

Department of Justice
Executive Office for United States Trustees

Final Agency Action
Case No. 02-0003

Review of the Decision of the
United States Trustee for [Redacted]
Regarding [Redacted]

[Redacted] (“Panel Trustee”), appointed by the United States Trustee to administer chapter 7 cases filed in the United States Bankruptcy Court for the [Redacted], seeks review under 28 C.F.R. § 58.6 of a decision by the United States Trustee to suspend his receipt of new case assignments. I affirm the United States Trustee’s suspension decision based upon the record¹ before me.

I. Course of this Proceeding

By delivery of the Notice, the United States Trustee suspended the Panel Trustee from the chapter 7 case assignment rotation.² See 28 C.F.R. § 58.6(a). The United States Trustee imposed the suspension because the Panel Trustee was the subject of an inadequate audit opinion contained in the Office of the Inspector General (“OIG”) Audit Report No. MR-90-02-010 issued on April 12, 2002 (the “OIG Audit Report”).³ If an inadequate audit opinion is issued, the panel trustee will be suspended from the active rotation for receiving new cases in accordance with the procedures described in 28 C.F.R. §58.6, as required in the Handbook for Chapter 7 Trustees (Mar. 1, 2001 ed., as revised effective July 1, 2001)(“Handbook”).⁴ See Handbook at page 9-23. Further, the United States

¹The record includes the United States Trustee’s Notice of Suspension from Panel Rotation dated April 25, 2002 (“Notice”), including attached Exhibits 1 through 4; the Panel Trustee’s Request for Review dated May 14, 2002 (“Request for Review”), including attached Exhibits 1 through 15; and the United States Trustee’s May 28, 2002 response to matters raised in the Request for Review (“Response”).

²The Panel Trustee continued to receive new case assignments during the pendency of this review. See 28 C.F.R. 58.6(c).

³ The Panel Trustee was audited by the OIG previously and an audit report for the previous audit was issued in September 1998. The September 1998 audit report contained no major findings and only three minor deficiencies were noted.

⁴ The Handbook is prepared by the U.S. Department of Justice, Executive Office for U.S. Trustees. The
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Trustee has concluded that the Panel Trustee has negatively impacted bankruptcy estates and reduced payments to creditors as a result of substandard case administration and excessive payment of professional fees. Finally, the United States Trustee asserts that the Panel Trustee has failed to close cases in a timely manner or timely file accurate final reports. See Notice pp. 2-3.

The Panel Trustee timely filed his Request for Review. In his Request for Review, he asserts that his three most recent trustee performance reviews reflect that he has performed his panel trustee duties adequately (with the exception of closing cases). See Request for Review at p. 3. Moreover, he contends that his higher than average payments to professionals percentage is the result of one case⁵ that skewed the numbers. See Request for Review at pp. 3-4. The Panel Trustee also asserts that he has taken seriously and addressed the United States Trustee's case administration concerns and that he has shown substantial improvement in filing final reports in a timely and efficient manner and with a substantial reduction in errors. See Request for Review at pp. 9-10.

It is the Panel Trustee's position that his past failure to close cases in a timely manner has caused the United States Trustee to be overly critical of even the most insignificant or innocent mistakes. See Request for Review at p. 4. The Panel Trustee also believes his progress in filing final reports in a timely and efficient manner has been overshadowed by the United States Trustee's lingering frustration relating to his previous performance in closing case. See Request for Review at p. 10. Finally, the Panel Trustee states that he has completely addressed or corrected each of the deficiencies identified in the OIG Audit Report and he invites a follow up visit to confirm the responsive actions his office has taken. See Request for Review at p. 1-2.

The United States Trustee timely filed a Response to the Panel Trustee's Request for Review. The Response takes issue with the Panel Trustee's claim that the high payment to professionals average is the result of one "unique" case. See Response at pp. 1-2. Further, the United States Trustee asserts that for the past three years, the Panel Trustee's failure to close cases in a timely and accurate manner has consistently been and continues to be a significant problem. See Response at pp. 2-3.

The United States Trustee contests the Panel Trustee's assertion that the last 41 final reports he has submitted resulted in a greatly reduced error rate. See Response at pp. 2-3. The United States Trustee also points out that the OIG, which is independent of the United States Trustee's office, was of the opinion that the Panel Trustee's accounting and cash management practices and procedures were inadequate for safeguarding bankruptcy estate funds. See Response at p. 3.

