



**United States Department of Justice
Executive Office for United States Trustees**

Public Report:

**Debtor Audits by the
United States Trustee Program
Fiscal Year 2008**

*(As required by Section 603(a)(2)(D) of the Bankruptcy Abuse
Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8)*

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EXECUTIVE SUMMARY

Under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (2005) (BAPCPA), the United States Trustee Program (USTP) is authorized to audit individual chapter 7 and chapter 13 bankruptcy cases. Section 603(a)(2)(D) of the BAPCPA states that the Attorney General must:

(D) Establish procedures for providing, not less frequently than annually, public information concerning the aggregate results of such audits including the percentage of cases, by district, in which a material misstatement of income or expenditures is reported.

In Fiscal Year 2008, the USTP designated 1,691 cases for audit. Of the cases designated for audit, 306 were either still in process as of October 15, 2008, or were dismissed before the case was assigned to an audit firm. Of the remaining 1,385 cases, 1,025 were random audits and 360 were exception audits (audits of cases with income or expenditures above a statistical norm). Reports of Audit were filed in 1,276 of the completed cases, and at least one material misstatement was reported in 21 percent (265) of these cases. There were 109 Reports of No Audit filed. A Report of No Audit is filed when a case selected for audit is closed without completion either because the debtor failed to provide sufficient information to complete the audit or the case was dismissed while the audit was in process.

INTRODUCTION

The United States Trustee Program is the component of the Department of Justice whose mission it is to promote the integrity and efficiency of the bankruptcy system by enforcing bankruptcy laws, providing oversight of private trustees, and maintaining operational excellence. The Program consists of 21 regions with 95 field offices nationwide and an Executive Office in Washington, DC. Each field office is responsible for carrying out numerous administrative,

regulatory, and litigation responsibilities under title 11 (the Bankruptcy Code) and title 28 of the United States Code.^{1/}

Under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, the USTP is authorized to contract with independent firms to perform audits of individual chapter 7 and chapter 13 cases designated by the USTP. The purpose of the audit is to determine the accuracy, veracity, and completeness of petitions, schedules, and other information required to be provided by the debtor under sections 521 and 1322 of title 11. The audits are designed to provide baseline data to gauge the magnitude of fraud, abuse, and error in the bankruptcy system; to assist the USTP in identifying cases of fraud, abuse, and error; and to enhance deterrence.

To perform the audits, the USTP selected, through a competitive procurement process, independent audit firms that employ certified public accountants or independent licensed public accountants.^{2/} The debtor audits are conducted in accordance with audit standards promulgated by the USTP and published in the *Federal Register*.^{3/} The designation of cases for audit began on October 20, 2006.

The BAPCPA authorized the USTP to randomly designate for audit 1 out of every 250 consumer bankruptcy cases per federal judicial district and to designate cases for exception audit in which the income or expenditures of a debtor deviate from the statistical norm of the district in which the case was filed. Annually, the Attorney General is required to publicly report the results of the audits, including material misstatements of income or expenditures by judicial district.

^{1/} The USTP has jurisdiction in all federal judicial districts except those in Alabama and North Carolina.

^{2/} BAPCPA Section 603(a)(2).

^{3/} BAPCPA Section 603(a)(1); *Federal Register*, Vol. 71, No. 190 (October 2, 2006).

From October 1, 2007, through January 1, 2008, the USTP designated cases for random audit in 1 out of every 250 consumer cases per federal judicial district and also designated cases for exception audit. On January 2, 2008, the USTP temporarily suspended its designation of cases for random and exception audits for budgetary reasons. Effective May 12, 2008, the USTP resumed its designation of cases subject to audit, but random audits were conducted in 1 out of every 1,000 consumer cases filed in a judicial district instead of 1 out of every 250 cases.

I. CASE DESIGNATION PROCESS AND TERMINOLOGY

Random audits are selected randomly from all consumer bankruptcy cases within a federal judicial district. In contrast, cases designated for exception audit must meet specific criteria established by the USTP. These criteria are based on income or expenditures greater than a statistical norm for the district where the case was filed, as specified under uncodified section 603(a)(2)(C) of the BAPCPA. In Fiscal Year 2008, the income and expenditure thresholds for designating a case for exception audit were refined.

