professional. The United States Trustee should review pleadings, documents, or reports drawn by the trustee's professionals, and attend court hearings in which the trustee's professionals appear so that an assessment of the professionals§ preparation and demeanor as well as the professional quality of the service or presentation can be made. The trustee may not delegate his or her section 704(b) decision making authority to professionals. The trustee's efforts to achieve greater diversity among the professionals employed should be determined.

The United States Trustee reviews the trustee's exercise of control over fees and expenses of professionals. The compensation request should evidence the

trustee's determination that the professional has provided quality professional services, the requested fees and expenses are reasonable, and the work was effective. The trustee's approval of the compensation request must be evident in the compensation request. See *Guidelines for Reviewing Applications for Compensation and Reimbursement of Expenses*, Section II, A.5. Professional fee applications must not include time spent on trustee duties; expense requests must include only actual and necessary expenses. The trustee must be effective in negotiating reductions or filing objections to fee applications, when appropriate.

When the trustee employs an auctioneer, the trustee must ensure that the auctioneer is adequately bonded, prior to taking possession of estate property, in an amount that is sufficient to cover all receipts from the sale. The bond should be in favor of the United States of America and is distinct from any other auctioneer's bond required under state law. The amount of the bond will be established by local bankruptcy rule or the United States Trustee. The trustee should contact the United States Trustee to ensure that the auctioneer is bonded in an appropriate amount to cover all estates in which the particular auctioneer has been employed. All original bonds should be forwarded to the United States Trustee. The trustee also should determine if the auctioneer maintains insurance for lost or stolen property, since the trustee may wish to make a claim against the insurer for any such losses.

When the auctioneer assumes control over estate property for a period of time prior to sale, the trustee should keep an inventory of the items stored and periodically verify that the assets still exist and are in good condition. Insurance claims for lost or stolen property should be made promptly, and the trustee should inform the United States Trustee of such claims.

The United States Trustee should object to any application to employ an auctioneer if the trustee fails to comply with the foregoing. A representative of the United States Trustee should periodically attend auctions to ensure that the sales are conducted in a proper manner and are free from coercion or other irregularities.

The United States Trustee should also review the trustee's application for the trustee's own compensation. Section 330(a)(7) provides that the trustee fee is to be "treated as a commission." Absent extraordinary factors, the United States Trustee will not object to a trustee receiving the full statutory commission on all "moneys disbursed or turned over in the case by the trustee to parties in interest, excluding the debtor, but including holders of secured claims." Extraordinary factors are expected to arise only in rare and unusual circumstances and include situations such as where the trustee's case administration falls below acceptable standards or where it appears a trustee has delegated a substantial portion of his or her duties to an attorney or other professional.

Section 331 permits a trustee to apply to the court for interim compensation or reimbursement of expenses pursuant to section 330. Section 326(a) provides a cap

on the trustee's compensation based upon all funds disbursed by the trustee. A literal reading of section 326 requires that a trustee receive compensation only after a disbursement to parties in interest. Nonetheless, a line of cases has developed that allows interim reasonable compensation to trustees in certain circumstances, although distribution may not have been made to any creditor. The United States Trustee should carefully examine a trustee's request for interim compensation and object as warranted.

The United States Trustee should ordinarily object to a trustee's application for interim compensation unless the application is linked to an interim distribution to creditors. However, when a trustee is heavily engaged in the administration of a case over an extended period of time and the trustee is providing substantial services to the estate, those factors may present good cause for interim compensation to the trustee.

2-2.5 BANKING AND BONDING

The United States Trustee must ensure that the trustee banks with a depository that has entered into a Uniform Depository Agreement with the United States Trustee to provide collateral for uninsured deposits. The trustee's banking responsibilities are covered in *Handbook Chapter 5.E*, and the United States Trustee's responsibilities to monitor a trustee's banking are covered in Volume 7 of this Manual. The United States Trustee also must ensure that the trustee is adequately bonded. The United States Trustee's responsibilities to monitor a trustee's bond are covered in Manual Volume 7.

2-2.6 STATISTICS: CASELOAD AND DISTRIBUTIONS TO CREDITORS

Caseload and distribution statistics for chapter 7 trustees are collected and maintained by the EOUST. The statistics are used by field offices, regional offices, and the EOUST to determine whether cases are administered competently and expeditiously by a trustee. Both caseload statistics and closed case distribution statistics are an integral component of the trustee's performance review.

2-2.6.1 Caseload Statistics

The following statistical information should be reviewed for each trustee on a quarterly basis: the number of chapter 7 no-asset cases pending 120 days or more after the date when the section 341 meeting was held; the status of final reports and final accounts; and the asset and no-asset caseloads.

The EOUST will provide the United States Trustee with quarterly caseload statistics.

2-2.6.2 Distribution Statistics

Statistics from chapter 7 closed asset cases have been collected since 1994. Publicly available statistics can be found on the Program's Website. The statistics are also compiled for trustee oversight purposes.

2-2.7 AUDITS, UST FIELD EXAMINATIONS, AND CASE ADMINISTRATION REVIEWS

Independent audits by Certified Public Accountants (CPAs), UST Field Examinations (field exams), and Case Administration Reviews (CARs) provide information concerning a trustee's financial management, internal control procedures, organizational support, and legal administration of cases.

