UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF ILLINOIS
235 U.S. COURTHOUSE
600 EAST MONROE STREET
SPRINGFIELD, ILLINOIS 62701

CHAMBERS OF
MARY P. GORMAN
CHIEF JUDGE

TELEPHONE
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October 30, 2015

To: Chapter 7 Trustees

Re: Procedures for Chapter 7 Cases - Springfield and Urbana Divisions

Clarification appears to be necessary with respect to some of the procedures Chapter 7 Trustees have been asked to follow in administering Chapter 7 cases in the Springfield and Urbana Divisions. This memo is intended to supplement prior correspondence from the Clerk of Court on certain issues and will be posted on the Court's website under the section for my procedures. Your continued assistance in the efficient administration of Chapter 7 cases is greatly appreciated.

1. Rule 2013 and Applications for Compensation

The Clerk of Court is required to maintain a public record of all fees awarded to trustees and to any professionals employed by trustees. Fed. R. Bankr. P. 2013(a). The Clerk is able to meet her obligation only if orders are entered specifically awarding fees to trustees and professionals. The Clerk cannot—and should not—be required to try to pick up this information from references to fees included in sale orders, orders allowing compromises, or other such orders. The Code and Rules are clear that compensation of professionals is awarded upon a proper application and, except in very limited circumstances, a distinct application for compensation must be filed in order for compensation to be awarded and for a trustee to be authorized to pay compensation to himself, herself, or an employed professional. 11 U.S.C. §330(a)(1); Fed. R. Bankr. P. 2016(a).

Notices of Intent to Sell may include, for informational purposes, the details of professional fees and costs expected to be paid from sale proceeds. That information is helpful to parties in interest as they evaluate whether to object to a sale. But including the information in the Notice of Intent or even in the order authorizing the sale to proceed does not mean that an application for compensation is no longer necessary. An application for compensation must be filed unless all of the information regarding requested fees and costs is contained in a report of sale and the report of sale is noticed with a specific request for approval of the compensation. Either way, approval of all compensation paid as part of a sale must be obtained after the sale.

As an aside, you have all previously been notified that it is not necessary to notice reports of sale for approval or obtain orders confirming sales unless you are using the report of sale process to also

obtain approval of compensation. Orders approving compensation contained in reports of sale should be limited to approving the compensation and should not contain language confirming or approving the sale. Orders purporting to confirm or approve a sale will no longer be accepted. Additionally, we have noticed that occasionally a trustee will seek approval of an auctioneer or broker fee under $1000 using the report of sale and then will file a separate application for costs also under $1000. The purpose of using two separate documents may be to avoid having to notice either document to the entire matrix. But when the total compensation including costs proposed to be paid to a professional exceeds $1000, the notice must go to all, and splitting the compensation into two components does not change what is required.

Motions to compromise are brought under Rule 9019 and the relief available through such motions is limited to authorizing a trustee to settle or compromise controversies in which the estate has an interest. Orders entered on motions to compromise should not include language that does anything more than grant authority to a trustee to proceed to finalize the proposed settlement or compromise. Orders submitted on motions to compromise that purport to require a debtor or third party to settle or to take other actions are generally rejected.

Disclosure of fees and costs that may be paid if a settlement or compromise is effectuated is important information, and trustees have been requested to provide such information in all such motions. In the past, we have had motions to compromise filed and approved only to find out that after the payment of fees, costs, medical liens, and the like, no funds were generated to pay unsecured creditors, and the estate was insolvent. Thus, at least an estimate of all such anticipated expenses should be included in all motions to compromise. But the inclusion of information about expected fees and costs in a motion to compromise is not a substitute for the filing of the required application for compensation. Recently, we have held up several final reports because they disclosed payments to professionals for which no order approving compensation had been entered even though orders allowing compromises where the fees were disclosed had been entered.

To be clear, motions to compromise may be combined in a multi-part motion with an application for compensation. This may be done only when the exact amount of fees and costs is known at the time the compromise is presented. **All applications for compensation including those combined with motions to compromise must contain a complete and detailed itemization of costs**. And any order entered on the multi-part motion must specifically and separately authorize both the compromise and the compensation.

