How to Effectively Utilize the Subchapter V Trustee to Make Your Subchapter V Case Magical: The Statutory Role of the Subchapter V Trustee, the Subchapter V Trustee as Facilitator/Mediator, and Other Ways to Effectively Utilize the Subchapter V Trustee

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1. Role of the Subchapter V Trustee

On March 27, 2020, the Small Business Reorganization Act of 2019 (as subsequently amended) (the "**SBRA**") was enacted. *See* 11 U.S. C. § 1181 et. seq. ("**Subchapter V**"). It added Subchapter V to Chapter 11 of the Bankruptcy Code to make the long and often winding and expensive road to confirmation of a plan in a small business bankruptcy case faster, cheaper, and easier. To be eligible to file a small business bankruptcy, a debtor must meet the following tests: (1) the debtor must be a person (individual, partnership, corporation) that is not subject to the reporting requirements of section 13 or 15(d) of the Securities Exchange Act of 1934 or an affiliate of a corporation described above[1], (2) the debtor must be engaged in commercial or business activities as of the filing, (3) the debtor must have total noncontingent liquidated secured and unsecured debts as of the filing of not more than $7.5 million (excluding any debt owed to affiliates or insiders but including any debts of affiliated debtors), and (4) the debtor's primary business activity cannot be owning single asset real estate. *See* 11 U.S.C. § 1182(1). In many ways, a Subchapter V case is no different than a traditional Chapter 11. Unlike traditional Chapter 11s, however, every Subchapter V case comes with a Subchapter V trustee. Each region or district typically has a pool of Subchapter V trustees who are appointed by the Office of the United States Trustee on a case-by-case basis.

Who is the subchapter V trustee? What is his or her role? Is the trustee a friend or a foe? The Subchapter V trustee is a fiduciary for the estate. Absent expansion of the trustee's role upon an order of the court, the debtor remains in possession and the trustee's duties are largely

[1] Section 1182(1)(B)(iii) was amended by the Bankruptcy Threshold Adjustment and Technical Corrections Act (enacted April 7, 2022). The previous version of the statute made any debtor that was an affiliate of an issuer as defined in section 3 of the Securities Exchange Act of 1934 (15 U.S.C. 78c) ineligible for relief under Subchapter V.

supervisory in nature. In every case, the trustee is required to perform the statutory duties enumerated in § 1183(b)(1), (3), (4), (6), and (7). Section 1183(b)(1) incorporates by reference certain chapter 7 trustee duties as specified in § 704(a)(2), (5), (6), and (7), and (9). It requires the trustee to:

- Be accountable for all property received [§ 704(a)(2)].
- If a purpose would be served, examine proofs of claims and object to the allowance of any claim that is improper [§ 704(a)(5)].
- If advisable, oppose the discharge of the debtor [§ 704(a)(6)].
- Unless the court orders otherwise, furnish such information concerning the estate and the estate's administration as is requested by a party in interest [§ 704(a)(7)].
- Make a final report and file a final account of the administration of the estate with the United States Trustee and the court [§ 704(a)(9)].

In every case, the Subchapter V trustee is required to appear and be heard at the status conference conducted under § 1188 and at any hearing that concerns the value of property subject to a lien, confirmation of a plan, modification of a plan after confirmation, or the sale of property of the estate. § 1183(b)(3). In cases involving domestic support obligations, the trustee is required to provide written notice to the holder of the claim in accordance with § 704(c). § 1183(b)(6). Unlike any other chapter of the Bankruptcy Code, in every Subchapter V case, the trustee is required to facilitate the development of a consensual plan of reorganization and to ensure that the debtor commences making timey payments required by any confirmed plan. § 1183(b)(7), (4), respectively.

The U.S. Department of Justice, Executive Office for United States Trustees has published a *Handbook for Small Business Chapter 11 Subchapter V Trustees*, which describes additional duties that the trustee is expected to perform in each Subchapter V case (as necessary and appropriate):

- Review initial case filings to determine whether the trustee has any connection to any parties in the case or conflicts; communicate any issues to the United States Trustee; in the absence of a conflict, prepare and transmit to the United States Trustee for filing with the court a written verification establishing the trustee's disinterestedness.