⁴(...continued)

Handbook represents an operational manual for panel trustees under United States Trustee supervision.

⁵ [Redacted] (Hereinafter referred to as " the [Redacted] case").

The documents referenced above, and their accompanying exhibits, constitute the record in this case.

II. Standard of Review

In conducting this review, the Director must consider two factors:

- (1) Did the United States Trustee's decision constitute an appropriate exercise of discretion; and,
- (2) Was the United States Trustee's decision supported by the record.

See 28 C.F.R. § 58.6(i) (specifying the scope of the Director's review).

III. Analysis

A. The Duties of the United States Trustee and Panel Trustee

United States Trustees supervise panel trustees, 28 U.S.C. § 586(a)(1), and appoint them to individual chapter 7 cases. 11 U.S.C. § 701. United States Trustees carefully “monitor the performance of panel members . . . in order to determine whether they should be continued in or removed from panel membership.” H.R. Rep. No. 595, 95th Cong., 1st Sess. 102 (1977). Under the law, “[t]he United States trustee is permitted to conduct his own investigation . . . to exercise effective supervision and make an effective evaluation of the performance of the private trustees on the panel.” Id. at 110.

Panel trustees are fiduciaries with wide-ranging responsibilities to effectuate the goals of the particular chapter under which a bankruptcy case is filed. Because they are fiduciaries, trustees are also held to very high standards of honesty and loyalty. See generally Woods v. City National Bank & Trust Co., 312 U.S. 262, 278 (1941); Mosser v. Darrow, 341 U.S. 267 (1951). See also Meinhard v. Salmon, 249 N.Y. 458, 464, 164 N.E. 545, 546 (1928) (Cardozo, C.J.).

B. The OIG Audit Report Supports Suspension of the Trustee

The deficiencies which caused the Panel Trustee to receive an inadequate audit opinion, as listed in the OIG Audit Report, are as follows:

1. Bank reconciliations were not initialed or dated by the Trustee to indicate his timely review.
2. Transaction descriptions on Forms 2 for five cases were not complete.

3. Forms 1 for two cases did not contain all scheduled assets.
4. Disbursements in one case totaling \$2,900.00 were not authorized by court order.
5. A computational error caused overpayment of \$1,170.00 to release certain estate property from a deed of trust.
6. A cancelled check in one case in the amount of \$82,038.00 was missing from the case files.
7. The Panel Trustee's internal controls could be strengthened.
8. There was no evidence that the panel Trustee had reviewed supporting documentation prior to payment.
9. Supporting documents were not marked paid or canceled in some way to prevent duplicate payment.
10. Receivables ledgers were not used to track multiple payments.⁶
11. The Panel Trustee's use of a signature stamp in his legal practice that was not adequately controlled.⁷

See OIG Audit Report (United States Trustee Exhibit 1) at p. 2-3.

The first three deficiencies listed above were identified by the United States Trustee during a field review in August 2001 and were not corrected by the Panel Trustee by the time of the OIG review. Although not forming the basis of the inadequate audit opinion, the OIG Audit Report identified four other deficiencies in addition to those listed above.⁸ The above listed deficiencies and the four

⁶ This item is referenced inconsistently in the OIG Audit Report. At page 3, the last bullet point identifies this as a general deficiency without reference to any specific cases. Conversely, in Appendix II of the OIG Audit Report, found at page 14, line item 16 references a deficiency in two specific cases.

⁷ The fact that the signature stamp was in an unlocked desk drawer and accessible to anyone, makes this deficiency pertinent to the Panel Trustee's chapter 7 operations.

⁸ The additional deficiencies are: (1) in one case the Panel Trustee maintained funds in excess of \$200,000 for nearly seven months without investing such funds in a higher yielding account; (2) the receipts log was not

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additional deficiencies are listed at Appendix II of the OIG Audit Report. See OIG Audit Report at p. 13-14. The deficiencies identified in the OIG Audit Report indicate that the Panel Trustee’s accounting and cash management practices and procedures were inadequate for safeguarding bankruptcy estate funds, justifying a suspension of new case assignments. See 28 C.F.R. §58.6(a); Handbook at p. 9-22 and 9-23.

