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WHAT, WHO
§ 1.1 ~ A Good Story

A good story needs a plot and characters. Bankruptcy has both. In this chapter, we begin by sketching the plot. We provide an overview of the purposes of bankruptcy, and a brief sketch of a bankruptcy case. Then we describe the main characters.

§ 1.2 ~ What Bankruptcy Is About: A Short Description

Bankruptcy is about debtors who cannot, or will not, pay their debts. It offers some relief to debtors from the burden of their obligations. It offers some protection to creditors who want an efficient and convenient means to liquidate claims. It allows society to prioritize obligations when there’s not enough value to pay everyone. It seeks to preserve the value of the debtor and its assets. These goals often conflict with one another. In some cases, it will be possible to reconcile the conflicts; often, it will not be.

§ 1.3 ~ The Purposes of Bankruptcy

“Bankruptcy” is not a single concept. It is a set of loosely connected, more or less overlapping concepts that have to do with the relationship between a debtor and its creditors. Some of these serve the interests of creditors, some of debtors, and some may serve both at once.

For a long time — specifically, from 1898 to 2005 — and for most people, “bankruptcy” meant “the discharge.” Most cases were filed by individual debtors who sought to wipe out their past debts, and most of them got what they came for. They had to turn over their nonexempt assets, but most of them had no nonexempt assets, so it wasn’t a barrier. Perhaps most important, they got to insulate their post-bankruptcy earnings from pre-bankruptcy claims.
Traditionally, the U.S. has been unique in regards to the extent of its bankruptcy protection, and the ease with which you could get it. That has been changing lately, in two ways. For one, other countries have been catching up and liberalizing their bankruptcy laws, perhaps in imitation of the American model. Secondly, and far more important for our purposes, Congress amended the Bankruptcy Code in 2005, passing the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA), which resulted in the barrier to entry being raised for individuals seeking chapter 7 bankruptcy protection. Specifically, in an attempt to minimize abuse of the bankruptcy system, Congress imposed a “means test” that creates a presumption of abuse in certain circumstances.1

The “means test” requires the court to dismiss the chapter 7 cases of some debtors if their income is above the median amount in their state and, after deducting allowable expenses, it would leave a sufficient surplus to service past debt.2 At the time that the means test was enacted, it was quite controversial. Banks, credit card companies and their political supporters had been claiming that there was significant abuse in the bankruptcy system. They said that debtors who had the ability to pay their debts were instead filing for bankruptcy and getting a discharge, and that doing this was too easy. They claimed that this was not only unfair to the creditors, it also increased the cost of credit for other consumers.

Consumer advocates, and many bankruptcy law professors and bankruptcy lawyers, contended that abuse was rare. The overwhelming majority of debtors were in dire straits, they argued — often resulting from a job loss, a health care crisis, or some other unfortunate circumstances — and really needed relief. They argued that bankruptcy discharge had only a trivial impact on the cost of credit. They expressed fear that the means test would do violence to the discharge, which has been a fundamental tenet of our bankruptcy system since (at least) the nineteenth century.

With the benefit of a decade or so of experience, it seems they were both largely wrong. It turns out there was not so much abuse. Of course, there are cases of it. But for the most part, debtors who elect to file for chapter 7 bankruptcy have below-median incomes and really do need relief. As a result, the means test — which was intended to create a hurdle for abusers — does not appear to have barred very many debtors. For the same reason, the prediction that the means test would create a sea change in the availability of the bankruptcy discharge has proved to be overblown. It seems to us that most people who need chapter 7 and the discharge can still get it. There are exceptions, of course. But for the most part, relief for the honest-but-unfortunate debtor still exists.3

1 See, e.g., In re Schoen, No. 06-20864-7, 2007 WL 643295, at *3 (Bankr. D. Kan. Mar. 2, 2007) (providing that “Congress created a detailed and complicated mathematical test for evaluating the debtor’s income and expenses to determine whether a presumption of abuse would arise”).
2 For more on the “means test,” see infra § 5.2.
3 For an analysis of the impact of BAPCPA, including the means test, on individual bankruptcy filings, see Stephen J. Sparr and Kevin M. Ball, The Effects of a Statute (BAPCPA) Designed to Make It More Difficult for People to File for Bankruptcy, 87 AM. BANKR. L.J. 27 (2013).
While the discharge for individuals may be the reason most debtors file for bankruptcy, it is far from bankruptcy's only purpose. Creditors also use the bankruptcy process to liquidate their claims. Think of it as a kind of "class action," where the creditors get together and appoint a representative to collect the property of the debtor, sell it, and distribute the proceeds. As a matter of history, this "collect and distribute" purpose of bankruptcy precedes "discharge" by several hundred years. It survives today in cases where there are assets to distribute.

We speak of bankruptcy as providing for the distribution of assets on a pro rata basis. For example, if there is enough to pay 40 percent of all unsecured claims, and those claims have the same priority, we pay 40 percent of each claim. Pro rata distribution thus supplants the "race to the courthouse" system that would apply under state law if bankruptcy did not intervene. But to speak of a pro rata distribution of assets can be misleading. In fact, the Bankruptcy Code articulates its own list of claim priorities (for administrative expenses, taxes, wages and so forth), and distributions are made pro rata to each priority creditor until all value has been exhausted. Also, bankruptcy respects the non-bankruptcy rights in collateral of a creditor with a valid and perfected security interest. This means that a secured creditor is entitled to receive the value of its collateral up to the amount of the secured debt (the debt that exceeds the collateral value is treated as an unsecured claim). Taken together, even in those cases where a debtor has assets to distribute, these priority and secured creditors often eat up most of the estate, leaving little or nothing for the residual class.

Defenders of the system offer any number of justifications for the bankruptcy "class action." Defenders frequently speak of the pro rata distribution as appealing to a generalized sense of fairness. But there are any number of more specific justifications for the bankruptcy device. In a well-known law review article, Prof. (and former university president) Thomas H. Jackson analyzed the pro rata distribution scheme as implementing a kind of "creditor's bargain," substituting the certainty of a modest recovery for the hazard of winning or losing a race.  

A different justification argues that the collective proceeding is more economical. Call it the "death by a thousand cuts" argument: Letting one agent act for all eliminates the duplication and outright waste that you get in a race to dismember the debtor's assets.

But there is a still more subtle justification. Consider the hypothetical business debtor IndusCo, a heavy-industry manufacturer. IndusCo owns a factory, where it has and maintains a boiler. As a going-concern business, IndusCo could be sold for $5 million. Broken up for scrap, the assets would yield $1.5 million — some $1 million from the boiler alone. The factory cannot run without the boiler.