An audit consists of a comparison between selected items on a debtor's originally filed bankruptcy papers and documents produced by the debtor at the request of the audit firm. Audit firms also conduct at least two searches using commercially and publicly available database services to look for unreported assets and to verify the market value of assets.

After an audit has been completed, a Report of Audit is filed with the court by the audit firm and a copy is transmitted to the United States Trustee. The Report of Audit identifies any material misstatement that is reported by the audit firm. The report is not a legal determination and the legal effect of the auditor's finding of a material misstatement, if any, is a question for the court. Prior to filing a Report of Audit noting a material misstatement with the court, the audit firm contacts the debtor, through counsel if represented, to provide the debtor an opportunity to offer an explanation or supply additional information that may negate the finding. A material misstatement indicates the audit produced information that challenged the accuracy, veracity, or completeness of a debtor's petition, schedules, or other filed bankruptcy documentation. Inaccurate or incomplete information deprives the court, the United States

Trustee, the private trustee, and creditors of adequate information to decide whether to conduct further investigation, recover assets, or seek or impose relief against the debtor.

In Fiscal Year 2008, the Program adjusted the criteria used by audit firms for identifying material misstatements. The specific criteria for reporting a material misstatement are not released to the public to preserve the integrity of the audit process. If a material misstatement is identified in a Report of Audit, the bankruptcy court gives notice to all creditors in the case. In addition, the United States Trustee determines what action is appropriate based on the material misstatement(s) and may pursue a variety of actions depending on the circumstances of the case, including seeking denial or revocation of discharge, or reporting the material misstatement to the U.S. Attorney.^{4/} In many instances, the United States Trustee may take no action on a material misstatement identified in a Report of Audit based on a number of factors, including whether the debtor corrected the error (e.g., filed amended schedules) or whether the material misstatement was intentional.

If the audit firm cannot complete the audit because the debtor did not produce documents requested in connection with the audit or because the case was dismissed while the audit was in process, a Report of No Audit is filed with the court by the audit firm and a copy is transmitted to the United States Trustee. When a Report of No Audit is filed, the United States Trustee may take appropriate enforcement action, including seeking revocation of discharge, if the debtor fails to satisfactorily explain the failure to make available the documentation requested for the audit.^{5/}

II. OUTCOMES

Outcomes are presented in this report both as aggregate national numbers from all judicial districts within the jurisdiction of the USTP, as well as separately by judicial district.

^{4/} See 11 U.S.C. §§ 707, 727(a), 727(d)(4)(A).

^{5/} See 11 U.S.C. § 727(d)(4)(B).

Aggregate Audit Outcomes

Table 1 shows the total number of cases designated for audit, broken down between cases with no report (i.e., cases that were still in process as of October 15, 2008, or were dismissed prior to assignment to an audit firm) and cases where either a Report of Audit or a Report of No Audit was filed with the court. For Reports of Audit filed with the court, the table also identifies the number of cases with at least one material misstatement and the number of cases with no material misstatements. Further, for all cases designated for audit, the table shows the distribution between random audits and exception audits.

In Fiscal Year 2008, the USTP designated 1,691 cases for audit. Of the cases designated for audit, 306 were either still in process as of October 15, 2008, or were dismissed by the debtor before the case was assigned to an audit firm (cases with no report). Of the remaining 1,385 cases, 1,025 were random audits and 360 were exception audits. Reports of Audit were filed in 1,276 of the completed audits, and at least one material misstatement was reported in 21 percent (265) of these cases. Twenty-eight percent of exception audits identified at least one material misstatement compared to 18 percent of random audits. There were 109 Reports of No Audit filed. A Report of No Audit is filed when a case selected for audit is closed without completion either because the debtor failed to provide sufficient information to complete the audit or the case was dismissed while the audit was in process.