The trustee is subject to an audit or field exam at least once every four years. An audit conducted by an independent auditor selected by the EOUST must occur at least once every eight years. Thus, during an eight-year cycle, every panel trustee who administers a chapter 7 estate will receive at least one audit conducted by the independent auditor and at least one field exam conducted by the United States Trustee, unless a second audit is performed in lieu of the field exam.

Non-panel and elected trustees may be included in the audit/field exam cycle when warranted. At the United States Trustee's discretion, however, an audit or field exam may be waived if the non-panel trustee's few remaining cases will be closed within a short period. Key factors to be considered are the number and age of the cases, the amount of funds on hand, and the possible benefit to be derived from the audit/exam.

In addition to the audits and examinations, CARs may be conducted by the United States Trustee when deemed necessary or appropriate by the United States Trustee. The United States Trustee also meets annually with the trustee in a trustee conference.

2-2.7.1 Independent Audits

Independent audits are designed to identify a trustee's internal control weaknesses in case administration and cash management practices. Prior to the audit, the United States Trustee should communicate any concerns about the trustee to the auditor.

An audit will contain one of the following three opinions:

1. "Adequate;"

2. "Adequate Except For" noted deficiencies; and

3. "Inadequate."

Audit deficiencies noted as consequential require special consideration. Consequential deficiencies indicate potential for fraud, are serious internal control weaknesses, or are chronic, repeat deficiencies.

At the conclusion of an audit, the auditor will conduct an exit conference with the trustee. The United States Trustee should attend the conference to determine the appropriate remedial actions that may be necessary. A written report of the results of the audit is issued to the United States Trustee within 60 days of the exit conference. The United States Trustee forwards a copy of the report to the trustee and requests a written response within 21 days of the date of the written audit report, confirming that corrective action has been taken and changes implemented. Whenever an audit report contains a consequential finding or a series of less consequential findings, an on-site visit to the trustee's office must be made to verify compliance within six months of the trustee's response.

An audit should be closed within six months from the date of the audit report. A written request that the audit be closed must be submitted by the United States Trustee to the Office of Oversight regardless of whether deficiencies were noted. When deficiencies have been noted, and the United States Trustee has determined that a trustee has corrected all noted deficiencies, the audit closure memorandum should contain a written recommendation from the United States Trustee to close the audit, a description of an on-site visit or other action taken to verify that all deficiencies were corrected, the trustee's response addressing each noted deficiency, and all relevant documents supporting the United States Trustee's recommendation.

Refusal by the trustee to implement the necessary changes should be reported to the Assistant Director for Oversight and the Deputy Director for Field Operations, with a recommendation as to the appropriate enforcement action.

2-2.7.2 UST Field Examinations (Field Exams)

Field exams are conducted by the United States Trustee. The field exams are designed to identify whether the trustee's accounting and cash management practices are adequate to safeguard estate assets. Written notice of deficiencies and required changes with deadlines for implementation must be provided to the trustee and to the Office of Oversight. A written response to the report is required from the trustee within 21 days. Whenever a field exam report notes a consequential deficiency or a series of less consequential deficiencies, a visit to the trustee's office should be made to verify compliance. The field exam report, along with the trustee's response, must be maintained in the trustee oversight file. Appropriate remedial action should be taken by the United States Trustee for failure by the trustee to correct noted deficiencies or to meet deadlines set forth in the report. All post-field exam activity and closure should be concluded within six months. Closure is achieved by submitting the United States Trustee's memorandum or letter to the Office of Oversight explaining how each deficiency

has been resolved, including the trustee's response to each deficiency, and requesting closure.

2-2.7.3 Consequential Deficiencies

Both audits and field exams may report deficiencies that are considered consequential. These types of deficiencies require special consideration. The United States Trustee Program defines consequential deficiencies as those deficiencies that indicate the potential for fraud, are serious internal control weaknesses, or are chronic, repeat deficiencies, in contrast to deficiencies that are ministerial in nature. When an audit contains one or more consequential deficiencies, there are certain requirements for resolving each deficiency, one of which is that the trustee's audit response must include appropriate documentation demonstrating correction of the deficiencies.

Depending upon the number and severity of the specific audit deficiencies, the United States Trustee will visit the trustee's office to verify the trustee's corrective actions. Follow-up office visits are required when:

1. An audit or examination contains certain consequential deficiencies;

2. Correction of a consequential deficiency, or a series of less than consequential deficiencies, cannot be verified by examining the documentation submitted with the trustee's response to the audit or examination report; or

3. Due to the nature of the consequential deficiency, or series of less than consequential deficiencies, correction can be verified only at the trustee's office.

2-2.7.4 Inadequate Audit Opinion or UST Field Examination Conclusion

A trustee who receives an inadequate audit opinion from the auditor or an inadequate conclusion from a UST Field Examination will be suspended from active rotation, in accordance with the Administrative Procedures found at 28 CFR § 58.6(d). The trustee will receive written notice of the suspension pursuant to the Administrative Procedures, and an interim directive requiring immediate suspension of case assignments may be issued, if the circumstances under section 58.6(d) exist. Reinstatement of the trustee requires the approval of the Deputy Director for Field Operations. Prior to reinstatement, the trustee shall provide evidence that the necessary corrective actions were implemented. The United States Trustee shall review the trustee's response and make an on-site visit to the trustee's office to verify compliance. To expedite the trustee's reinstatement, the audit or examination closure memorandum sent to the Assistant Director for Oversight should state that reinstatement is requested. The Assistant Director for Oversight will forward the request to the Deputy Director for Field Operations with a recommendation.