IndusCo owes $1 million to Carlos, and $3.5 million to an array of other creditors. Carlos levies on the boiler. He puts it up for sale, and the proceeds pay his entire claim. The going-concern value of the business is lost; the

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liquidation value of the remaining assets is just $500,000, which the other creditors share pro rata. The other $3.5 million in going-concern value is dissipated. Creditors (except for Carlos) wind up with just 20 cents on the dollar, and the owners of the business’s equity are wiped out.

What we mean is this: A business might have two different values — the liquidation value of the component assets piecemeal, and the value of the business kept together as a going concern. Sometimes, but not always, the business is worth more as a going concern than in liquidation because a going concern might have the ability to continue to operate at a profit, producing a stream of positive cash flows that can be projected and discounted to its present value. A piecemeal liquidation has the potential to destroy the value of the going concern.

Now, an individual creditor may have no incentive to care whether he destroys the value of the going concern; as far as he is concerned, if he gets paid, that is the end of it. But the creditors as a whole may have a powerful interest in preserving the going concern. So when we say that one of the goals of bankruptcy is to “protect asset values,” then at least part of what we mean is “to protect going-concern value.”

Part and parcel of protecting asset values, bankruptcy (chiefly through chapter 11) offers an opportunity to make and implement deals about a debtor’s liabilities and their satisfaction. Sometimes, it may be in the creditors’ interest to settle for less than the full amount they are owed, particularly if they can rely on others to do so as well. Nothing bars debtors and creditors from making a deal, even independent of bankruptcy. But a non-bankruptcy deal may be considerably harder to achieve and harder to enforce than one that is reached through the bankruptcy process.

Why does the bankruptcy process make the deal easier? In part, it is because the automatic stay prevents individual creditors from jumping to the head of the line. But an equally important reason is that the court may impose the terms of the deal on a dissenting minority of creditors that might otherwise hold out for better terms than the rest in a non-bankruptcy setting. This power to impose the plan on dissenters may mean the difference between a successful and an unsuccessful deal. It is so important that some plan proponents will make their deal outside bankruptcy and then, if they cannot get unanimous consent, shepherd it through bankruptcy to impose it on dissenters in what is known as a “pre-packaged” or “pre-negotiated” chapter 11 case.5

A final set of purposes has less to do with any particular debtor or its creditors, but rather with achieving societal interests. One such interest is encouraging entrepreneurial risk-taking. By offering a measure of protection if the venture fails (an individual can obtain a “fresh start”; a business can restructure its balance sheet and continue as a going concern), the bankruptcy system helps to encourage such risk-taking. Another such interest is preserving business operations. Ongoing businesses serve the interests of employees, retirees, customers, vendors, taxing authorities and the communities in which the businesses operate. This purpose may be contentious

5 For more on imposing a deal, see Chapter 18 ("The Plan").
to the extent it is inconsistent with the notion of a "free marketplace" — the idea that businesses that cannot survive competition should fail and disappear. But there have always been limitations on the free marketplace where societal interests are served — and our business bankruptcy system constitutes such a limitation.

To repeat, then, we see five predominant purposes in bankruptcy law:

- to grant the debtor a discharge;
- to orchestrate claims;
- to protect asset (and going concern) values;
- to provide an opportunity to implement deals; and
- to give business debtors an opportunity to restructure.

§ 1.4 ~ A Bankruptcy Case

Next, the narrative. Most cases begin when the debtor files a voluntary petition for bankruptcy relief6 (the Code also allows creditors to initiate the process by filing a petition to create an involuntary bankruptcy case,7 but it does not happen very often). The commencement of a case creates an estate,8 and operates as a stay of just about anything a creditor would want to do to liquidate or enforce its claim.9 The debtor must also file schedules of assets and liabilities and a statement of financial affairs providing information on the state of its finances.10 Additionally, individual debtors must file evidence of compliance with the means test, discussed above, as well as a certificate showing completion of an approved credit-counseling course, which is often an online affair.11

After it receives the petition, the court generates a notice of a meeting of creditors, also known as a "341 meeting" after the Code section that provides for it. The debtor must appear at this meeting of creditors, and testify under oath. In individual-debtor cases, a battalion or more of debtors may show up at the same time

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7 Id. § 303.
8 Id. § 541.
9 Id. § 362. Note the exceptions to the automatic stay in § 362(b). The automatic stay and its exceptions are discussed in Chapter 7.
11 For more information on means testing, see U.S. Dep't of Justice, Means Testing, available at www.justice.gov/ust/means-testing, and for more information on credit counseling, see U.S. Dep't of Justice, Frequently Asked Questions (FAQs) - Credit Counseling, available at www.justice.gov/ust/frequently-asked-questions-faqs-credit-counseling#counselcertificates.
at a trustee’s office, where the trustee asks each of them in turn a few more-or-less searching questions to see whether the debtor appears to be telling the truth on its schedules.

Creditors, if they show up at all, will sometimes find that they are discouraged from asking many questions; the trustee has too many cases to process, and he cannot hold up the room for detailed individual inquiry. In business cases, the meetings are conducted by the U.S. Trustee’s office and tend to be less rushed. But even in these cases, they don’t tend to get into great detail. The bankruptcy judge does not attend these meetings. The meeting is not normally recorded by a court reporter, but it is taped, so if you need a record of the meeting you can get a copy of the tape. In any event, if the creditor really wants to investigate, he has plenty of opportunities throughout the course of the bankruptcy process. This may include at continued 341 meetings, which are common, as the trustee seeks additional information from debtors, who are given some time to gather documents and information.

What happens next depends on the kind of case. In the most common case, the individual chapter 7, if the debtor plays by the rules, then (with certain exceptions) he gets a discharge, wiping out his unpaid pre-petition debts. If there is any property to distribute (but remember, usually there is not), a trustee takes charge of it, turns it into cash, and distributes it among creditors as their interests warrant. After the trustee finishes, the court closes the case and the file goes to storage. These cases take as little as 90 to 120 days from filing of the petition to closing of the case.

In practice, these bankruptcies are far more an administrative than a judicial proceeding. Most debtors never go to the courthouse. Every case is assigned to a judge, but most judges never hear most of their cases. Instead, most of the action goes forward in the clerk’s office, and is handled between the debtor and the trustee.

In chapter 13 cases, the debtor files a plan that provides for payment of some or all of his debts over a three- to five-year period. The amount of debt repaid under the plan will vary depending on the amount of debt and the debtor’s assets, income and expenses.