- Review the docket and case file (petition, creditor matrix, schedules, and statement of financial affairs, first day pleadings, debtor's 1116 statement and accompanying financial documents (i.e. balance sheet, statement of operations, cash-flow statement, and tax returns)).

- Review the debtor's books and records.

- Meet with the debtor and counsel.

- Attend the initial debtor interview.

- Review the monthly operating reports.

- Analyze the debtor's eligibility for relief under Subchapter V.

- Attend the § 341 meeting of creditors (and examine the debtor as appropriate).

- Review the debtor's pre-status conference report.

- Analyze the debtor's claim of exemptions; communicate any concerns to the debtor; object (as appropriate).

- Review and analyze the plan; communicate any concerns to the debtor; object (as appropriate).

- Review and analyze other pleadings filed by the debtor, creditors, the United States Trustee, and other parties in interest; communicate any concerns; take positions as appropriate.

- Facilitate resolution of contested matters and adversary proceedings.

- File a final report and account of the trustee's administration of the estate.

- Refer suspected violations of criminal law (i.e. bankruptcy crimes, bank fraud, mail fraud, wire fraud, and tax fraud) to the appropriate United States Attorney.

- Report to the United States Trustee the loss or potential loss of personally identifiable information.

- Follow certain banking and accounting practices to protect monies of the estate in the trustee'spossession in accordance with the provisions of § 345.

- Obtain and maintain an appropriate trustee bond for each case administered as required under § 322.

- Submit monthly and annual reports to the United States Trustee.

- Maintain and preserve adequate records for the cases administered.

U.S. Department of Justice, Executive Office for United States Trustees, *Handbook for Small Business Chapter 11 Subchapter V Trustees*, February 2020 ("**Handbook**"), at Chapter 3. Available at: www.justice.gov/ust/file/subchapterv_trustee_handbook.pdf/download.

The trustee's statutory duties can be expanded by the court without removing the debtor-in-possession upon the request of a party in interest, the trustee, or the United States Trustee. If so ordered by the court, the trustee is required to:

- Investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan [§ 1106(a)(3)].

- File a statement of the investigation once completed, including any fact ascertained pertaining to fraud, dishonesty, incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the debtor, or to a cause of action available to the estate, and transmit a copy or a summary to any creditors' committee, equity security committee, indenture trustee, or such other entity as the court designates [§ 1106(a)(4)].

- File post-confirmation reports as necessary or as ordered by the court. [§ 1106(a)(7)].

If the debtor-in-possession is removed, the trustee's duties can be expanded to include taking possession of property of the estate and operating the debtor's business. § 1183(b)(5). If so ordered by the court, the trustee is required to:

- If the business of the debtor is authorized to be operated, file with the court, with the United States trustee, and with any governmental unit charged with responsibility for collection or determination of any tax arising out of such operation, periodic reports and summaries of the operation of such business, including a statement of receipts and disbursements, and such other information as the United States trustee or the court requires [§704(a)(8)].

- Perform various duties specified in section 704(a), including: (2) be accountable for all property received; (5) examine proofs of claim and object to improper claims; (7) unless

the court orders otherwise, provide information regarding the estate as requested to parties in interest; (8) file reports of operations if the debtor is authorized to be operated (9) make a final report and file a final account of the administration of the estate; (10) provide notice of the debtor's domestic support obligation; (11) administer any employee benefit plan; (12) if debtor is a health care business, take reasonable steps to transfer patients. [§ 1106(a)(1)].

- File the schedules and statements of financial affairs required under § 521(a)(1) if the debtor has not filed them [§ 1106(2)].
- For any year for which the debtor has not filed a tax return required by law, furnish, without personal liability, such information as may be required by the governmental unit with which such tax return was to be filed, in light of the condition of the debtor's books and records and the availability of such information. [§ 1106(a)(6)].

Among the most important subchapter V trustee duties are assessing the financial viability of the small business debtor, facilitating a consensual plan of reorganization, and helping ensure that the debtor files or submits complete and accurate financial reports. *Handbook*, at 1-1.