If a multi-part motion is used, an objection to one part may hold up the entry of an order on the other part, and, accordingly, you may prefer to file a separate application at the same time as the motion to compromise to avoid having approval of the compromise delayed if there are questions about compensation. **If a multi-part motion is used, it must be captioned, docketed, and noticed as to all parts of the motion. Failure to properly caption, docket, or notice all parts of the motion**

will result in the motion being effective only as to the part, if any, that was captioned, docketed, and noticed properly. This is the same procedure used to process all multi-part motions. Information about docketing multi-part motions is available on our website and should be consulted if you or your staff are unfamiliar with the process.

All costs included in applications for compensation for trustees or other professionals must be itemized. Only costs that are directly related to the case and are not of the type generally included in overhead will be allowed. Costs for copying and mailing motions and notices served on the entire matrix are allowed. The cost of a sheet or two of paper and one stamp for sending a letter would not be allowed because it is overhead. All copying and postage expenses should be specifically identified as relating to particular motions or matters. Claims for such expenses without identifying what was copied and mailed will not be allowed. Mileage within the city where a trustee's or professional's office is located will not be allowed. Mileage to other cities for hearings, sales, and the like will generally be allowed, but when multiple hearings in different cases are attended at the same location on a particular day, an estate should only be charged for its fractional share of the mileage involved. That is true even if some of the cases/estates for which hearings were held do not have assets to cover a share of those costs. Mileage to attend regularly scheduled creditors' meetings is overhead for trustees and does not become a cost chargeable to a particular estate after assets are discovered.

Some serious self-policing is required in this area and all professionals employed should be advised of these guidelines. Because most trustees seek approval of their compensation with their final reports, including questionable or insufficiently detailed costs in those reports is not advised as a denial of some of the costs may result in the final report having to be amended and re-noticed.

2. Contingency Fees

Over the last several years, trustees have frequently requested to employ themselves and their own firms on a contingency fee basis rather than on an hourly basis. Applications to employ for purposes of collecting accounts receivable, preferences, and fraudulent conveyances on a contingency fee basis have routinely been allowed. Employment for those types of legal matters on a contingency basis is consistent with the professional and ethical guidelines that allow contingency fee representation. More recently, however, trustees are seeking to be employed on a contingency basis to obtain turnover of estate assets from debtors and to prosecute lien avoidance actions. Neither of these types of legal matters lends itself to contingency fee representation. In some of these cases, applications to employ have been denied or granted only in part. In other cases, the applications to employ may have been granted but may need to be reconsidered as improvidently granted. 11 U.S.C. §328(a).

With respect to actions against debtors for turnover of property of the estate, a contingent fee may be improper because a significant amount of the initial work required to determine what is property

of the estate and what should be turned over is trustee work not subject to additional compensation. And if a debtor takes property of the estate and refuses to turn it over, an action objecting to discharge may be—and frequently is—filed along with the action for turnover. Legal work on the objection to discharge is compensable only on an hourly basis, so it becomes difficult to sort out what is covered by the contingency fee and what should be paid on an hourly basis. Paying for all legal work on an hourly rate in related actions assures that attorneys are adequately compensated but also prevents a double payment that might occur otherwise. Employment applications providing for a contingency fee to prosecute an action against the debtor will not be routinely allowed. To the extent that a particular circumstance suggests that a contingency fee would be appropriate for a turnover action, those circumstances should specifically be set forth in the application to employ and not lumped together with a general request to be employed on a contingency basis for third party actions.

Also problematic are requests to be employed on a contingency basis to pursue lien avoidance actions. In many cases, lien avoidance actions are based on allegedly faulty documents or defective perfection of the claimed lien. In either case, if a trustee prevails, it is usually because the court has found that no valid, enforceable lien exists. If there is no lien, then it is difficult to calculate the value of that nonexistent lien to compute a contingency fee. Frequently, the court will not have made any finding as to the purported value of the lien as part of the avoidance action, and there would be no reason to spend the time and resources necessary to try to value the lien after avoidance solely to establish a trustee's contingency fee.