| Table 1 - USTP Debtor Audits for Fiscal Year 2008 (Nationwide Aggregate) | | | | |
|---|--------------|---------------|------------------|-------------------------------|
| | Total | Random | Exception | % of Cases Designated* |
| Cases Designated for Audit | 1,691 | 1,177 | 514 | |
| Cases with No Report (As of October 15, 2008) | 306 | 152 | 154 | 18 |
| Cases with Report | 1,385 | 1,025 | 360 | 82 |
| Report of Audit Filed | 1,276 | 944 | 332 | 76 |
| At Least One Material Misstatement | 265 | 172 | 93 | |
| % of Reports of Audit | 21 | 18 | 28 | |
| No Material Misstatements | 1,011 | 772 | 239 | |
| % of Reports of Audit | 79 | 82 | 72 | |
| Reports of No Audit Filed | 109 | 81 | 28 | 6 |
| * Percents are rounded. | | | | |

Outcomes by Judicial District

Table 2 shows the distribution of cases by judicial district in which either a Report of No Audit or a Report of Audit was filed. For cases with a Report of Audit, a breakdown of the number and percentage of cases with at least one material misstatement is provided. This table combines information from both random and exception audits. Due to differences in the number of case filings per judicial district, there is wide variation among districts in the number of Reports of Audit; districts with fewer filings will have fewer reports. For districts with 10 or more Reports of Audit, the percent of audits with material misstatements ranged from 0 percent to 43 percent.

| Table 2: Outcomes by Judicial District for Fiscal Year 2008 | | | | |
|--|----------------------------|-------------------------|---|------------------------------|
| District | Reports of No Audit | Reports of Audit | At Least One Material Misstatement | |
| | | | # of Cases | % of Reports of Audit |
| Alaska | 0 | 1 | 0 | 0 |
| Arizona | 2 | 19 | 4 | 21 |
| Arkansas Eastern | 0 | 14 | 2 | 14 |
| Arkansas Western | 2 | 4 | 0 | 0 |
| California Central | 5 | 55 | 15 | 27 |
| California Eastern | 2 | 38 | 10 | 26 |
| California Northern | 0 | 18 | 6 | 33 |
| California Southern | 0 | 20 | 2 | 10 |
| Colorado | 2 | 35 | 7 | 20 |
| Connecticut | 1 | 7 | 1 | 14 |
| DC | 0 | 2 | 0 | 0 |
| Delaware | 0 | 5 | 2 | 40 |
| Florida Middle | 6 | 49 | 10 | 20 |
| Florida Northern | 0 | 1 | 0 | 0 |
| Florida Southern | 3 | 14 | 1 | 7 |
| Georgia Middle | 1 | 14 | 2 | 14 |
| Georgia Northern | 10 | 34 | 8 | 24 |
| Georgia Southern | 2 | 10 | 0 | 0 |
| Guam | 0 | 3 | 0 | 0 |
| Hawaii | 1 | 1 | 1 | 100 |
| Idaho | 0 | 5 | 2 | 40 |
| Illinois Central | 1 | 12 | 3 | 25 |
| Illinois Northern | 9 | 47 | 16 | 34 |
| Illinois Southern | 0 | 10 | 2 | 20 |
| Indiana Northern | 4 | 18 | 5 | 28 |
| Indiana Southern | 1 | 27 | 2 | 7 |
| Iowa Northern | 0 | 5 | 0 | 0 |
| Iowa Southern | 0 | 10 | 2 | 20 |
| Kansas | 0 | 21 | 5 | 24 |
| Kentucky Eastern | 1 | 18 | 3 | 17 |
| Kentucky Western | 0 | 14 | 6 | 43 |
| Louisiana Eastern | 1 | 9 | 2 | 22 |
| Louisiana Middle | 0 | 1 | 0 | 0 |
| Louisiana Western | 2 | 15 | 3 | 20 |
| Maine | 0 | 5 | 1 | 20 |