2. Facilitation Role is Most Important and is Unique

Of all the duties, the Subchapter V trustee's statutory duty to facilitate the development of a consensual plan of reorganization is perhaps the most important role and is unique to Subchapter V. 11 U.S.C. § 1183(b)(7). Section 1183(b)(7) of the Bankruptcy Code provides that a principal duty of the trustee is to facilitate the development of a consensual plan of reorganization. *Handbook*, at 3-9. The Subchapter V trustee appointed in each case is tasked primarily with facilitating a consensual plan. *Handbook*, at 1-2. *See also*, *In re Ozcelebi*, 639 B.R. 365, 381 (Bankr. S.D. Tex. 2022) ("The Subchapter V trustee's primary duty is to "facilitate the development of a consensual plan of reorganization.").

The facilitator role is a role not given to trustees under other chapters of the Bankruptcy Code. "The subchapter V trustee's special duty to 'facilitate the development of a consensual plan of reorganization' appears nowhere else in the Bankruptcy Code and is specific to subchapter V."

Id. *See also, In re 218 Jackson LLC*, 631 B.R. 937, 947 (Bankr. M.D. Fla. 2021) ("The subchapter V trustee is the *only* trustee directed to 'facilitate the development of a consensual plan of reorganization'. This duty is assigned to no other trustee in bankruptcy. This distinction is significant.")

"The subchapter V trustee, tasked primarily with facilitating consensual plans, occupies a unique position as contrasted with its counterparts in traditional chapter 11 and other cases, who tend to be adversarial to the debtor by virtue of their duties to protect the bankruptcy estate and its creditors." *Ozcelebi*, 639 B.R. at 381. "Traditionally, trustees tend to be adversarial to the debtor as a result of their duties in protecting the estate and creditors." *218 Jackson LLC*, 631 B.R. at 947. "Chapter 7 trustees take possession of the estate's property and dispose of or administer those assets in order to pay creditors." *Id.* *See also*, *Ozcelebi*, 639 B.R. at 381 ("Chapter 7 trustees marshal and administer estate assets to pay creditors"). "This role typically puts a trustee in conflict with the debtor and sometimes creditors." *218 Jackson*, 631 B.R. at 947. "A chapter 11 trustee, if one is appointed, similarly takes possession of estate assets for the purpose of liquidation, sale, or less frequently, a reorganization." *Id.* *See also*, *Ozcelebi*, 639 B.R. at 381 ("Chapter 11 trustees take possession of estate assets and facilitate either a liquidation or a reorganization"). "A chapter 13 trustee similarly is gathering assets, but in the form of plan payments in order to distribute to creditors." *218 Jackson*, 631 B.R. at 947. *See also*, *Ozcelebi*, 639 B.R. at 381 ("Chapter 13 trustees gather assets in the form of plan payments for distribution to creditors"). "A chapter 12 trustee is perhaps the most similar here—not taking possession of estate property and occupying a similar oversight role." *218 Jackson*, 631 B.R. at 947. *See also*, *Ozcelebi*, 639 B.R. at 381 ("Chapter 12 trustees are perhaps the closest to subchapter V trustees because they occupy a similar role as overseer without taking possession of estate property unless directed to do so in

the administration of a confirmed chapter 12 plan of reorganization."). "But even a chapter 12 trustee is not charged with *facilitation* of a consensual plan." *218 Jackson*, 631 B.R. at 947.

The Subchapter V trustee's role was intentionally designed to be less adversarial. *Id.* Facilitation of a consensual plan requires the Subchapter V trustee to work with the parties—the creditors and debtor—to agree on a plan. *Id.* "The definition of facilitate is to 'make the occurrence of (something) easier; to render less difficult.'" *Id.* (*quoting Black's Law Dictionary* 734 (11th Ed. 2019). As a result, the Subchapter V trustee acts more like a mediator than an adversary. *Id.* (*quoting In re Seven Stars on the Hudson Corp.*, 618 B.R. 333, 346 n.81 (Bankr. S.D. Fla. 2020)("A substantial part of the Subchapter V trustee's pre-confirmation role, therefore, should be to serve as a de facto mediator between the debtor and its creditors.").