The Panel Trustee devotes one page of his eleven and one-half page Request for Review to suggest that some of the deficiencies identified in the OIG Audit Report are more in the nature of procedural, as opposed to substantive, deficiencies.⁹ See Request for Review at p. 10-11. In addition, the Panel Trustee submitted a detailed response to each of the deficiencies identified in the OIG Audit Report. See document titled “Audit Response” attached to Request for Review.

The Panel Trustee’s detailed response provides an explanation as to why the deficiencies occurred and sets forth the corrective actions the Panel Trustee has implemented. The Panel Trustee does not contest the facts underlying the OIG Audit Report. Moreover, the Panel Trustee states that he shares the United States Trustee’s concern regarding the inadequate OIG Audit Report and that he is prepared to accept a forty-five day suspension of new case assignments to allow confirmation of his implementation of corrective actions.

As set forth in Handbook, “[i]mplementation of corrective actions, a follow-up visit by the United States Trustee, and the approval of the Deputy Director, Executive Office for the United States Trustees, are required in order for case assignments to resume.” See Handbook at p. 9-23. The Panel Trustee provides that he has implemented corrective actions. The United States Trustee shall schedule with the Panel Trustee and conduct a follow up visit to determine whether implementation of corrective actions has occurred, and whether such actions will prevent the reoccurrence of similar deficiencies in the future. The United States Trustee shall communicate her recommendation and the results of her follow-up visit to the Assistant Director for Review and Oversight. If satisfied, the Assistant Director, subject to conditions set forth in section C. 2. below, will recommend that the Principal Deputy Director approve the resumption of new case assignments.

⁸(...continued)

marked to show that receipts were periodically traced to the bank statements and deposit slips; (3) in one case a \$9,120.44 check had been outstanding approximately seven months and no follow-up action had been taken to resolve the issue; and (4) in two cases the assets scheduled on Form 1 were not listed in the respective debtor’s bankruptcy petition.

⁹ For example, the Panel Trustee notes that he has always maintained an accounts receivable log, however, prior to the OIG audit, he did not maintain such log within the financial file. Similarly, the Panel Trustee explains that although he has always reviewed and approved estate payables before a check was cut, he had been using removable notes to indicate review and approval of payables. The problem with his system was that upon payment all evidence of his review and approval was removed together with the notes.

C. Certain of the Panel Trustee's Case Administration Deficiencies Support Suspension

The United States Trustee's decision to suspend the Panel Trustee was also due to other problems, including those identified in a Trustee Performance Review for the period of July 1, 2000 through June 30, 2001 (the "October 2001 Performance Review"). See Notice at pp. 2-4. As a result of the October 2001 Performance Review, the Panel Trustee was given a shortened three month appointment to the panel, followed by a shortened four month appointment, which was to expire on May 30, 2002. See United States Trustee's collective Exhibit 6.

In the October 2001 Performance Review, the Panel Trustee's overall performance was regarded as less than adequate. Further, his performance was inadequate in the area of "TFRs and TDRs"¹⁰ and his performance was less than adequate in three other areas. See United States Trustee Exhibit 4 at pp. 1, 2; Panel Trustee Exhibit 4 at pp. 1, 2. This was a departure from the Panel Trustee's two previous performance reviews in which his overall performance was regarded by the United States Trustee as adequate and his performance was adequate in all areas except "TFRs and TDRs," which was reported as less than adequate. See United States Trustee Exhibits 2 and 3 at pp. 1, 2; Panel Trustee Exhibits 2 and 3 at p. 1, 2.

1. The Panel Trustee's payments to professionals are high for the past year but his payments to professionals averaged over a five year period and his distribution to creditors percentages are in the reasonable range.

Regarding the issue of the Panel Trustee's distribution of estate funds to professionals, the record supports the conclusion that over the past twelve months the Panel Trustee's performance in this area has also declined. Excluding the [Redacted] case¹¹, the Panel Trustee's professional fees for cases closed during 2001 were 28.9% of total case receipts. This is well above both the national average for panel trustees and the average for panel trustees in the United States Trustee Program Region within which the Panel Trustee is located¹² (16.1% and 17.0% respectively) during 2001. However, when viewed over a five year period (1997 - 2001) excluding the [Redacted] case, the Panel Trustees payments to professionals are in the reasonable range.