The chapter 13 trustee will review the plan, and it will be submitted to the court for approval. Creditors have an opportunity to object to the plan but cannot vote on the plan. If the plan is approved, the debtor makes payments under it every month. If he completes the payment plan, he gets a discharge at the end. Prior to BAPCPA, the chapter 13 discharge was broader than it presently is — and some debtors who were eligible for chapter 7 relief would choose chapter 13 instead, in order to avail themselves of the chapter 13 “super discharge.” In addition to limiting access to chapter 7 for some debtors — essentially “forcing” them into chapter

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13 See infra §§ 2.23-24.
15 Id. § 704.
13 — BAPCPA reduced the scope of the chapter 13 discharge. It is still broader than the chapter 7 discharge but not as broad as it once was.

Although we skipped over it in this discussion, there is also a chapter 12, which is basically a version of chapter 13 for individuals who are fishermen and family farmers. They need a special chapter because they often have large amounts of secured and unsecured debt — financing for boats, land and supplies — that make them ineligible for chapter 13, which has debt limits for eligibility and is primarily designed for consumer debtors.

In chapter 11, the debtor will negotiate with its creditors, shareholders and other parties to come up with a plan of reorganization (or sometimes liquidation). This plan will be voted on by creditors and then submitted to the court for confirmation. The process is considerably more complicated than chapter 7 or 13 and tends to take more of the court’s time, although even in chapter 11 much of the action takes place in conference rooms rather than in court. Today, many business reorganization cases are effectively processed via a quick “363” sale of all assets early in the case to a third party,16 with the sale proceeds then distributed among creditors under a subsequently confirmed plan.17

There are also cases under chapter 9, which is used by governmental entities below the state level, such as a city or a water district. Detroit’s bankruptcy case is the most prominent example.18 Finally, chapter 15 provides a mechanism for coordinating international bankruptcy cases.19

§ 1.5 ~ The Judge and the Courthouse Staff

The central role in any bankruptcy — at least, any bankruptcy that is more complicated than a straight chapter 7 liquidation — belongs to the bankruptcy judge who presides over the bankruptcy court. Most bankruptcy matters are litigated before her, although, as explained in more detail elsewhere, she derives her jurisdiction from the district court.20

The bankruptcy judge is appointed by the court of appeals sitting in her circuit. She holds office for a 14-year term and is considered a “unit” of the local federal district court. Since she does not have life tenure, a bankruptcy judge is not an “Article III” federal judge, which has caused issues in some types of cases with regard to

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16 Id. § 363.
17 An alternative to a post-sale liquidating chapter 11 plan, which some courts allow, is a structured dismissal. See, e.g., Official Comm. of Unsecured Creditors v. CIT Group/Business Credit, Inc. (In re Jevic Holding Corp.), No. 14-1465, 2015 WL 2403443 (3d Cir. May 21, 2015).
18 See infra § 5.9.
19 See infra § 5.10.
20 See generally infra Chapters 3 and 4.
whether the bankruptcy judge has the constitutional power to issue a final order, or whether she can only make recommendations to the district judge.21

Typically, a bankruptcy judge has a secretary and a law clerk. She very likely also has the regular services of a deputy clerk assigned to her courtroom, as well as a court reporter. Communication between counsel and the court may go through the secretary, the law clerk, or the courtroom deputy, depending on the preference of the particular judge.

The bankruptcy court also has its own clerk’s office. In the old days, lawyers (or their staff) would show up at the clerk’s office in person to file bankruptcy petitions, motions, objections, etc. The clerk’s office managed a ton of paper. These days, most filings are done electronically. As a result, the clerk’s job has changed somewhat. But they still deal with the “administrative aspects” of the bankruptcy system, including things like taking filing fees, maintaining dockets and files, providing certified copies of orders, transmitting records for matters on appeal, etc. They tend to be the first stop for anyone who has questions about how things work in the bankruptcy court, though they are quick to point out that they cannot provide legal advice.

§ 1.6 ~ Trustees

One difficulty with clarifying the role of the trustee is that there are different kinds of trustees:

► There is the chapter 7 trustee who administers chapter 7 cases;

► There are standing trustees who supervise cases in chapters 13 and 12;

► There can be a chapter 11 trustee appointed to supplant management in chapter 11 cases — and where that does not happen (and it usually does not), there is the debtor-in-possession (DIP), which is the debtor itself acting as if it were a trustee; and

► There is the U.S. Trustee, an employee of the U.S. Department of Justice, who, among other things, supervises trustees.22

We will now address each type in turn.

21 See generally infra Chapter 3.
22 Responding to local concerns, Congress carved out an exception to the ordinary plan of administration for judicial districts in Alabama and North Carolina. In those locations, there is no U.S. Trustee, and chapter 11 cases are supervised by a “bankruptcy administrator.”
§ 1.7 ~ CHAPTER 7

Every chapter 7 bankruptcy case has a trustee. He is appointed by the U.S. Trustee, although the statute is somewhat misleading on that point. What the statute provides is that the U.S. Trustee names an interim case trustee, and that creditors may thereafter elect a trustee. The statute says that if creditors fail to elect a trustee, then the interim trustee continues as case trustee. But in practice, creditors rarely exercise their right to elect a trustee, so the U.S. Trustee’s appointed “interim” trustee usually continues as case trustee.

The duties of the case trustee are set forth in § 704. In summary, he collects the property of the estate, reduces it to cash, and distributes the proceeds among creditors. He is also charged with “investigat[ing] the financial affairs of the debtor,” and “if advisable, oppos[ing] the discharge of the debtor.” BAPCPA imposed additional duties on chapter 7 trustees, including an obligation to request the dismissal of an individual debtor’s bankruptcy case if that debtor fails the “means test.”

The Code provides that the U.S. Trustee appoints the interim trustee, but where does the U.S. Trustee find candidates? The answer is that the U.S. Trustee maintains a panel of individuals whom it deems qualified to serve as case trustees and selects from that panel (hence, sometimes the trustee is called a “panel trustee”). Many are lawyers, but there is no requirement that one be a lawyer in order to gain membership on the panel. Many are accountants. Some are people who have simply developed good skills at managing or investigating.

§ 1.8 ~ HOW MUCH DOES THE TRUSTEE EARN?