In performing this role, the Handbook provides the following guidance to Subchapter V trustees. As soon as possible, the trustee should begin discussions with the debtor and principal creditors about the plan the debtor will propose, and encourage communication between all parties in interest as the plan is developed. *Handbook*, at 3-4, 3-9. "The trustee should be proactive in communicating with the debtor and debtor's counsel and with creditors, and in promoting and facilitating plan negotiations." *Handbook*, at 3-9 "Depending upon the circumstances, the trustee also may participate in the plan negotiations between the debtor and creditors and should carefully review the plan and any plan amendments that are filed." *Id.*

3. Always Disinterested, Sometimes Neutral

Under § 1183, where there is no standing Subchapter V trustee, the United States Trustee is directed to appoint a disinterested person to serve as trustee in the case. § 1183(a). A "disinterested person" is a person (not necessarily an individual) who is not a creditor, equity security holder, insider, officer, employee or other stakeholder in the debtor, and does not have an

interest materially adverse to the estate or any class of creditors or equity security holders. 11 U.S.C. § 101(14). In essence, the Subchapter V trustee must not have any pecuniary interest in the outcome of the case, or any conflicts of interest that might impair the trustee's ability to carry out his or her duties. *Handbook*, at 2-2. Prior to appointment in a case, the Subchapter V trustee is required to prepare and submit to the United States Trustee a verified statement of disinterestedness. *Id.* at 2-3. As a result, the trustee begins the appointment as disinterested and is required to notify the United States Trustee of any circumstances that develop during the course of the case that impair the trustee's disinterestedness.

Does the disinterestedness requirement also require the trustee to be neutral at all times? Black's Law Dictionary defines "neutral" as "not supporting any of the people or groups involved in an argument or disagreement; indifferent to the outcome of a dispute; refraining from taking sides in a dispute; impartial; unbiased." NEUTRAL, *Black's Law Dictionary* (11th ed. 2019). The trustee is an independent third party who must be fair and impartial to all parties in the case. Handbook, at 2-2. From this standpoint, the Subchapter V trustee appears uniquely positioned to serve as an impartial actor to facilitate not only a consensual confirmation but perhaps also resolution of other contested matters and adversary proceedings.

However, the trustee is also party in interest in the case, with standing to take positions on a myriad of issues including, without limitation, eligibility for Subchapter V relief, use of cash collateral, payment of prepetition wages, payment of affiliate officer salaries, maintenance of prepetition bank accounts, employment of professionals, exemptions, stay relief, assumption and rejection of leases and contacts, asset sales, plan confirmation, objections to claims, conversion, dismissal, and other contested matters and adversary proceedings. Taking a position on any one

of the foregoing issues would not impact the trustee's disinterestedness but would terminate the trustee's case-inception neutrality.

While the trustee must always be "disinterested" that does not mean that the trustee must also be neutral at all times for all purposes. So, if a Subchapter V trustee is not necessarily neutral at all times and for all purposes, can the trustee serve as a meditator?

4. Facilitator is De Facto Mediator or Mediator-Like

A facilitator is someone that helps a group of people engage in discussions or work together; one who interacts with parties in negotiations, exchanging information and trying to further the process. FACILITATOR, *Black's Law Dictionary* (11th Ed. 2019). "The term 'facilitator' is often used interchangeably with the term 'mediator. . .'" *Id.* (*quoting* U.S. Office of Personnel Management, Alternative Dispute Resolution: A Resource Guide 8–9 (2001)).

The role of facilitating plan confirmation or other case issues can look like conducting a mediation. Indeed, the trustee's facilitator role has been analogized to that of a mediator. *See* Christopher G. Bradley, *The New Small Business Bankruptcy Game: Strategies for Creditors Under the Small Business Reorganization Act,* 28 Amer. Bankr. Inst. L. Rev. 251, 261 (2020) ("Trustees seem likely to play the role of mediator."); 22 Donald L. Swanson, *SBRA: Frequently Asked Questions and Some Answers,* 38 AMER. BANKR. INST. J. (Nov. 2019) at 8 (the statutory goal of a consensual plan suggests that the trustee also fill a mediation role).