If the United States Trustee believes that the inadequate audit opinion or examination conclusion is unwarranted because of factual inaccuracy, a mistake in judgment, or another reason, the United States Trustee should immediately notify the Assistant Director for Oversight to request advance approval from the Deputy Director for Field Operations for the trustee to remain on rotation. The United States Trustee will need to provide written documentation in support of retaining the trustee on rotation and may be requested to visit the trustee's office to determine the advisability of keeping the trustee on rotation. The Assistant Director for Oversight will review the documentation and forward a recommendation to the Deputy Director for Field Operations, who will determine whether the suspension will be waived.

2-2.7.5 Case Administrative Reviews (CARs)

The CAR is discretionary; it may be conducted if, and whenever, the need arises. A CAR addresses issues that include the trustee's pursuit of assets, filing of objections, closing of cases, compliance with laws and United States Trustee requirements, and all other matters relevant to a case. At the discretion of the United States Trustee, the CAR may also incorporate internal control reviews and testing that go beyond the scope of a field exam.

When appropriate, the trustee will receive a written notice of deficiencies with deadlines for implementing corrective actions. The trustee should provide a written response to the United States Trustee within 21 days of the date of the written notice. The United States Trustee may arrange a follow-up visit or accept documentation to verify implementation of the corrective actions described in the trustee's response.

2-2.7.6 Trustee Conferences

The United States Trustee will meet with each trustee no less than once a year. The substance of the trustee meeting should be directed to any area that the trustee's oversight file indicates may call for attention. The trustee meeting should include a review of the trustee's performance in case reporting and case closing, administration of estate assets, distributions to creditors, and performance of the trustee's other duties under section 704. At least every other year, the visit should take place at the trustee's office.

2-2.8 MONITORING TRUSTEE COOPERATION IN FURNISHING REPORTS AND REQUESTED INFORMATION

The trustee must timely and appropriately respond to the United States Trustee's requests, whether those requests are for specific actions or information. The trustee's responses should be timely, professional, considerate, clear, and accurate. The trustee should demonstrate a willingness to attend and participate in training provided by the United States Trustee.

Copies of written responses, notes of oral responses, training attendance records, and responses to United States Trustee enforcement actions should be maintained in the trustee oversight file.

2-2.9 MONITORING TRUSTEE INVESTIGATION OF AND RESPONSE TO BANKRUPTCY FRAUD AND ABUSE

The United States Trustee must maintain in the trustee oversight file a list of all civil enforcement action referrals and criminal referrals made by the trustee; the list should contain the case name, case number, and outcome. *Handbook Chapters 4.N.7 and 4.N.9* contain a description of the trustee's duties to make referrals to the United States Trustee.

2-2.10 MONITORING TRUSTEE RESPONSE TO PUBLIC COMPLAINTS

All complaints concerning a trustee should be made in writing. Upon receipt of a public complaint, the United States Trustee should send it to the trustee requesting a response within a reasonable time. Each complaint is to be independently reviewed and should not be evaluated solely on the basis of the trustee's response. Appropriate remedial action should be taken on all valid complaints.

If the complainant has requested confidentiality, or if there is another reason to keep the name of the complainant confidential, the issue may be raised by letter from the United States Trustee to the trustee without identifying the complainant.

All complaints and a full report of the investigation are to be maintained in the oversight file. A pleading requesting a trustee to close a case, abandon estate property in a case more than 60 days after the section 341 meeting is concluded, or distribute estate funds, or seeking the removal of the trustee, may be considered a public complaint if allegations of improper actions are made against the trustee.

Complaints against trustees received from or through members of Congress or the White House should be handled as described in Manual Volume 1.

2-2.11 MONITORING TRUSTEE RETENTION AND PROTECTION OF ESTATE RECORDS, INCLUDING PERSONALLY IDENTIFIABLE INFORMATION

For an asset case, the trustee must retain the paper and electronic case files and estate accounting records for a period of at least two years after the date on which the trustee was discharged and during which a proceeding on the trustee's bond may be commenced. For a no-asset case, the trustee must retain in paper or electronic estate files all of the documentation that supports the trustee's independent investigation and determination that the case is a no-asset case, for a period of at least two years after the date on which the trustee was discharged and during which a proceeding on the trustee's bond may be commenced. The trustee is

responsible for ensuring that the information contained in these records is not lost, stolen, or disclosed to unauthorized persons. In addition, the trustee is responsible for ensuring that computer equipment, including desktop computers and portable equipment with memory capability (e.g., laptops, personal digital assistants (PDAs), and removable drives such as USB flash drives and CD-ROMs), are safeguarded from unauthorized access or use. For further information about these requirements, see *Handbook Chapters 5.G.3 and 5.G.5*.

The United States Trustee monitors compliance with these requirements through audits and field exams and through regular communication with trustees. The United States Trustee must ensure that the trustee reports to the United States Trustee, immediately upon discovery, any loss or potential loss of personally identifiable information (PII), including the theft or the accidental loss of bankruptcy papers such as section 341 meeting notices and final reports, desktop computers, laptops, PDAs, and removable drives such as USB flash drives and CD-ROMs. The United States Trustee must notify the Assistant Director of Oversight upon learning of the loss or potential loss of PII by a trustee.