How much does the trustee earn? The answer is found in § 326(a), which prescribes that the court may allow compensation that is “reasonable” but not to exceed a prescribed schedule, which is a function of the amount distributed by the trustee. In many cases, referred to as “no-asset cases,” there is nothing to distribute. In those cases, the trustee gets a fee of $60. So, if a trustee gets 150 new cases a month, he books a minimum gross monthly income of $9,000. A trustee who has enough volume of cases and runs an efficient operation may find the fees he earns from “no-asset cases” sufficient to pay — or at least make a substantial dent in — his office

24 Id. §§ 701(a) and 702(b).
25 Id. § 702(d).
26 Even though it does not happen often, you still may want to consider demanding an election when the stakes are high enough, and/or when specialized knowledge will be necessary in order to realize on the value of the debtor’s assets. The election (if any) takes place at the meeting of creditors under § 341. The request has to have the support of at least 20 percent of all eligible claims. The candidate is elected if he gets a majority in amount of claims voting, and if at least 20 percent vote. See generally id. § 702.
27 Id. § 704.
28 Id. § 701 and 28 U.S.C. § 586(a)(1). A list of the panel trustees in each state can be found at www.usdoj.gov/ust/eco/private_trustee/locator/.
overhead, leaving him free to earn an income from the occasional case that has assets and other professional activities.

In addition to the standard fee, panel trustees are compensated on a commission basis. The purpose of the commission system is to incentivize trustees to maximize the dollar amount of assets brought into the estate. The commission is determined based on the total disbursements made by the trustee to interested parties of the estate, excluding any payment to the debtor. The maximum commission rate is 25% on the first $5,000 distributed, 10% on the next $45,000 distributed, 5% on the next $955,000, and 3% for every dollar distributed in excess of $1,000,000. The commissions earned by the trustee are reviewed by the bankruptcy court, when requested, to determine whether the amounts are reasonable. In some cases, the court may award a lower amount.

The Code authorizes the trustee to serve as his own attorney or accountant, with court approval, if doing so would be “in the best interest of the estate.” This is another way that trustees can make money. But it comes with some challenges. One of them is that it can be difficult to distinguish when the trustee is doing “trustee work,” which is compensated on a commission basis (where there are assets to distribute), and when he is doing “lawyer work” (or “accountant work”), which is ordinarily paid on an hourly basis. For this reason, some judges will not allow a trustee to retain himself as counsel or accountant.

But there are other approaches. For example, sometimes a trustee will, with court approval, retain his law firm (or accounting firm) as a professional, and have other individuals at the firm do that work. This allows the distinction between “trustee work” and “lawyer work” (or “accountant work”) to be somewhat easier to make. Another approach is to have regular retention arrangements with friendly professionals in the same community: On Monday, Ralph, as trustee, employs Margaret as his lawyer in the case of DebtorCo. On Tuesday, Margaret, as trustee, hires Ralph to represent her in the case of LittleCo. Some may find the reciprocity troubling, but the system offers a protection: All of these appointments (and all relevant compensation) take place under judicial scrutiny, so if the judge does not want this sort of thing to go on, she can make it stop.

One practical consequence of the trustee compensation system is that you cannot expect the trustee to work hard looking for assets unless someone (that is, an aggrieved creditor) is willing to fund the inquiry. In addition, because of the statutory percentages and the minimum, the trustee really does not want to find assets unless he is going to find a lot. So estates that are small but not empty tend to go unadministered, and debtors who hide $5,000 or $10,000 have a better chance of getting away with it than those who hide $1 million.

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30 But make no mistake: Bankruptcy fraud is a federal crime, punishable by substantial fines and prison time. See 18 U.S.C. § 157. And, like driving under the influence, there is the belief that there is more of it going on than is ever detected, providing an incentive to the U.S. Attorney and U.S. Trustee to seek harsh enforcement of the law if a violation is detected.
§ 1.9 - DEBTOR-IN-POSSESSION (DIP)

So far, we have been talking mostly about chapter 7. Chapter 11 does not provide for the automatic appointment of a trustee. In particular, § 1104(a)(1) states that the court shall appoint a trustee on motion if there is cause. The statute defines “cause” to include “fraud, dishonesty, incompetence, or gross mismanagement.”

It also provides that cause exists if appointment of a trustee is in the interests of creditors, shareholders and other parties, or if there are grounds to dismiss or convert the case under § 1112 but the court decides that appointment of a trustee would be better for creditors and shareholders. The practical fact is that creditors rarely ask for a trustee, and courts even more rarely order the appointment. While BAPCPA broadened somewhat the grounds for appointing a chapter 11 trustee, in the vast majority of cases, the debtor will still remain in possession of the assets as DIP.

The DIP is not just the old debtor with a new name. The law clothes the DIP with powers and responsibilities much like those of a trustee. There is often a tension between the objectives of the DIP’s management (usually, protecting the interests of management and equity) and the fiduciary duty that the DIP assumes when the bankruptcy petition is filed. This is an area in which skilled legal counsel can play an important role and where a creditors’ committee may also be influential.

In the ordinary case, the DIP will be just what the statute seems to suggest: the old debtor with new responsibilities and duties. Some larger cases take on a special character. In these cases, creditors (or shareholders) have already forced out old management before the commencement of the case, sometimes replacing them with “turnaround specialists,” who thus may function as de facto independent trustees, even though they are operating under the DIP hat.

§ 1.10 - CHAPTER 11 TRUSTEE

If the court does order the appointment of a trustee, then the U.S. Trustee appoints “one disinterested person” to serve as trustee. Conversely, on the request of a party in interest, creditors may elect a trustee.

31 See also 11 U.S.C. § 1104(a)(2).
32 BAPCPA requires the U.S. Trustee to move for appointment of a chapter 11 trustee if the debtor’s managers or directors have participated in fraud, dishonesty or criminal conduct. See id. § 1104(e).
33 Id. § 1112(b)(1).
34 Id. § 1101(1).
35 But he does not have all of the duties or powers of a trustee. For example, he is not obligated to investigate himself, nor is he empowered to pay himself. See id. § 1107(a).
36 Id. § 1104(d).
37 Id. § 1104(b)(1).
Note that the chapter 11 trustee does not need to come from the trustee panel. Moreover, the U.S. Trustee is authorized to make his appointment only after consultation with the parties. Ideally, the trustee and the creditors work together to try to identify a person with skills suitable to the case at hand. There is a growing cadre of turnaround specialists who hold themselves out as experts in the matter of managing and reorganizing chapter 11 debtors. Some of them sometimes work as chapter 11 trustees.

Because chapter 11 provides for reorganization, the duties of a chapter 11 trustee are not identical to the duties of a chapter 7 trustee. The chapter 11 trustee is directed to be accountable for all property received, to operate the business (if authorized), and to review and, where appropriate, object to claims. But since the hope in a chapter 11 case is typically to reorganize the business rather than to liquidate, often the trustee will not “collect and reduce to money the property of the estate, [and] close [the] estate as expeditiously as is compatible with the best interests of the parties in interest,” which are the standard duties imposed on the chapter 7 trustee. Also, unlike the chapter 7 trustee, the chapter 11 trustee is directed to file a plan (or a statement as to why he is not doing so).