Bankruptcy courts have also described the Subchapter V trustee as a *de facto* mediator or mediator like. In *In re Seven Stars on the Hudson Corp.*, 618 B.R. 333, 346 (Bankr. S.D. Fla. 2020), Judge Grossman described the role as follows:

> A Subchapter V trustee is specifically charged with the duty to "facilitate the development of a consensual plan of reorganization." 11 U.S.C. § 1183(b)(7). This role should include working not only with the debtor, but with creditors as well, to

> facilitate negotiation of a consensual plan. A substantial part of the Subchapter V trustee's pre-confirmation role, therefore, should be to serve as a *de facto* mediator between the debtor and its creditors.

In *In re 218 Jackson LLC*, 631 B.R. 937, 947 (Bankr. M.D. Fla. 2021), Judge Vaughan described the role as follows:

> "Facilitation of a consensual plan requires the subchapter V trustee to work with the parties—the creditors and debtor—to agree on a plan. The definition of facilitate is to "make the occurrence of (something) easier; to render less difficult." Black's Law Dictionary 734 (11th Ed. 2019). As a result, the subchapter V trustee acts more like a mediator than an adversary.

As a practical matter, the trustee's facilitator role naturally matches a mediator's role. "The mediator's role in the settlement is to suggest alternatives, analyze issues, question perceptions, conduct private caucuses, stimulate negotiations between opposing sides, and keep order." M.D. Fla. L.B.R. 9019-2. The trustee's role as facilitator is identical.

In some instances, the trustee fulfills his or her facilitator role by engaging in shuttle diplomacy with respect to contested issues by transmitting settlement offers between counsel via telephone or email communications. In other cases, it is critical for the parties and their counsel to participate in face to face (Zoom or in-person) discussions/negotiations with the trustee with break-out sessions to facilitate the open flow of communication. During these negotiations, the trustee is not simply a message carrier. The trustee is actively analyzing issues, questioning perceptions, conducting private caucuses, stimulating negotiations between opposing sides, suggesting alternatives, and keeping order amongst the parties and counsel.

The author serves as a Subchapter V trustee in the Middle District of Florida for cases filed in Tampa and Fort Myers, and has been appointed in approximately 60 cases. In some cases, the court has ordered the parties and their counsel to participate in "meet and confer" or "mediation" sessions with the author, in her capacity as a Subchapter V trustee. *See e.g., In re Joseph Robert Verna and Karen Elizabeth Verna*, Case No. 2:22-bk-00021-FMD (M.D. Fla. 4/27/22) (Doc. No.

87) directing the parties to participate in zoom mediation with the Subchapter V trustee. In other cases, no formal order has been entered, but the court has orally directed the parties to participate in "meet and confer" sessions with the trustee.

5. Not a Mediator

But the Subchapter V trustee cannot, in the traditional sense, be a mediator. Mediators, by longstanding practice and by codification in almost all jurisdictions, are not involved in the underlying case. Mediators typically sign, and require the parties to sign, confidentiality agreements. Mediators are also subject to strict limitations on disclosures pursuant to professional and ethical standards. Thus, they are required to maintain the parties' confidences. Once the mediation is concluded, mediators do not touch the case again; they do not show up in court at a subsequent hearing following an unsuccessful mediation and participate as a party in interest.

Mediation is "a method of nonbinding dispute resolution involving a neutral third party who tries to help the disputing parties reach a mutually agreeable solution." MEDIATION, *Black's Law Dictionary* (11th ed. 2019). It is an opportunity for the parties to negotiate a mutually acceptable, but equally painful settlement consistent with the mediation policy of self-determination. "Mediation is a confidential process that includes a supervised settlement conference presided over by an impartial, neutral mediator to promote conciliation, compromise and the ultimate settlement of a civil action." *Id. See also, Florida Rules for Certified & Court Appointed Mediators* ("**Florida Mediation Rules**"), Rule 10.210 (August 2021) ("Mediation is a process whereby a neutral and impartial third person acts to encourage and facilitate the resolution of a dispute without prescribing what it should be. It is an informal and non-adversarial process intended to help disputing parties reach a mutually acceptable agreement.")