CHAPTER 2-3: COMPLIANCE MEASURES

2-3.1 INTRODUCTION

The United States Trustee must be prepared to take swift, assertive actions whenever a trustee demonstrates an inability or unwillingness to perform as a fiduciary or departs from standards. Compliance measures include both remedial and enforcement actions, and play an important and vital role in trustee supervision.

Remedial actions are those actions taken by the United States Trustee to improve trustee performance or address trustee deficiencies. Examples include:

1. Requiring the trustee to file more frequent TIRs.

2. Placing a trustee on a case closing plan when the trustee has a backlog of old cases that appear ready for closure.

Enforcement actions are more serious remedial actions such as those described in this section. The United States Trustee should consult with the Office of Oversight before taking any enforcement action to ensure that the United States Trustee has substantiated the basis for taking action.

A range of enforcement actions can be taken to ensure prompt, honest, and effective case administration by trustees. These include administrative, civil, and criminal proceedings. The United States Trustee may be able to effectuate a remedy by suspending or terminating a panel member. In other circumstances, the United States Trustee may decide to initiate formal legal proceedings in court or before an administrative tribunal such as a state licensing agency. Finally, there may be circumstances that require referral of a possible criminal violation to the United States Attorney for prosecution. It is critical that enforcement actions be exercised in a manner that is justified by the facts and the law, and in keeping with the high standards of the Department of Justice.

In selecting the appropriate enforcement action to address trustee misconduct, the United States Trustee must consider the nature of the problem, the resources to be committed, and the impact the enforcement action will have on the bankruptcy system. If the nature of the trustee's misconduct reflects dishonesty, deceitfulness, fraud, or the serious mishandling of estate funds, a single substantiated incident may justify immediate action by the United States Trustee to protect estates. These remedies include trustee removal, temporary restraining orders, orders to turn over books and records, and referral to the United States Attorney and state licensing authorities.

Trustee misconduct short of dishonesty, fraud, or immediate asset risk calls for the use of progressive or cumulative remedies that may range in severity from meetings with the trustee to filing motions to compel, seeking disgorgement or surcharge, temporarily suspending the trustee from rotation, terminating the trustee's appointment to the panel, or seeking permanently to remove the trustee from the panel. Imposition of these remedies is at the discretion of the United States Trustee. The types of conduct that may warrant one or more of these remedies include inadequate reporting or asset investigative efforts, inadequate internal controls, weak case administration, and repeated instances of under-bonding. The identification and documentation of these problems are an integral part of supervision and serve to establish a record upon which to base future action.

In commencing any type of enforcement action, the United States Trustee should bear in mind the impact it will have on the integrity of the bankruptcy system. The preference to negotiate and avoid formal proceedings may be outweighed by conduct that undermines the integrity of the bankruptcy system. A trustee must not be able to negotiate the closure of asset cases and leave those with minimal assets for a successor trustee without penalty. Disgorgement, surcharge, disallowance of fees, and the imposition of sanctions must be pursued when appropriate.

2-3.2 MOTIONS TO COMPEL

Section 704(1) states that a trustee shall "close estate[s] as expeditiously as is compatible with the best interests of parties in interest." Delays in case closure

diminish the return to creditors, undermine the creditors' and public's confidence in the bankruptcy system, increase the trustee's exposure to liability, raise the costs of administration, and expose the debtor to increased penalties and interest in cases involving non-dischargeable pre-petition tax liabilities. The expeditious closure of cases can be enhanced by filing a motion to compel the filing of a final report.

When evaluating whether to file a motion, it is important to assess the posture of the case and whether there is a reasonable basis for the trustee's delay in closing. For example, if the trustee has requested the court to send notice to creditors to file claims pursuant to Fed. R. Bankr. P. 3002(c)(5), the delay in closing may not be attributable solely to the trustee's conduct, unless the claims bar date has long since passed. Other factors that can cause delays include the need to file tax returns and a request for a review of the return pursuant to section 505(b) which may result in a 60-to-180-day delay.

If a final report is filed as a result of a motion, the United States Trustee often expends substantial resources to assist in preparing the report. In such circumstances, a reduction of the trustee's fee, corresponding to the equivalent costs of private accounting or paralegal assistance, should be sought. The time spent should be documented so that this objection may be properly presented to the court in conjunction with the hearing on approval of the final report.
A motion to compel a final report should request a deadline for the filing of both the final report and the final account. The motion should also state that the reports must be in a format approved by the United States Trustee. Any order compelling the filing of a final report should provide for consequences if the trustee fails to comply with the deadline for filing an acceptable final report. Where appropriate, these consequences should include automatic removal of the trustee from all cases upon the filing of an affidavit of default by the United States Trustee.

2-3.3 SUSPENSION AND TERMINATION OF APPOINTMENT PURSUANT TO 28 C.F.R. § 58.6

The United States Trustee may temporarily suspend case assignments to a trustee pursuant to 28 C.F.R. § 58.6 as an enforcement tool. Suspension can lead to termination of a trustee's appointment to the panel. In accordance with 28 C.F.R. § 58.6(a), the United States Trustee must notify the trustee in writing of the decision to suspend or terminate. The trustee will continue to receive cases for the next 20 days or longer if the trustee administratively appeals the United States Trustee's action. 28 C.F.R. §§ 58.6(b) and (c). Unless the United States Trustee specifies that the suspension or termination decision is effective immediately via an interim directive, the criteria for which is enumerated in 28 C.F.R. § 58.6(d), trustees who timely file an administrative appeal will continue to receive cases and will remain on the panel until final agency action is completed. 28 C.F.R. § 58.6 (c).