Because the DIP has most of the rights and powers of a trustee, when one reads “trustee” in the context of a chapter 11 case, we can usually understand the word as meaning “DIP.” For example, § 363 provides terms under which “the trustee” may use, sell or lease property of the estate. But in reality, the “use, sell, or lease” powers are asserted by the DIP far more often than by an appointed trustee.

§ 1.11 ~ EXAMINERS

As an alternative to appointing a trustee, the court may appoint an examiner. The Code provides that if the debts exceed $5 million, then the court, in lieu of appointing a trustee, shall appoint an examiner to “investigate” the debtor. In terms of sheer numbers, there aren’t very many examiners, but in contested cases, asking for an examiner may be a good litigation strategy. It gives the judge an independent voice to hear from, without the disruption that appointment of a trustee may impose.

Requesting an examiner can also result in delay, which is sometimes in the tactical interest of a party, such as a creditor trying to slow down a prepackaged plan. Some courts, perhaps pressing the limits of the statute, are experimenting with the use of examiners for services beyond mere investigation — e.g., to try to promote set-

38 Id. § 1106(a)(1).
39 Id. § 704(a).
40 Id. § 1106(a)(5). Note that, as with chapter 7 trustees, BAPCPA imposed some additional duties on chapter 11 trustees. See id. §§ 1106(a)(1), 1106(a)(8) and 1106(c).
41 Id. § 1104(c). If a party moves for an examiner, and if the fixed liquidated unsecured debts (other than certain insider debts) total more than $5 million, the statute appears to require the court to appoint an examiner, using the word “shall.” Sometimes, though, courts decline to appoint an examiner, or significantly limit the scope of the examiner’s authority, if they believe it would be costly and unhelpful. The court may also appoint an examiner if it is in the interests of creditors, any equity security-holders, and others with interests in the estate, etc., to have an examiner. In either case, the court has discretion regarding the scope of the engagement.
tlement of complex cases. On occasion, one hears a reference to an “examiner with expanded powers,” which refers to this practice of enlarging the role of an examiner.

§ 1.12 ~ STANDING TRUSTEES

For cases under chapter 13 (and chapter 12), the statute authorizes the appointment of a standing trustee if the number of cases so warrants. The standing trustee collects and distributes the debtors’ earnings under chapter 13 plans. He also takes a prominent role in setting standards for plans and in supporting (or opposing, as the case may justify) motions to dismiss or convert, or motions for relief from the stay. Standing trustee compensation is a function of the amount of money he handles, subject to a statutory cap.

§ 1.13 ~ U.S. TRUSTEE

In an earlier generation, trustees had a bad reputation. To some observers, a trusteeship was seen as an attractive plum, awarded to a crony of the judge as a license to pillage the estate. This was part of what was sometimes referred to as “bankruptcy rings,” involving cross-referrals and approvals of the same group of trustees, attorneys, accountants and other professionals in particular courts.

In the run-up to the 1978 law creating the Code, some critics wanted to do away with the system of appointed trustees altogether. They wanted to bring trusteeship into some sort of government agency. The notion met with resistance, and Congress struck on a compromise: It created the Office of the U.S. Trustee as a unit of the Justice Department, and gave it the job of supervising the case trustees. The Office’s own mission statement says:

The most important part of the job is that the U.S. Trustee maintains and supervises the panel of private trustees and has the power to remove them. The U.S. Trustee also appoints creditors’ committees. At least in some districts, the U.S. Trustee has proven aggressive in helping to police bankruptcy fraud.

The U.S. Trustee also comments on professional retentions and fee applications. In 2013, the U.S. Trustee promulgated controversial guidelines for reviewing fee applications in large chapter 11 cases. Proponents of the new guidelines asserted that professional fees in large chapter 11 cases were too high, creating concerns about public confidence in the bankruptcy system, and that enhanced review procedures were necessary in order to facilitate a more thorough evaluation of fee applications. Detractors generally believed that compliance with the guidelines would be onerous, that some of the guidelines created ethical concerns for professionals, that the guidelines may exceed in some respects the authority of the U.S. Trustee’s office, and that the burden imposed by the guidelines outweighed any benefit they may offer.

Bankruptcy lawyers in general tend to feel that the participation of the U.S. Trustee, at least in large chapter 11 cases, is unnecessary or counterproductive. This hostility may arise in part from self-interested concerns regarding the U.S. Trustee’s review of fee applications. But beyond that, in major chapter 11 cases, the conflicting interests are typically represented by experienced and sophisticated counsel. The bureaucrat’s voice in these cases does not usually add much value. The U.S. Trustee often seems to recognize this by participating actively in the early days of chapter 11 cases, then backing off — other than in matters regarding the retention and compensation of professionals — once a creditors’ committee is appointed.

Judges, by contrast, often speak well of the U.S. Trustee program. They view the U.S. Trustee as able to help them with some of the most onerous parts of their job — cleaning up the docket, identifying systematic abuses, and, again, policing fees.

BAPCPA imposed a host of new obligations on the U.S. Trustee, including:

- reviewing debtor means test filings and, in appropriate cases, filing either a bad-faith objection or a statement as to why no objection is being filed;48
- supervising audits of debtor filings to determine their accuracy, veracity and completeness;49
- moving for the appointment of a chapter 11 trustee in cases of suspected fraud;50
- certifying credit counseling agencies and otherwise supervising BAPCPA’s credit-counseling

certifying entities to teach debtors how to better manage their finances; and

> overseeing small business chapter 11 reorganizations.

§ 1.14 ~ The Debtor

It may appear that the debtor is the star of the show, but in most bankruptcies, that is not the case. Most cases begin with the individual debtor who files a bankruptcy petition seeking a discharge, and end when he gets it. In most of these cases, there are no assets available to be liquidated by the trustee for distribution to creditors, given that all of the debtor’s assets are either exempt or so heavily encumbered by secured claims that there is nothing to administer. Contrast this with the class of cases where there are some assets worth saving. While these are fewer in number, they absorb a lot more of a lawyer’s time and energy. The debtor may be an active participant in these asset cases, although in most of them it is just a trustee liquidating the assets and the creditors fighting amongst themselves for the proceeds.

The debtor’s role is so limited that some courts have said he does not have standing in an individual chapter 7 case. This is obviously an overstatement: As to an objection to his discharge or in other issues of dischargeability, he may be a necessary party. As to issues involving property of the estate, however, the lack-of-standing argument has more merit. But more-alert courts have qualified this proposition to recognize that the debtor may have a pecuniary interest even in a chapter 7 case. For example, there may be a surplus after the payment of creditors. In such cases, he certainly ought to be heard if he wants to be.