| Table 2: Outcomes by Judicial District for Fiscal Year 2008 | | | | |
|--|----------------------------|-------------------------|---|------------------------------|
| District | Reports of No Audit | Reports of Audit | At Least One Material Misstatement | |
| | | | # of Cases | % of Reports of Audit |
| Maryland | 4 | 17 | 6 | 35 |
| Massachusetts | 1 | 24 | 5 | 21 |
| Michigan Eastern | 1 | 53 | 10 | 19 |
| Michigan Western | 1 | 14 | 6 | 43 |
| Minnesota | 1 | 25 | 4 | 16 |
| Mississippi Northern | 1 | 12 | 2 | 17 |
| Mississippi Southern | 0 | 17 | 4 | 24 |
| Missouri Eastern | 0 | 21 | 6 | 29 |
| Missouri Western | 1 | 20 | 5 | 25 |
| Montana | 0 | 1 | 0 | 0 |
| Nebraska | 0 | 10 | 2 | 20 |
| Nevada | 2 | 14 | 3 | 21 |
| New Hampshire | 0 | 3 | 1 | 33 |
| New Jersey | 3 | 24 | 8 | 33 |
| New Mexico | 1 | 6 | 2 | 33 |
| New York Eastern | 1 | 24 | 5 | 21 |
| New York Northern | 0 | 16 | 2 | 13 |
| New York Southern | 2 | 16 | 2 | 13 |
| New York Western | 0 | 15 | 2 | 13 |
| North Dakota | 0 | 2 | 0 | 0 |
| Northern Mariana Islands | 1 | 1 | 0 | 0 |
| Ohio Northern | 2 | 46 | 9 | 20 |
| Ohio Southern | 0 | 31 | 5 | 16 |
| Oklahoma Eastern | 0 | 4 | 0 | 0 |
| Oklahoma Northern | 0 | 9 | 2 | 22 |
| Oklahoma Western | 1 | 11 | 2 | 18 |
| Oregon | 3 | 16 | 2 | 13 |
| Pennsylvania Eastern | 2 | 9 | 1 | 11 |
| Pennsylvania Middle | 0 | 10 | 1 | 10 |
| Pennsylvania Western | 0 | 13 | 4 | 31 |
| Puerto Rico | 0 | 12 | 2 | 17 |
| Rhode Island | 0 | 3 | 0 | 0 |
| South Carolina | 0 | 7 | 1 | 14 |
| South Dakota | 0 | 3 | 0 | 0 |
| Tennessee Eastern | 1 | 23 | 5 | 22 |

| Table 2: Outcomes by Judicial District for Fiscal Year 2008 | | | | |
|--|----------------------------|-------------------------|---|------------------------------|
| District | Reports of No Audit | Reports of Audit | At Least One Material Misstatement | |
| | | | # of Cases | % of Reports of Audit |
| Tennessee Middle | 2 | 13 | 1 | 8 |
| Tennessee Western | 7 | 15 | 4 | 27 |
| Texas Eastern | 1 | 8 | 2 | 25 |
| Texas Northern | 7 | 20 | 2 | 10 |
| Texas Southern | 2 | 10 | 2 | 20 |
| Texas Western | 0 | 16 | 2 | 13 |
| Utah | 0 | 10 | 3 | 30 |
| Vermont | 0 | 3 | 2 | 67 |
| Virgin Islands | 0 | 1 | 0 | 0 |
| Virginia Eastern | 0 | 22 | 5 | 23 |
| Virginia Western | 0 | 8 | 1 | 13 |
| Washington Eastern | 1 | 2 | 1 | 50 |
| Washington Western | 2 | 16 | 1 | 6 |
| West Virginia Northern | 0 | 2 | 0 | 0 |
| West Virginia Southern | 1 | 3 | 0 | 0 |
| Wisconsin Eastern | 1 | 20 | 4 | 20 |
| Wisconsin Western | 0 | 13 | 3 | 23 |
| Wyoming | 0 | 1 | 0 | 0 |
| TOTAL | 109 | 1276 | 265 | 21 |

CONCLUSION

In Fiscal Year 2008, the United States Trustee Program continued to successfully administer the statutorily required audits of individual chapter 7 and chapter 13 bankruptcy cases. The audits are designed to provide baseline data to gauge the magnitude of fraud, abuse, and error in the bankruptcy system; to assist the USTP in identifying cases of fraud, abuse, and error; and to enhance deterrence. It is important to note, however, that the debtor audit program is relatively new, and the USTP continues to perfect the exception audit and material misstatement thresholds. It is, therefore, premature to use this report to draw firm conclusions regarding the magnitude of fraud, abuse, and error in the bankruptcy system. More reliable estimates may become available as the debtor audit program matures.