¹⁰ 11 U.S.C §704(9) requires a trustee in a chapter 7 case to file a final report ("TFR") regarding the administration of the bankruptcy case. Within 125 days after entry of an order allowing final compensation and expenses, a trustee must submit to the United States for review a final account ("TDR"). Once the United States Trustee is satisfied, the TDR is filed with the bankruptcy court.

¹¹ See n. 4, *supra*.

¹² The [Redacted] office of the United States Trustee is located in Region [redacted] There are twenty-one regions in the United States Trustee Program.

The percentage of estate assets distributed to unsecured creditors by the Panel Trustee for all cases during 2001 (19.1%) falls between the national average (23.0%) for panel trustees and the average for Region [redacted] panel trustees (18.7%). Excluding the [Redacted] case, the Panel Trustee's distributions to unsecured creditors (29.5%) is at the high end for panel trustees nationally and in Region [redacted] for 2001 and over the 1997-2001 time frame.

2. The Panel Trustee's duty to close cases in a timely and consistently satisfactory manner, including the filing of timely and accurate reports.

Regarding the closing of cases and final report issues, 11 U.S.C. §704(1) provides that a trustee shall close an estate as expeditiously as is compatible with the best interests of the estate. Delays in case closure diminish the distribution to creditors, undermine the creditors' and public's confidence in the bankruptcy system and increase the panel trustee's exposure to liability. One of the prerequisites to case closure, is the filing of TFRs and TDRs by the panel trustee after they have been approved by the United States Trustee.

Beginning with the July 1, 1998 to June 30, 1999 time period that is covered by the Trustee Performance Review issued in October 1999, the Panel Trustee began displaying an inability to close cases and submit his final reports in a timely manner. See United States Trustee Exhibit 2 at pp. 1, 4; Panel Trustee Exhibit 2 at pp. 1, 4. Beginning with the July 1, 1999 to June 30, 2000 time period that is covered by the Trustee Performance Review issued in October 2000 ("October 2000 Performance Review"), in addition to problems with timeliness, the Panel Trustee began displaying an inability to submit accurate final reports. See United States Trustee Exhibit 3 at pp. 1, 4; Panel Trustee Exhibit 3 at pp. 1, 4. The Overall Comments and Recommendations section of the October 2000 Performance Review, contained the following comments:

This is a very critical time in [the Panel Trustee]'s trustee career. There have been several changes in his administration over the last year, and the UST has noticed that [the Panel Trustee] has not been giving his cases the attention to detail that once was evident in filing his TFRS and/or negotiating reductions in his professionals' compensation requests....

Id. at p. 2.

Despite the admonition in his October 2000 Performance Review, the Panel Trustee's performance deteriorated further over the following twelve months. On the October 2001 Performance Review (which covers the subsequent twelve month period), it was noted that there were significant deficiencies and serious issues of delay in the Panel Trustee's administration of his asset cases. See United States Trustee Exhibit 4 at pp. 2, 5; Panel Trustee Exhibit 4 at pp. 2, 5. In the Overall Comments and Recommendations section of the October 2001 Performance Review, the United States Trustee includes the following comments:

Since the last performance appraisal, [the Panel Trustee]'s administration has declined. He has significant deficiencies in his asset case administration, as nearly one-half of his large caseload of approximately 122 asset cases are ready for closure by submission of his Trustee Final Report and Account and/or distribution. In fact, many of his cases should have had final reports submitted over a year ago. [The Panel Trustee] has been counseled on numerous occasions during this review period to prepare and submit final reports in these cases that are fully administered. While he does not dispute the need for closure of these cases, his response has generally been to offer additional future dates for submission of final reports....

Id. at p. 2.