In re Cult Awareness Network Inc. draws an interesting line. The debtor was a nonprofit corporation dedicated to fighting cults. Because of an adverse judgment, it filed for relief under chapter 11, but subsequently converted to chapter 7. The trustee undertook to sell the trade name. The debtor objected to a prospective sale, fearing that the intended buyer would use the name to promote cults. The court concluded that the debtor lacked standing because he had no financial stake, but it added that if he had shown a “reasonable possibility” of a surplus in the estate, then the result might have been different.

51 Id. § 111.
52 Id.
54 151 F.3d 605 (7th Cir. 1998). The purchaser was an individual believed to be associated with the Church of Scientology — “an organization not in complete harmony with the beliefs of the Cult Awareness Network.” Id. at 607.
In a chapter 11 case involving an operating business, the situation is different. There, the debtor does play a central role. First of all, the recovery of other stakeholders will depend (among other things) on how good a job the debtor does in running its business. Contrast that with a chapter 7 liquidation, where creditors’ recoveries will depend on whether there are any assets available to the trustee to liquidate and what price the trustee can get for those assets. Second, the debtor typically orchestrates the negotiations that lead to a chapter 11 plan, or a sale. The Code helps to ensure the debtor’s central role by giving the debtor the exclusive right to propose a plan during the first 120 days of the case.\footnote{See 11 U.S.C. § 1121. The 120-day period may be extended by the bankruptcy court for up to a total of 18 months. The court may also shorten or terminate the exclusive period. See \textit{infra} § 6.16.} This “exclusivity,” and other powers given to a chapter 11 debtor, impel parties to negotiate with the debtor.

It is a lot easier to get something done with the debtor’s support than over its objection. On occasion, one will see a weak debtor that does not step up to play the central role envisioned by the Code. In such a situation, other parties (lenders, creditors’ committee, bondholders, etc.) may negotiate among themselves, reach a deal, and seek to “force” it upon the debtor. But in most operating business chapter 11 cases, the debtor plays a central role.

\section*{§ 1.15 - Professionals: Counsel for the DIP}

Section 327 provides that “the trustee, with the court’s approval, may employ one or more attorneys [and other professionals] to represent or assist the trustee in carrying out the trustee’s duties.” This means, \textit{inter alia}, that the DIP is authorized to retain counsel. Indeed, probably the most important single role in the ordinary chapter 11 is that of the lawyer for the DIP. Usually, he is the one who has been counseling the debtor outside of bankruptcy, and usually he recommended the filing in the first place. Typically, it is he who speaks for the DIP in court. He is often the center of plan negotiations. Also, for good or ill, the judge usually depends on him as if he were a kind of trustee.

This is problematic, however; it can force counsel to make some difficult choices about how to reconcile his obligations as an advocate for his client and his obligations as a representative of the bankruptcy estate and an officer of the court.\footnote{See \textit{infra} §§ 6.17 and 16.14. For the moment, the point to remember is that the DIP is (in some ways) an entity separate from the debtor, with differing duties. Accordingly, insofar as counsel represents the DIP, he does not (only) represent the debtor. It should not surprise you that this distinction is often lost in practice, where the individual debtor (or the business debtor’s management) gives instructions to the DIP’s counsel and is the one who hired that counsel in the first place.}
Counsel for the DIP (and indeed, any professional appointed under § 327(a)) may take his compensation from the estate as an administrative expense, but only with court approval. First, to be employed under § 327(a), the professional must not “hold or represent an interest adverse to the estate” and must be a “disinterested person,” and the employment must be authorized by the court. Thus, if you are going to serve as counsel for the DIP, make sure that you meet the disinterestedness and lack-of-any-adverse-interest requirements, that an employment application is filed, and that you get an approval order. Then, when it is time to get paid, you must file a fee application and get an order approving your fees. In many cases, you will file interim fee applications during the case — so you don’t have to wait until the end of the case to get paid — and then a final fee application at the end of the case. In some cases — particularly larger ones — the court will enter an order at the beginning of the case establishing procedures for the compensation of professionals, which may include monthly compensation for professionals, subject to a hold-back amount.

In addition to the required applications, you will want to make sure the debtor has money to pay you. A starting point is to get a retainer before the bankruptcy case is filed. You need to disclose the amount of the retainer in your employment application. Beyond that, you will want to make sure that either the debtor has unencumbered cash sufficient to pay your fees (as well as the debtor’s other projected fees and expenses) or, if the debtor’s cash is encumbered, the lienholders have agreed to a “carve-out” from their liens to allow you to get paid.

Many judges look to the U.S. Trustee for help on employment applications. Some require that the U.S. Trustee sign off before the application is approved. In many districts, it is a good idea to ask for U.S. Trustee approval on any application for employment before it is filed and to have the approval entered into the record.

But what if you overlook getting your appointment at the beginning and go ahead and do all the work? The answer is not completely bleak. You may be able to get some kind of nunc pro tunc (retroactive approval of the employment) or quantum meruit (payment for the value of services rendered) relief. But it may take some groveling, or at least a lot of explanation as to why you missed the deadline in the first place. And if the judge has any reason at all to not want to see you compensated, this is a great peg to hang his wishes on.

For convenience, we have talked here about attorneys. But note that the provisions of §§ 327 and 330 apply to any “professional person.” Just who qualifies as a professional person may be open to some debate, but the class certainly also includes accountants and investment bankers. When in doubt, seek court authorization before employing someone who may be considered a “professional person.” We’ve seen too many real estate brokers go away empty-handed because nobody informed them that they needed court approval for their employment.

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57 11 U.S.C. § 330. For a more extensive discussion of employment compensation, see Chapter 16, especially § 16.20.
§ 1.16 ~ Note on Petition Preparers

An individual who needs bankruptcy protection is not going to find it cheap; even the basic filing fee likely exceeds the reach of the most exigent debtors, to say nothing of the fee for an attorney. Since the enactment of BAPCPA, this problem has been exacerbated. The added obligations and risks imposed on consumer debtors’ lawyers have increased legal fees in most jurisdictions. Generally, chapter 7 case filings will cost between $1,000 and $2,000, depending on complexity, plus the $335 court filing fee. Chapter 13 fees generally start in the neighborhood of $3,000, plus the $310 court filing fee. Yet, the protections of bankruptcy are surprisingly easy to obtain: The mere filing of a petition (even without supporting schedules) will stop a foreclosure fast in its tracks.

The facts help to explain why, when the Code was young, judges found themselves choked by a deluge of petitions, many of them barely legible and often with no purpose other than to get the protection of the automatic stay. It didn’t take much detective work to grasp that there was a stratum of debtors coming in below the radar with the aid of non-lawyer drafters who took a fee to write (but not to file) the bankruptcy papers.