An inadequate audit opinion issued by the independent auditor or an inadequate UST Field Examination conclusion issued by the United States Trustee indicates

an inability to confirm that the trustee is adhering to fiduciary standards. The United States Trustee's options upon receipt of an inadequate opinion or an inadequate conclusion are:

1. A suspension with or without an interim directive;

2. A deferral of suspension with approval of the Deputy Director for Field Operations; or

3. A waiver of suspension with approval of the Deputy Director for Field Operations.

An interim directive can be issued with the suspension notice only when the continued assignment of cases places estate assets at risk. A deferral of suspension may be appropriate when the audit deficiencies will be corrected and verified within 20 calendar days or less from when the audit report is issued. Waiver of suspension may be appropriate when the United States Trustee believes the inadequate opinion is unwarranted because of a factual inaccuracy, mistake in judgment, or the nature and type of deficiencies. If a trustee is suspended for an inadequate audit opinion or examination conclusion, the United States Trustee shall not return the trustee to active rotation without the approval of the Deputy Director for Field Operations and closure of the audit or field exam by the Office of Oversight.

Unless the United States Trustee allows a late-filed submission, a trustee's untimely filing of the TIR requires suspension from the panel until, at a minimum, the reports are submitted and reviewed by the United States Trustee.

A suspension may also be used in cases where a trustee has a disproportionate number of asset cases that impedes his or her resolution of cases or where a trustee has old cases that should have been closed. Suspension in these latter instances is for the purpose of providing the trustee with sufficient time to address the present cases and demonstrate the ability to receive future cases. The stated goal should be as specific as possible – for example, that final reports be filed by a date certain.

Suspension is also warranted when a trustee has failed to adhere to acceptable fiduciary standards. For example, the administration of assets for the sole benefit of secured creditors, failure to close cases in an expeditious manner, and failure to examine claims sufficiently may all constitute cause for suspension.

If the trustee voluntarily seeks temporary suspension from case assignments, the trustee should submit a Notice of Voluntary Suspension that conforms to the format prescribed by the EOUST. Voluntary suspensions, which are not subject to 28 C.F.R. § 58.6, may result under two scenarios. First, the trustee may request a suspension for personal reasons. For example, the trustee may have health concerns, wish to take parental leave, or need to care for a family member. The

voluntary suspension may be for an indefinite period, but not longer than a year. Second, the trustee may request a suspension to correct a deficiency or deficiencies in the trustee's administration of bankruptcy estates. If the United States Trustee agrees, 28 C.F.R. § 58.6 is not invoked as an enforcement tool. Under this scenario, the prescribed format mentioned above may be modified to delete the time period, so the United States Trustee determines when the deficiency has been resolved and the suspension may be lifted. If the deficiency has not been resolved within one year, the United States Trustee should seek the trustee's resignation or terminate the trustee's appointment to the panel pursuant to 28 C.F.R. § 58.6. If a time period is set and the deficiency has not been remedied within the allotted time, the United States Trustee may grant additional time up to one year, or pursue suspension or termination of the trustee's appointment.

A review of a trustee's cases that demonstrates a history of serious and frequent failure to administer assets, properly report on estate administration, or close cases in a timely manner may result in a decision to terminate the trustee's appointment to the panel. Termination may also result from cumulative evidence that a trustee cannot carry out the responsibilities of the office.

See 28 CFR § 58.6 for additional circumstances that may warrant suspension or termination of the trustee's appointment to the panel.

2-3.4 RESIGNATION

When confronted with evidence of deficiencies and the United States Trustee's intention to take formal action, trustees will frequently resign from the problem case(s) voluntarily. Whenever a trustee resigns from certain cases, the United States Trustee must assess whether to seek the trustee's removal from all assigned cases pursuant to section 324. If the resignation was negotiated, it should be accompanied by an agreement to close all remaining cases expeditiously within specific time frames and with specific consequences. The agreement must be monitored and enforced aggressively.

2-3.5 REMOVAL

Section 324 provides that the court, after notice and a hearing, may remove a trustee for cause. The statute also provides that whenever the court removes a trustee in a case, the trustee shall be removed in all other assigned cases unless the court orders otherwise.

There is wide latitude to bring removal actions under varying fact patterns. The clearest circumstance for removal is where embezzlement or fraud is discovered. Cases where a trustee has failed to timely file reports such as interim reports, final reports, or reports of sale; to expeditiously close cases; to timely collect, liquidate, protect, or preserve estate assets; to appropriately investigate estate assets or debtor's conduct; and to pursue actions for preferences, fraudulent conveyances,

or turnover may serve as a basis for removal. Finally, there are circumstances where the failure to administer an estate over a significant length of time demonstrates sufficient cause for removal.

The Office of the General Counsel must review and approve all motions to remove a trustee.

2-3.6 DISALLOWANCE OR DISGORGEMENT OF FEES, AND SURCHARGE

The disallowance of fees or disgorgement – the recovery of fees previously approved and paid – must be considered a remedy for trustee misconduct or inadequate administration. This remedy ensures adequate funds for a successor trustee's administration and prevents a trustee from receiving an unjust enrichment. Surcharge may be asserted against a trustee whose actions have reduced the amount of income for the estate. An example of an action that results in lost income is the failure of a trustee to maintain estate funds in an interest-bearing account. Moreover, when the trustee's inaction causes the United States Trustee to perform the trustee's duties, a reduction of the trustee's fees corresponding to the equivalent cost of private legal, accounting, or paralegal assistance should be sought. The time spent should be documented so that this objection may be properly presented to the court in conjunction with any hearing on the matter.

