

Role of the United States Trustee in Supervising Bankruptcy Auctions



Many administrative aspects of bankruptcy cases are supervised by federal employees working for the Office of the United States Trustee. For example, local U.S. Trustees review requests to hire professionals (including auctioneers) and review applications for compensation filed by auctioneers and other professionals. The U.S. Trustee is not an employee of the bankruptcy court, but has the right to appear in court and to be heard on almost any issue relating to the administration of a bankruptcy case. In chapter 7 liquidation cases, the U.S. Trustee appoints the trustee in charge of collecting the debtor's assets and supervises the performance of the trustee. What are some of the specific U.S. Trustee responsibilities that relate to auction sales?

Nicholas Kajon, a bankruptcy attorney in NYC, says: "Initially, the U.S. Trustee needs to be satisfied that the auctioneer is independent and has no conflicts of interest. The review includes a review of the affidavit filed by the auctioneer in support of the proposed retention, and follow up if there are any questions. The U.S. Trustee may also review the auctioneer's qualifications and will certainly review the proposed commission schedule and expense reimbursement provisions to make sure the commissions conform to the standard schedules or there is a good reason for any departure."

After the auction is held and concluded, the auctioneer may be required to file a report of sale. This is needed by the chapter 7 trustee or by the debtor in order to properly account for the property which was sold. The auctioneer's report includes an explanation of the auctioneer's costs and expenses, as well as a calculation of commissions. If the U.S. Trustee does not object to the report, a court order may be entered approving payment of the expenses and commissions.

An important concern of the U.S. Trustee is that auctions be run fairly and honestly, since the integrity of the judicial sale process is paramount. For example, an auctioneer cannot bid for property that it has been hired to auction, and to do so is a violation of the federal criminal laws. The U.S. Trustee has the power to bring a civil complaint or to refer the matter to the United States Attorney for investigation and criminal prosecution. If there is fraud or collusion among the bidders at the auction, the U.S. Trustee may conduct an investigation and has the right to take action to enforce the provisions of the Bankruptcy Code that prohibit collusion.

Mr. Kajon suggested that auctioneers and bankruptcy trustees should read the Handbook for Chapter 7 Trustees prepared by the Office of the United States Trustee. The Handbook is the working manual for chapter 7 bankruptcy trustees, and covers topics including general rules for the sale of assets, tax aspects of sales and sales free and clear of liens. Different judicial districts also have specific local rules controlling how bankruptcy sales are conducted.

The Handbook suggests that the trustee should not sell or auction assets unless the value at auction is likely to exceed the amount of the liens and secured claims. In some cases, the auctioneer may be called upon to do a "back of the envelope" appraisal to assist the trustee in determining whether assets should be sold. The trustee must also consider whether the costs of the sale will be so high that the sale will bring no benefit to the estate or to unsecured creditors, in which case the trustee may consider abandoning the asset to the creditors holding liens, which will then be responsible for selling the assets.

Sometimes the trustee and the secured creditors having a security interest in other property cooperate in having a joint auction, particularly if a joint auction is likely to attract more bidders. For example, a secured creditor could have a security interest in machinery and equipment, but not have a security interest in the real property on which it is located, in which case a joint sale may generate a higher price than if the equipment was sold separately and the bidders had the expense of removal. In these situations there should be a written agreement with the auctioneer and the other parties covering subjects such as the allocation of sale proceeds, allocation of expenses of sale and the responsibility of the different sellers for the auctioneer's commissions. Of course, these agreements should be disclosed to the U.S. Trustee and approved by the bankruptcy court for them to be enforceable against the chapter 7 trustee or other seller.

The Handbook gives as an example the situation where the trustee can obtain a higher price from an aggregate sale of assets than from selling the assets individually. In determining whether the sale of secured property is appropriate, the trustee must consider possible adverse tax consequences and the sale's effect on the trustee's ability to fully administer the assets (i.e. reduce all assets to cash), make a distribution of the cash, and close the case.



When working with the chapter 7 trustee, the Handbook indicates that the trustee and the auctioneer should sell assets for cash, except in special circumstances. Valuation of the assets of a bankrupt company can be difficult, particularly assets that involve a future income stream. The auctioneer with the ability to provide appraisal services can help the trustee perform his or her duties. For example, if the bankrupt company is entitled to a future income stream of royalty payments, the trustee should attempt to determine the present value of the income stream and should then sell that income stream for a cash payment as expeditiously as possible. There are also specialized companies that value income streams from intellectual property using their own proprietary data bases. The auctioneer plays an important role in bankruptcy auctions by finding buyers able to pay a fair price for intangible assets that generate future income.

If the fairness of proposed auction procedures is challenged, or the results of the auction are challenged by the unsuccessful bidders, then these issues may be raised before the bankruptcy court. The U.S. Trustee can appear in court and be heard on any of the issues, although the bankruptcy judge makes the final decision after hearing from all the parties. "While issues over the best way

to sell assets can be fought over in court, the better practice is to keep the U.S. Trustee informed about the sale process and proposed procedures and to be open to suggestions. After all, the U.S. Trustee's office has administered thousands of auctions and undoubtedly has insights from other experiences," says Attorney Kajon. It is quicker, easier and less expensive to discuss and resolve issues in advance of litigation.

Ultimately, the integrity of the bankruptcy system, particularly in chapter 7 liquidation cases, depends on the auctioneer, who is counted on to organize and market the bankrupt's property and to get the best possible price. The auctioneer is also asked to be alert to collusive bidding, and to be available to testify before the bankruptcy court in support of the fairness of the auction which has been held. Creditor confidence in the bid value attained at public auctions translates into confidence of creditors that they have been treated fairly by the bankruptcy system, even if they are recovering only a small proportion of their claims.

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