Judges quickly developed an animosity to these petition preparers, and it is not hard to see why. A lot of their work cluttered up the system. And there is no doubt that the preparers, barely visible and unpolicied, often took money from debtors and then did them no service or even harmed them. Yet the problem of the preparers was more complicated than that. The existence of the preparers made it clear that for plenty of debtors, standard legal services were not available. Moreover, incompetent or irresponsible as some of the preparers might be, the fact was they did seem to provide a service: to get some debtors bargain relief at bargain prices.

As a consequence of these competing concerns, in 1994 Congress adopted § 110 of the Code, which does not outlaw, but does regulate, the preparers. It requires them to sign petitions and disclose their fees. They even run the risk of being disbarred if they violate the rules and, in some cases, being fined or imprisoned. The provision may have limited the abuses of the preparers, but it also provided at least a backhanded acknowledgment that they are there and that they may perform a service for those that are un- or under-served by the bar in general.

§ 1.17 ~ Creditors’ Committees

From the Code’s provisions dealing with committees, you can quickly infer that the drafters anticipated a different sort of chapter 11 than the one that came into being. Section 1102 says that “as soon as practicable after the order for relief ... the United States Trustee shall appoint a committee of creditors holding unsecured claims.” Section 1103(c) sets forth a detailed catalog of committee powers. You would be entirely justified

in concluding that the drafters intended the committee to be a linchpin of the chapter 11 process, policing the
developer and formulating a plan.

Sometimes it works this way. But in most cases, especially smaller ones, either there is no committee at all or
it is substantially moribund — a paper committee only. There are at least two reasons why it works this way.

First, there is a class of cases for which a committee makes no intrinsic sense at all. Take Limited LP, a hypo-
thetical limited partnership with one asset, Blackacre, a medical office building worth $3 million. Limited
owes $5 million to BigBank, the mortgagee. It owes $35,000 to suppliers of goods and services, including the
building management company, the janitorial service, and others. There is little point to assembling a commit-
tee of creditors in a case like this. BigBank will take care of itself. For the unsecured, the amount of money at
issue does not begin to justify the time, effort, and expense of a committee — especially because, practically
speaking, both Limited and BigBank want the unsecured to get paid so they will continue to provide services.

Second, there is another class of cases where the potential role of the committee is more problematic. Con-
sider DebtorCo, a small widget-maker with annual gross revenues of about $2 million a year. DebtorCo owes
FirstBank $800,000 secured by Whiteacre, its factory/office/warehouse. DebtorCo owes $700,000 to FinCo,
an asset-based lender who provides a revolving working capital facility secured by inventory and receivables.
It owes 30 vendors an aggregate of $240,000. The largest vendor claim is for $25,000.

There may be good arguments in favor of assembling a committee of creditors in this case, but the practical
hurdles may be insurmountable. Individual creditors are likely to be unsophisticated, or at least uneducated
in the niceties of chapter 11. They may be demoralized by their past misfortune and unwilling to send good
efforts after bad. On numbers of this size, it may be hard to find a lawyer willing to take the time and effort to
give them good representation. So even if a committee is appointed, it is likely to remain moribund. Indeed,
if the debtor qualifies as a “small business debtor,” then on request of a party in interest, the court may order
that a committee not be appointed.\footnote{See 11 U.S.C. §§ 1102(a)(3), 101(51C), 101(51D), 1116 and 1121(e); see also infra § 5.6 on small business debtors.}

On the other hand, in those cases where the numbers justify it, the committee can play an important role. The
committee may employ counsel (and other professionals).\footnote{11 U.S.C. § 1103(a).} Like DIP counsel, the committee counsel may
be paid as administrative claimants out of assets of the estate, subject to bankruptcy court approval. A well-
organized committee of sophisticated creditors, speaking through a competent counsel, can play a major part
in shaping a case and sometimes even dominate a case.
Consider LittleCo with secured claims of $10 million and unsecured claims of $8 million (total = $18 million) but where assets will never, under the most optimistic forecast, be worth more than $14 million. On these numbers, there will be nothing for equity, so the old owners may choose to throw the keys on the table and walk away. This leaves unsecured creditors as the de facto equity class, with the same motivations as any other junior class. Properly organized and represented, they may be able to act to preserve going-concern values or otherwise do what is necessary to maximize the value of their claims.

Another perhaps increasingly common role for a creditors’ committee is to extract modest value for unsecured creditors where they are out of the money. Say DebtorCo has assets with a value of $40 million in a best-case scenario. All the assets are subject to BigBank’s lien, securing $85 million in debt. The unsecured are owed $10 million, collectively. The company cannot reorganize, so the path is an asset sale. BigBank will act as the stalking-horse bidder, with a credit bid. If another buyer comes along, at a price BigBank finds acceptable, then BigBank will allow itself to be outbid. Otherwise, BigBank will own the assets. In either case, there’s nothing for the unsecured. So what is the creditors’ committee to do?

One answer is the committee will spend some of BigBank’s cash collateral investigating potential claims against BigBank — perhaps for avoidance of its lien, or equitable subordination of its claim. The committee will ask for a bunch of documents and will schedule depositions. The committee may also object to the asset sale, threatening to derail or at least delay it. Probably there’s not much merit to the committee’s arguments. But if it makes enough noise, BigBank may agree to pay $500,000 to make the committee go away, paving the way for a fast, consensual process. Thus, the committee “created” a 5 percent recovery for its constituency. Whether or not this dynamic is a good thing is certainly debatable. But, for better or for worse, it is a common scenario.

Another basic fact about committees is that judges tend to like them. More precisely, in an operating case where there is no trustee, the judge may feel uncomfortable depending solely on the representations of the DIP. The judge may be eager for another voice, either to challenge or confirm what the DIP is telling him. Moreover, lawyers for the committee often find that they have a freer hand than lawyers for the DIP.

This may seem ironic in that the committee lawyer has many “clients” — the whole committee — rather than just one. But for any individual creditor, this case is likely to be only a secondary item. The practical result is that individual creditors will often leave broad discretion to committee counsel and other committee professionals and rely on those professionals for all but the most important business judgments. This framework gives committee counsel, in some ways, the best of both worlds: an important voice in the case without the
enormous administrative responsibilities that come from representing the DIP. In addition, committee members are authorized to receive reimbursement of expenses from the estate.\textsuperscript{61}

Section 1102(b)(3) requires committees to share information with and receive comments from members of their constituency who are not on the committee.\textsuperscript{62} This makes sense as a way to assume that the committee is representing its constituency's interests, but it raises concerns about maintaining privileges and dealing with the sort of confidential and sensitive information to which committees often have access. In some cases, committees have filed motions seeking approval of procedures for complying with these new requirements and protections relating to confidentiality and privilege.