A mediator is "a neutral person who tries to help disputing parties reach an agreement. MEDIATOR, *Black's Law Dictionary* (11th ed. 2019). "The role of the mediator is to reduce obstacles to communication, assist in the identification of issues and exploration of alternatives, and otherwise facilitate voluntary agreements resolving the dispute." *Florida Mediation Rules*, Rule 10.220. *See also*, M.D. Fla. L.B.R. 9019-2 ("The mediator's role in the settlement is to suggest alternatives, analyze issues, question perceptions, conduct private caucuses, stimulate negotiations between opposing sides, and keep order."). "The mediator should not opine or rule upon questions of fact or law, or render any final decision in the case." *Id.* Indeed, the ultimate decision-making authority rests with the parties. *Florida Mediation Rules*, Rule 10.220. At the conclusion of mediation, the mediator is required to report to the court (1) the identity of the parties in attendance at the mediation, and (2) that parties either reached an agreement in whole or in part or that the mediation was terminated without the parties' coming to an agreement. M.D. Fla. L.B.R. 9019-2(a).

In most jurisdictions, mediators are governed by standards of professional conduct. *See e.g., Florida Mediation Rules*, Part II. *See also,* M.D. Fla. L.B.R. 9019-2(d) ("All mediators who mediate in cases pending in this District, whether or not certified under the rules adopted by the Supreme Court of Florida, shall be governed by standards of professional conduct and ethical rules adopted by the Supreme Court of Florida for circuit court mediators."). Typically, this prevents the mediator from disclosing, outside the context of mediation, any oral or written communications made during mediation or in furtherance of mediation. *See e.g.,* M.D. Fla. L.B.R. 9019-2(g)(2) ("Except as provided in this section (g), all Mediation Communications are confidential, and the mediator and the Mediation Participants shall not disclose outside of the mediation any Mediation Communication, and no person may introduce in any Subsequent Proceeding evidence pertaining

to any aspect of the mediation effort."). In addition, communications made during mediation are generally privileged and not admissible in evidence in a subsequent proceeding. *See e.g.,* M.D. Fla. L.B.R. 9019-2(g)(3) ("Without limiting subsection (2), Rule 408 of the Federal Rules of Evidence and any applicable federal or state statute, rule, common law, or judicial precedent relating to the privileged nature of settlement discussions or mediations apply.).

While the trustee is not able to rule or render decisions in the context of mediation, the trustee is an estate fiduciary and a party in interest in the case. The trustee can be called upon by the court to express a position on sales of assets, confirmation of a plan, or other matters that come before the court. In such a case, the trustee may be required to make disclosure with respect to matters learned during the course of "mediation" even if the parties requested or directed the trustee to maintain confidentiality. This would undoubtedly place the trustee into a conflict position. That begs the question—can the parties waive the conflict?

Rule 10.340(a) of the *Florida Mediation Rules* provides that "[a] mediator shall not mediate a matter that presents a clear or undisclosed conflict of interest. A conflict of interest arises when any relationship between the mediator and the mediation participants or the subject matter of the dispute compromises or appears to compromise the mediator's impartiality." *Florida Mediation Rules*, Rule 10.340(a). A mediator may serve following appropriate disclosure of a conflict so long as: (1) all parties agree, and (2) the conflict does not clearly impair the mediator's impartiality. *Florida Mediation Rules*, Rule 10.340(c). If the conflict clearly impairs the mediator's impartiality, the mediator is required to withdraw. *Id.* The result under the local bankruptcy rules in the Middle District of Florida is the same. *See* M.D. Fla. L.R. 9019-2(c)(2) ("The parties may waive a mediator's actual or potential conflict of interest, provided that the mediator concludes in good faith that the mediator's impartiality will not be compromised. The

unique nature of bankruptcy cases favors the parties' ability to waive conflicts and supersedes the concept of nonwaivable conflicts.").