2-3.7 SANCTIONS

Fed. R. Bankr. P. 9011 is patterned after Fed. R. Civ. P. 11 and permits the imposition of sanctions for the unnecessary delay or needless increase in the cost of the administration of a case. The rule provides that a trustee's signature on a document constitutes a certification that the trustee has read the document; that to the best of the trustee's knowledge, information, and belief, after reasonable inquiry, the document is well grounded in fact and warranted by existing law or is a good faith argument for the extension, modification, or reversal of existing law; and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation or administration of the case. When the conduct of a trustee violates Fed. R. Bankr. P. 9011, the United States Trustee should consider filing a motion for the imposition of sanctions.

2-3.8 REFERRAL TO STATE LICENSING AUTHORITY

Many trustees are attorneys or CPAs. Both attorneys and CPAs are licensed and regulated by state authorities. State boards and associations have promulgated codes and rules of professional conduct to govern technical competence and professional ethics. Breaches of fiduciary duties by trustees who are attorneys or CPAs are to be reported to the relevant state licensing authorities.

A trustee's responsibilities are similar in many respects to those of attorneys and CPAs. Attorneys frequently have fiduciary relationships with their clients, other attorneys, and CPAs, and they must perform their duties promptly. Attorneys and CPAs have obligations of fidelity to their clients. Trustee misconduct is, therefore, relevant to the character and fitness of an attorney or a CPA to perform in that professional capacity. In circumstances demonstrating a level of misconduct reflecting on an individual's character and fitness, the United States Trustee shall make a referral to the appropriate disciplinary body. The United States Trustee should become familiar with the procedures of their region's state bar associations and accountancy boards in order to pursue the matter.

A referral to a state licensing authority must be approved by the Office of the General Counsel and the DOJ Office of Professional Responsibility.

2-3.9 ALLEGATIONS INVOLVING LOSS OF ESTATE ASSETS BY TRUSTEE OR TRUSTEE'S EMPLOYEE OR AGENT

2-3.9.1 Generally

The loss of estate assets or the inability to account for estate assets is a serious matter, and its expeditious resolution is a top priority. Allegations of the loss of estate assets by a trustee or anyone employed or retained by the trustee must be promptly investigated regardless of the source of the allegation. When the United States Trustee believes that a trustee or an employee of a trustee is unable to account for estate assets, the procedures detailed in the following paragraphs must be followed.

2-3.9.2 Preliminary Assessment and Report to the Executive Office

The United States Trustee must immediately notify the Assistant Director for Oversight. After consultation with the Assistant Director, the United States Trustee shall conduct a preliminary assessment of the likelihood of actual loss. The results of the assessment should be communicated to the Assistant Director.

2-3.9.2.1 Actions if No Loss Has Occurred

If the preliminary assessment determines that no loss of estate assets has occurred, the United States Trustee should prepare a written recommendation to the Assistant Director for Oversight to terminate the inquiry. The United States

Trustee should detail any action taken or to be taken to rectify any problems identified in the assessment. Upon concurrence of the Deputy Director for Field Operations, the inquiry shall be terminated.

2-3.9.2.2 Actions if Loss Has Occurred or Upon Sufficient Evidence of Likelihood of Loss

If the preliminary assessment indicates a loss or likelihood of loss of estate assets, including funds taken, or borrowed and later repaid, by the trustee, the United States Trustee shall immediately forward a written report to the Assistant Director for Oversight. The report should contain, at a minimum, the following information:

1. The name and location of the trustee;
2. Whether the trustee is receiving filings;
3. The number of open cases currently being handled by the trustee;
4. The names of any persons suspected of improper conduct in the handling of estate funds;
5. The number and location of bank accounts involved and the amount of funds on hand;
6. The name of the trustee's software vendor and bonding company;
7. A factual narrative of the circumstances that can be verified as a result of the preliminary assessment; and
8. The United States Trustee's recommendation of proposed action concerning the trustee and the estates under the trustee's administration.

Certain situations, such as where there is evidence that the trustee mishandled estate assets or failed to take adequate precautions to safeguard estate assets against loss, warrant immediate termination of future case assignments.

2-3.9.3 Discussions or Negotiations Regarding Losses

When there is a suspected loss of estate assets or an inability to account for those assets, the United States Trustee shall not enter into settlement negotiations, discussions, or agreements regarding the return of funds, compensation, or resolution of the matter, absent the written approval of the Deputy Director for Field Operations.

2-3.9.4 Additional Actions if Trustee Resignation or Removal May Be Sought

If it appears likely that the United States Trustee will seek to remove the trustee from pending cases or initiate a criminal referral, or both, the United States Trustee should immediately notify the Deputy Director for Field Operations, to be followed by a written memorandum on the matter. Copies should simultaneously be provided to the Assistant Director for Oversight and the Deputy Director/General Counsel.

Prior to requesting the trusteecs resignation or instituting removal action in pending cases, the United States Trustee shall consult on the matter with the Deputy Director for Field Operations. If removal or resignation is initiated, consideration must be given to the appointment of a successor trustee or the Assistant United States Trustee serving as the trustee pending a further review of the case files.