There is also a provision for a committee of creditors in chapter 7,\textsuperscript{63} but such committees are rarely constituted because the cases tend to be smaller and creditors do not have anything to gain from adding another layer of bureaucracy. One important distinction is that the chapter 7 committee is not appointed but elected (just like the equally rare "elected" chapter 7 trustee).

\section*{§ 1.18 ~ Limits on Committee Members}

There is a downside to committee service. The case of Pan Am World Airways provides a telling story. Once the crown jewel of U.S. aviation, Pan Am went into chapter 11 in 1991. Delta Air Lines undertook interim financing and bought some Pan Am routes while negotiating for a broader role. Hoping to keep the airline viable, some unions agreed to concessions. But the deal broke down, and the employees howled betrayal, perceiving that Delta had kept Pan Am alive only long enough to skim off the good assets. Thereupon, the employees sued Delta for $2.5 billion.

By way of defense, Delta sought to implead members of the Pan Am creditors' committee, alleging that the committee displaced the DIP in plan negotiations. In response, committee members asserted that they had immunity from suit.\textsuperscript{64} The judge, conceding that they had limited immunity, nonetheless found that the complaint alleged willful wrongdoing and thereby survived a motion to dismiss.\textsuperscript{65}

\begin{fnsymbollist}
\item On occasion, a committee member will seek to include within these expenses its own legal fees. Section 503(b)(4) appears to prohibit this, absent a finding of "substantial contribution." \textit{See, e.g., In re Lehman Bros. Holdings Inc.}, 508 B.R. 283 (S.D.N.Y. 2014), \textit{motion to certify appeal denied}, No. 13 Civ. 2211 (RJS), 2014 WL 3408574 (S.D.N.Y. June 26, 2014). In \textit{Lehman}, the bankruptcy court approved a plan provision providing for payment of committee members' professional fees and authorized payment of such fees as administrative expenses under § 1129(a)(4) of the Bankruptcy Code. On appeal, the district court reversed and remanded, holding that committee members' professional fees were payable as administrative expenses only if such fees could be shown to qualify under § 503(b)(3)(D). \textit{Id.} at 295-96. For a discussion on committee counsel conflicts and compensation, \textit{see infra} Chapter 16.
\item 11 U.S.C. § 1102(b)(3).
\item \textit{Id.} § 705.
\item \textit{Luedke v. Delta Air Lines Inc.}, 159 B.R. 385 (S.D.N.Y. 1993); \textit{see also In re PWS Holding Corp.}, 228 F.3d 224 (3d Cir. 2000); \textit{Westmoreland Human Opportunities Inc. v. Walsh}, 327 B.R. 561 (W.D. Pa. 2005).
\item 159 B.R. at 395.
\end{fnsymbollist}
Committee members may also be restricted in or barred from claims trading or trading in securities of the debtor. In some cases, courts have approved “ethical screening” mechanisms so that committee member institutions could continue to trade by separating those who serve on the committee (and therefore have access to nonpublic information) from those at the member institution who do the trading.66

§ 1.19 ~ Additional Committees

The court may (but is not required to) appoint additional committees — either of creditors or of equity securityholders.67 The court shall order such additional committees “if necessary to assure adequate representation of creditors or of equity security holders.” After a court order, it is left to the U.S. Trustee in the first instance to appoint such committees.

Additional committees are sufficiently rare that they do not merit extensive commentary here, but the idea of an equity committee does raise an interesting conceptual problem. If a bankruptcy proceeding is “for” creditors, then why is an equity committee necessary at all? Or, if there is a DIP — and if the DIP is looking out for the interests of shareholders — then again, what would the role of the DIP be where there is an equity committee?68

A partial answer is that courts have permitted equity committees in some cases where there are substantial conflicts between shareholders and managers — for example, where shareholders have been trying to oust management either before or in the chapter 11 process. Equity committees have also been appointed where it appears that the estate may be solvent.

Whatever nominal purpose equity committees serve, there is dramatic evidence of their function. In a study of large chapter 11 cases,69 researchers Lynn LoPucki and William Whitford showed a correlation between the existence of an equity committee and enhanced distributions to equity. Of course, if this comes about because equity expands the size of the pie, then everyone should be happy. But if equity gets more by leaving less to others, then the policy is more questionable. There are cases, however, where an equity committee appears to have played a prominent role and may well have changed the case’s outcome.70

66 See infra § 13.51. In addition, ABI’s Creditors’ Committee Manual is worthwhile reading for anyone contemplating service on, or representation of, a creditors’ committee.
68 For further discussion of this topic, see infra § 6.17 and the remainder of this section.
70 Two examples are the Adelphia case in the Southern District of New York and the Merant case in the Northern District of Texas, 336 B.R. 610, 619 (Bankr. S.D.N.Y.), aff’d, 342 B.R. 122 (S.D.N.Y. 2006); and 354 B.R. 113, 119 (Bankr. N.D. Tex. 2006), aff’d, 308 F. App'x 824 (5th Cir. 2009), respectively.
Aside from equity committees, we have seen committees appointed to speak for such various constituencies as subordinated debt-holders, employees, personal-injury plaintiffs, limited partners and retirees. They are perhaps most common where there is a constituency that would benefit (itself and the cases) from collective representation but is not adequately represented by the statutorily mandated unsecured creditors’ committee. However, this benefit needs to be balanced against the cost of additional committees, each of which is likely to hire its own counsel and perhaps other professionals — all at the estate’s expense.

§ 1.20 ~ Committee Membership

The Code provides that a committee of creditors “shall ordinarily consist of the persons, willing to serve, that hold the seven largest claims against the debtor of the kinds represented on such committee.”71 But the Code also allows the U.S. Trustee to carry over a prepetition committee “if such committee was fairly chosen and is representative of the different kinds of claims to be represented.”72 This provision allows creditors to organize and negotiate with the debtor outside of chapter 11, carrying some expectation that they will be able to continue after the petition.

On occasion, a creditor is unhappy with the U.S. Trustee’s decision about who gets appointed to the committee or who does not. The court may order the U.S. Trustee to change the committee’s composition order to ensure adequate representation.73 This is rare, but the remedy is available, if warranted.

71 11 U.S.C. § 1102(b)(1); cf. id. § 1102(b)(2) (seven largest equity security-holders).
72 Id. § 1102(b)(1).
73 Id. § 1102(a)(4).