The October 2001 Performance Review, covering July 2000 to June 2001, referenced 15 TFRs and 11 were deficient in some respect. Between July 2001 and October 2001, 18 TFRs were submitted by the Panel Trustee. Of the 18 TFRs, 5 were rejected by the United States Trustee, 3 had fee reductions due to delay, 5 were unresolved and 5 had no delay or deficiencies and were submitted to the bankruptcy court. Between November 2001 and January 31, 2002, 18 TFRs were submitted by the Panel Trustee. 8 of the 18 appear to have been error free and forwarded to the bankruptcy court, 7 needed corrections and 3 had fee reduction related objections (including 1 that needed corrections). From February 2002 to April 2, 2002, 8 TFRs were submitted and 6 were either incomplete or contained errors and 2 were forwarded to the court with objections related to delay or lost interest.

The Panel Trustee does not dispute these numbers but relies upon a slightly different time frame. The Panel Trustee asserts that during the January 2001 to April 2002 time period, his deficiency rate on final reports had declined from 58% to 20% and that his final report return rate had declined from 25% to 11%. The United States Trustee disagrees with the Panel Trustee's conclusion about a greatly reduced error rate. Regardless, the parties do not dispute that from November 2001 to January 31, 2002 and from February 2002 to April 2002, the Panel Trustee's accuracy was very poor.

There are legitimate reasons why cases cannot be closed and panel trustees should not be viewed unfavorably for delays in case administration that are beyond their control.¹³ On the other hand, there is no excuse for the delays in submission associated with the Panel Trustee's final report history

¹³ For example, the Panel Trustee appears to have provided a legitimate reason why the [Redacted] case could not be closed by the deadline that had been established by the United States Trustee's office. Nevertheless, it appears that the United States Trustee's office may have included in their assessment of the Panel Trustee's case administration performance his inability to close the [Redacted] case by this deadline.

for the past three years or his high error rate for the past two years.¹⁴ The Panel Trustee has shown some progress in reducing the number of errors per final report. However, only 13 of the last 44 TFRs submitted were error free.

The filing of timely and accurate TFRs and TDRs and closing of cases are core panel trustee duties. The record supports the conclusion that the Panel Trustee's performance in closing cases and submitting final reports has for the past three years been unsatisfactory. Moreover, the record supports the conclusion that while the backlog of cases awaiting final reports has been reduced, the Panel Trustee's error/problem rate on final reports has remained at an unacceptably high level. Even the Panel Trustee acknowledges in his Request For Review that there are too many errors and that mistakes on his final reports must cease.

IV. Conclusion

In sum, the record illustrates that the Panel Trustee's accounting and cash management practices are inadequate. Moreover, the Panel Trustee needs to bring his asset case load current and needs to demonstrate that his office is committed to a consistent practice of submitting timely and accurate final reports before taking on the administration of new cases.¹⁵ The record demonstrates the United States Trustee has repeatedly advised the Panel Trustee of these deficiencies and has patiently worked with him to improve his performance. A suspension is an appropriate remedy to give the Panel Trustee an opportunity to undertake and complete corrective and preventative action before taking on the administration of new cases.

The United States Trustee's corrective action is directed toward the remedy and prevention of the deficiencies that led to the Panel Trustee's suspension. It should produce the desired result of improved administrative performance by the Panel Trustee. I encourage the Panel Trustee to use the suspension period to reestablish his credibility with the United States Trustee and to demonstrate his commitment to substantially improving his performance in the areas of closing cases and filing timely and accurate reports.

¹⁴ In his Request for Review, the Panel Trustee provides background on the operation of his office including a change of administrators that occurred around August 2000. The Panel Trustee notes that the new administrator's inexperience detrimentally impacted his office's ability to close cases. The performance numbers tend to support the Panel Trustee's explanation. However, the Panel Trustee is responsible for the administration of his cases and, in such circumstances, he must take steps to ensure that personnel changes do not adversely impact his case administration.

¹⁵ In the Response, the United States Trustee seems willing to look to a ninety day period. The Panel Trustee should use ninety days from the date of this decision as a goal for reestablishing his credibility with the United States Trustee and for demonstrating his commitment to remedy and prevent deficiencies pertaining to his reports.

Based upon my review of the record, including the written submissions of the United States Trustee and the Panel Trustee, I affirm the United States Trustee's decision to suspend the Panel Trustee's eligibility for assignment to chapter 7 cases until his deficiencies are corrected.

The foregoing conclusions and decisions constitute final agency action in this matter.

Dated: July 1, 2002

Lawrence A. Friedman
Director
Executive Office for United States Trustees