2-3.9.5 Investigation of a Trustee§s Financial Records

When the preliminary assessment indicates that assets cannot be accounted for or that embezzlement is likely to have occurred, an investigation of the trusteecs case and financial records will be initiated, with the approval of the Deputy Director for Field Operations. The Assistant Director for Oversight, in consultation with the United States Trustee, will coordinate and oversee the selection of an investigation team, the determination of the type and amount of work required, and the nature and extent of records that must be gathered to carry out the investigation. Specific steps will depend on the circumstances, and the format and distribution of the investigative report ultimately produced will be prescribed by the Deputy Director for Field Operations. Because these reports may serve both civil and criminal purposes, no single format can be set.

Absent the approval of the Assistant Director for Oversight, no case files, financial records, or other estate documents may be furnished to a successor trustee, other than the United States Trustee, until the investigation is complete. Further, without approval of the Assistant Director for Oversight, no disbursements should be made in any estates until the investigation is complete.

2-3.10 CRIMINAL REFERRALS

Whenever it is discovered that a trustee, an employee of a trustee, or an auctioneer is engaged in conduct that may constitute a crime, the United States Trustee must immediately notify the Assistant Director for Oversight, the Office of the General Counsel, and the Office of Criminal Enforcement.

The United States Trustee shall coordinate with the EOUST to provide whatever assistance is needed to carry out an investigation of trustee misconduct. The United States Trustee also shall make regular contacts with the Office of the United States Attorney to determine the progress of any criminal investigation or prosecution.

CHAPTER 2-4: STOCKBROKER AND COMMODITY BROKER LIQUIDATION

2-4.1 INTRODUCTION

The provisions of sections 741 through 766 address the manner in which stock and commodity brokers are to be liquidated. Once it has been determined that a debtor is a stockbroker or a commodity broker, the case must be assigned to a trustee as quickly as possible, and the trustee must be urged to liquidate the estate expeditiously in order to lessen the impact of the filing on brokerage customers.

The Securities and Exchange Commission (SEC) and the Securities Investor Protection Corporation (SIPC) should be provided notice of a filing by a stockbroker. The Commodity Futures Trading Commission (CFTC) should be informed of a filing by a commodity broker.

The United States Trustee should be aware that section 109(d) prohibits a stockbroker or a commodity broker from filing under chapter 11. See *In re SSIW Corp.*, 7 B.R. 735 (Bankr. S.D.N.Y. 1980); *In re CO Petro Marketing Group, Inc.*, 11 B.R. 546 (B.A.P. 9th Cir. 1981), *rev'd in part*, 680 F.2d 566 (9th Cir. 1982). If a broker files a chapter 11 petition, a motion should be made by the United States Trustee to convert the case to chapter 7 or to dismiss it, with specific notice to the SEC and SIPC for the stockbroker and to the CFTC for the commodity broker.

Because stockbroker and commodity broker cases are very rare and can present unusual issues, the United States Trustee should notify and consult with the Office of the General Counsel immediately upon the filing of such a case.

2-4.2 STOCKBROKER LIQUIDATION

Section 742 of the Bankruptcy Code exempts the SIPC from the automatic stay provisions of § 362. In fact, once the SIPC has invoked the provisions of the Securities Investor Protection Act of 1970, 15 U.S.C. § 78aaa *et seq*., all bankruptcy proceedings are stayed and the SIPC trustee liquidates the debtor. If the SIPC chooses not to invoke the provisions of 15 U.S.C. § 78aaa *et seq*., the United States Trustee should, if possible, appoint a panel member who has stock liquidation experience. The trustee should be encouraged to retain counsel with experience in the field. The trustee and counsel should be familiar with:

1. The 30-day period to assume or reject executory contracts (section 744);

2. The segregation of customer accounts (section 745);

3. The treatment of customers who dealt with the debtor not knowing of the filing (section 746);

4. The subordination of certain customer claims, such as those of insiders (section 747), and voidable transfers (section 749); and

5. The distribution of customer name securities and customer property (sections 750, 751, and 752).

2-4.3 COMMODITY BROKER LIQUIDATION

Due to the volatile nature of the futures trading market, a trustee must act quickly so as not to penalize customers unnecessarily. This is especially important because the CFTC does not have authority comparable to that of the SIPC in filing its own proceeding. The United States Trustee should, if possible, appoint a trustee with experience in commodity broker liquidation, and should encourage the trustee to retain counsel and other professionals with related experience. The following instructions are provided to assist the United States Trustee in supervising the trustee who is assigned to a commodity broker case.

2-4.3.1 Identifying and Securing Customer Property

2-4.3.1.1 First Priority

Sections 766(c) and 766(h) prescribe the first priority treatment of both specifically identifiable customer property and non-specifically identifiable customer property (e.g., segregated customer account funds). Customer property is defined at section 761(10).

2-4.3.1.2 Locating, Identifying, and Securing Computer Runs

Daily computer runs should be obtained and the debtor's computer service should be instructed to continue daily runs pending further instruction. Computer runs should contain:

1. A daily equity run reflecting the current status of all customer accounts, and credit balances marked to market as of the close of the prior day's trading; and

2. A general ledger that indicates where all customer property and other firm assets are located. It is important to note, however, that debtor records may not be up to date.