There will always be potential for conflict between the trustee's "mediator" role and its party in interest status. This is likely a conflict that clearly impairs the trustee's impartiality preventing the trustee from serving as a true mediator.

6. Encouraging Candid Communications with the Trustee

There are two concerns expressed by practitioners with respect to communications with the trustee: (1) confidentiality (i.e., protection from disclosure in almost all circumstances), and (2) admissibility into evidence under Rule 408 of the Federal Rules of Evidence.

The disclosure issue was discussed in section 5, above. Unfortunately, not every disclosure made to the trustee is protected. Astute bankruptcy practitioners are keenly aware of that fact. Some are refusing to engage in candid communications with the trustee or refusing to utilize the trustee's facilitation services for fear of subsequent disclosure compromising their case. There are certainly instances where the parties need a third-party mediator. But, the key is recognizing those instances and separating the issues for mediation from the issues which can be addressed efficiently and economically by the Subchapter V trustee without compromising the case.

Take this case for example. A creditor files an objection to the debtor's eligibility to proceed in Subchapter V. The debtor really wants to be in Subchapter V, but knows its eligibility case is weak and does not want to spend the time or money litigating the eligibility issue. Debtor's counsel wants to try and negotiate a quick plan to avoid having to litigate the eligibility issue. In order to express the exigency in getting a deal done, debtor's counsel wants the third-party neutral to know just how weak his case is. Obviously, debtor's counsel does not want the third-party neutral to communicate that to creditor's counsel. If the trustee serves as the third-party neutral

with respect to the eligibility issue and learns of weaknesses in the debtor's case, the trustee may be obligated to make subsequent disclosure to the court if the eligibility issue goes to trial and the court prompts the trustee for his or her position. In this case, the parties would be best served by a third-party mediator.

In most cases, however, the trustee is best suited to serve as *de facto* mediator with respect to contested matters and adversary proceedings. Why? The trustee is already up to speed. The trustee knows the parties, their counsel, the case, the financial issues, and the legal issues. In addition, many trustees bill at an hourly rate that is a significant discount off of their market rates. Therefore, utilizing the Subchapter V trustee should save the parties and their counsel substantial time and money.

So, how do you encourage parties to have candid communications with the trustee? Rule 408 of the Federal Rules of Evidence provides that "evidence of the following is not admissible — on behalf of any party — either to prove or disprove the validity or amount of a disputed claim or to impeach by a prior inconsistent statement or a contradiction:

> **(1)** furnishing, promising, or offering — or accepting, promising to accept, or offering to accept — a valuable consideration in compromising or attempting to compromise the claim; and
>
> **(2)** conduct or a statement made during compromise negotiations about the claim — except when offered in a criminal case and when the negotiations related to a claim by a public office in the exercise of its regulatory, investigative, or enforcement authority."

Fed.R.Evid. 408.

The trustee along with the parties and their counsel could agree that all oral and written communications about a particular matter are intended to be confidential settlement communications subject to Rule 408. Specifically, the trustee could have each party and their counsel sign an agreement which provides that statements made and materials used during the course of the settlement negotiations shall not be subject to disclosure in discovery (except for

statements and materials otherwise subject to discovery, which were not prepared specifically for use in the settlement negotiations) or admissible in any judicial or administrative proceeding.

7. Other Ways to Effectively Utilize the Subchapter V Trustee

Having a successful case depends upon several factors, perhaps the most important of which is determining whether the debtor has a viable business worth preserving or whether the owner(s), who have invested their blood, sweat, and tears into the business are simply delaying the inevitable. Whether you are a *pro se* debtor, represent the debtor, are a creditor, or represent a creditor, the Subchapter V trustee can help you analyze whether the dog can hunt. That is, the trustee can aid in determining whether the debtor has a viable business to reorganize, whether the business should be sold as a going concern, or whether the business should liquidate.

Making this determination requires the debtor and its counsel to timely furnish the trustee with financial statements (balance sheet, income statement, cash flow statement, and profit and loss statement), tax returns, accounts receivable aging reports, accounts payable aging reports, inventory turnover reports, etc. A deep dive through the financial history of the company will enable the trustee to help diagnose the problem(s)[2] and discuss potential solutions[3] with the debtor, its counsel, and other constituents.