Perhaps most troubling is the more recent practice of some trustees asking to be employed on a contingency basis to file avoidance actions where the liens in question are not even remotely sustainable. In some cases, debtors may say in their paperwork or at a first meeting that they told someone that he or she could have a lien on an asset of the debtor, but there is little or no paperwork to support the lien, the lien is not recorded anywhere, and the alleged lien holder has not appeared or filed anything in the case to enforce the lien. Over the years, some trustees have just ignored the possibility that a lien might be claimed under such circumstances. Others have filed avoidance actions for a minimal fee because of the obvious inability of such putative lien holders to make a case. Recently, however, trustees have filed lien actions for these types of cases and asked to be employed on a contingency fee basis for doing so. But again, if there is no lien, there is no value against which the contingency fee can be computed. And under these circumstances where the lien claim does not have even colorable validity, attempting to charge a significant fee for avoidance is not reasonable and is, therefore, not ethical.

As with requests for costs discussed above, some serious self-policing is needed here. Employment on a contingency basis is a valid way to hire counsel and to balance the risk of no recovery with the expenses of litigation. But when you are hiring yourself or your firm, you must be reasonable and consider what you would agree to pay if you were prohibited from hiring yourself and were hiring

unrelated outside counsel instead. Most of you would not pay thousands of dollars to an outside attorney to avoid a lien on a vehicle when you can see that the vehicle's title is clean from the Secretary of State's office's public records and the purported lien holder has made no claim.

As with the matters discussed above involving turnover of assets by debtors, if you think the facts of a particular case support a contingency fee for a lien avoidance action, you may request to be hired on that basis. But the request should be explained in detail in the application and not lumped with a more general request to be hired on a contingency basis to pursue third party actions.

3. Sales and Compromises by Chapter 7 Debtors

When a Chapter 7 case is filed, virtually all property of the debtor becomes property of the estate and, unless and until abandoned, is subject to administration by the Chapter 7 trustee. Debtors who ignore this fundamental premise find themselves in trouble and often are denied a discharge. Nevertheless, some trustees continue to ask that debtors be compelled to turn over proceeds after they settle their own personal injury case or sell their own house. Likewise, trustees often ask that debtors be directed to cash in insurance policies or continue to collect annuity or structured settlement payments for the benefit of the estate. Such requests that imply that a debtor retains control of assets of the estate are not proper and are frequently denied.

Trustees must take control of estate assets. Suggesting that a debtor can or should administer estate assets creates confusion and may put estate assets at risk. If there is a reason that a trustee does not want to take possession and control of an asset such as environmental contamination of real estate, the asset should be abandoned. Otherwise, trustees should take possession and control of estate assets to the extent allowed and should accept responsibility for the administration of such assets for the benefit of the estate and its creditors.

4. Stern v. Marshall

In *Stern v. Marshall*, 131 S. Ct. 2594 (2011), the Supreme Court held that bankruptcy courts lack constitutional authority to enter final judgments and orders in certain cases. *Stern* does not raise questions of subject matter jurisdiction. In any particular case or proceeding, a bankruptcy court either has subject matter jurisdiction or it does not and if it does not, it cannot proceed. 28 U.S.C. §1334(b); 28 U.S.C. §157(b)(1). But even when a bankruptcy court has subject matter jurisdiction, it may not have constitutional authority to enter a final order. In *Wellness International Network, Ltd. v. Sharif*, 135 S. Ct. 1932 (2015), however, the Supreme Court held that parties may consent to final adjudication of a matter by a bankruptcy court otherwise lacking the constitutional authority provided by Article III and that such consent must be knowing and voluntary but may be implied.

All trustees should acquaint themselves with the *Stern* and *Wellness* decisions as the implications of these cases on actions to collect estate assets are significant. *Stern* issues are generally implicated when actions are filed against non-debtor parties for causes of action that arise under non-bankruptcy law and would exist regardless of the bankruptcy filing. Actions to collect accounts receivable or to recover fraudulent conveyances are examples of actions frequently filed by trustees where *Stern* issues must be considered.

Attached are excerpts from the a recent meeting of the Advisory Committee on Bankruptcy Rules regarding certain proposed amendments to the Rules to address issues raised by *Stern* and *Wellness*. Although the information is about proposed but not yet adopted Rule amendments, it may provide some guidance on what should be included in complaints, motions for default judgments, and other documents to address these important issues.