2-4.3.1.3 Use of Debtor Personnel

A conference should be held immediately with the debtor's principals, key employees, and accountants. A list must be obtained of customer property accounts, specifically identifiable customer property, the location of physical commodities, the location of documents of title, proprietary accounts maintained by or for the debtor or its own principals, clearing broker or brokers if the firm does not clear its own trades, the names of contacts at exchanges, major commodity trade advisors, and major commodity pool operators. If the debtor's records are not up to date, accountants should be employed to update them to the day of filing.

2-4.3.1.4 Notification to Exchanges

All commodity exchanges should be notified of the trustee's appointment. All exchanges are to be instructed that no further trading in any accounts maintained by or for the debtor's account should be conducted except under the direct authorization and express authority of the trustee. An accounting of all bonds and securities that may be on deposit with each exchange should be requested.

2-4.3.1.5 Conference with Clearing Brokers

Immediate verification of the status of all customer-segregated and non-segregated accounts must be obtained, and clearing brokers must be instructed to stand by for the liquidation or transfer of open commodity contracts.

2-4.3.1.6 Customer Lists

A list of all customers with open commodity contracts, including names, addresses, and telephone numbers must be assembled.

2-4.3.2 Transferring or Liquidating Open Commodity Contracts

2-4.3.2.1 Notice to Customers

Each customer with open contracts pursuant to section 765(a)(2) must be notified, both by telegram and by telephone, that immediate election must be made to either transfer or liquidate open positions and, absent prompt instruction from the customer, that the trustee will liquidate. This notification must be done immediately because positions are at risk and subject to dramatic fluctuations in value. It is highly advisable to require the election from the customer either in writing or by telegram or to have a third party record responses. Otherwise, customers may try to disavow the election to liquidate if the contracts should subsequently appreciate.

2-4.3.2.2 Margin Calls

Margin calls are to be issued to customers with open positions and are to be liquidated immediately if payment is not remitted promptly.

2-4.3.2.3 Estimation of Distributive Shares Percentage

Estimated distributive share percentages for customers should be calculated. In order to transfer customer accounts with open contracts to receiving brokers, an estimated distributive share for each customer is necessary. A preliminary computation of the estimated distributive share is made by computing the percentage of required segregated funds that are actually on hand. For example, if $1,000,000 in customer segregated funds should be on hand, but only $250,000 can be located, the preliminary estimated distribution percentage is 25 percent. Adjustments must then be made for unposted items in the debtor's books, administrative expenses, and other charges against the $250,000 of segregated funds. If administrative expenses incurred in preserving customer property must be paid out of such segregated funds in an estimated amount of $25,000, and other adjustments will further deplete the fund in an amount of $25,000, then the adjusted estimated distributive share for each customer will be 20 percent (i.e., $200,000 divided by the required $1,000,000).

2-5.3.2.4 Estimated Distributive Share for Transferring Customer Shares

Once the estimated distributive share for transferring customers is calculated, the amount of cash to be transferred to receiving brokers with transferred accounts is determined by taking the estimated distributive share percentage of the transferring customer's net equity. Net equity is defined at section 761(17). In effect, it consists of the customer's net credit balance at filing, if there are no open contracts in the account or on the date of liquidation or transfer of open contracts, after adjusting for specifically identifiable property and offsetting obligations to the debtor.

2-4.3.2.5 Court Approval

Court approval of estimated distributive share calculations must be obtained prior to transferring open contract accounts on notice to transferring customers. If possible, testimony by an accountant and/or CFTC auditor should be obtained as to how the estimated share was calculated and safeguard adjustments for unposted items made.

2-4.3.2.6 Releases

Release and indemnification agreements from receiving brokers should be obtained prior to transferring accounts.

2-4.3.2.7 Open Contracts

All open contracts for which customers elect liquidation or fail to promptly elect after notification are to be liquidated. Clearing brokers must be instructed to remit customer account funds promptly to the trustee's account.

2-4.3.3 Expedited Interim Distribution of Customer Account Funds

2-4.3.3.1 Questionnaire

A questionnaire should be sent to all customers reflected on the debtor's books and records as having credit. The questionnaire should instruct each customer to file a proof of claim and should request:

1. Verification of the balance shown on the debtor's records;

2. A listing of beneficial owners of the accounts;

3. Other accounts with the debtor, other debts owed to the debtor, and business or personal relationships with the debtor or its principals or employees carrying the accounts; and

4. Any other information pertinent to the account to enable the trustee to perform the duties imposed by sections 746, 747, 750, and 751.

2-4.3.3.2 Contents of Questionnaire

The questionnaire should specify that no interim distribution will be made until the questionnaire is returned with all requested information. Each questionnaire should include an affirmation by the customer that the information is true and complete, that the customer submits to the jurisdiction of the bankruptcy court, and that the customer will indemnify the estate for all claims arising out of inappropriate or excessive customer distributions.

2-4.3.3.3 Interim Distributions

Questionnaires should be processed immediately and estimated distributive shares calculated for each customer with a confirmed net credit balance. Application should be made to the bankruptcy court, on notice to the CFTC, for authority to make interim distributions to customers with net credit balances and supporting schedules reflecting credit balance accounts and computation of each distributive share. Upon receipt of court approval, interim distributions of the estimated distributive shares should be made. The use of a questionnaire and interim distributions could also be helpful in a stockbroker liquidation.