One of the most significant challenges facing small business debtors is that they lack in-house resources to comply with the financial mandates of the Bankruptcy Code, the Bankruptcy Rules, the United States Trustee's Operating Guidelines, and the local rules, practices, and

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[2] Some of the more common problems plaguing debtors include incompetent or inefficient management; rapid expansion (and often loss of quality control); overleveraging assets (often to support the lifestyle of the principals); failure to shed unprofitable locations, divisions, or products.

[3] Potential solutions include rejecting or renegotiating unprofitable leases and contracts, eliminating products or services with low margins, downsizing or rightsizing the company, restructuring secured indebtedness, selling excess inventory or other assets, obtaining debtor in possession or exit financing, and selling the company as a going concern.

procedures of the bankruptcy court. Often, debtor's counsel is forced to assist the debtor with preparing an initial two-week cash collateral budget, a 13-week cash flow forecast, weekly budget to actual cash collateral reports, monthly operating reports, plan projections, a liquidation analysis, and a schedule of plan distributions. In other instances, the debtor prepares these items, only for debtor's counsel to have to painstakingly review and attempt to correct errors. Even where debtor's counsel is equipped to assist the debtor with these tasks, doing so distracts debtor's counsel from its primary responsibilities.

Although it is <u>not</u> the role of the Subchapter V trustee to <u>prepare</u> financial projections or reports that are the obligation of the debtor in possession, the trustee can provide valuable input regarding both the substance and the presentation of the reports. The trustee can provide insight to the debtor to ensure that all bankruptcy reporting is on a cash basis and that the formatting is consistent with the expectations of the court and local practice. The trustee can also review the initial two-week cash collateral budget with the debtor to ensure that it contains only those expenses that the debtor must pay in the first two weeks of the case (i.e. payroll, utilities, insurance, inventory). The trustee can provide valuable input regarding the terms of a proposed plan, and assist in plan negotiations with creditors. The trustee can analyze the plan projections in comparison to historical financial statements and bankruptcy case reporting (i.e. cash collateral reports, and monthly operating reports) and be a valuable resource in the feasibility analysis for confirmation. The trustee can review the liquidation analysis be a valuable resource in the analyzing the best interest of creditors test and facilitating resolution of valuation disputes .

The trustee can also facilitate resolution of a myriad of other contested matters and adversary proceedings including, without limitation, eligibility objections, stay relief/adequate protection motions, objections to claims, objections to confirmation, as well as adversary

proceedings seeking an injunction, avoidance and recovery of chapter 5 causes of action, and to deny the debtor's discharge or the dischargeability of a particular debt.

The key to ensuring that you have a magical Subchapter V case is communicating with the Subchapter V trustee early and often, and responding timely to the Subchapter V trustee's requests for documents and information, emails, and telephone calls. Beyond that, here are some suggested best practices to effectively utilize the Subchapter V trustee:

- If you have not heard from the trustee within 24 hours of his or her appointment, reach out to discuss the case and the plan. The trustee is particularly interested in hearing the back story—not the one you put in your case management summary. Who is the debtor? How did it get here? Who are the problem creditors? Who are the allies? What are its primary goals in the case? How can the trustee help you to achieve the goals? Will the plan be filed on time (or early)? What will the plan look like? Are there threshold issues that need to be addressed pre-confirmation?

- To the extent possible, provide the trustee with drafts of the following before filing them with the Court:

    - Motion to use cash collateral and the cash collateral budget;
    - Motion to value property subject to a lien along with the valuation;
    - Motion to sell property of the estate;
    - Plan, the plan projections, and the liquidation analysis,
    - Motion to modify the plan after confirmation; and
    - Any pleading seeking emergency or expedited relief.

- If you cannot provide the trustee with a complete draft of the plan prior to filing, provide a plan term sheet. If you anticipate filing one of the other motions, but are unable to provide a draft to the trustee prior to filing, call or email the trustee to preview the relief being requested.

- Provide the trustee with a case update prior to each hearing.